



Office of the
Comptroller of the Currency
Washington, DC 20219

SMALL BANK

PUBLIC DISCLOSURE

February 18, 2014

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

The First National Bank of Northfield
Charter Number 2073

329 Division Street
Northfield, MN 55057

Office of the Comptroller of the Currency

Campbell Mithun Tower
222 South Ninth Street
Suite 800
Minneapolis, MN 55402-3393

NOTE: This document is an evaluation of this institution's record of meeting the credit needs of its entire community, including low- and moderate-income neighborhoods consistent with safe and sound operation of the institution. This evaluation is not, nor should it be construed as, an assessment of the financial condition of this institution. The rating assigned to this institution does not represent an analysis, conclusion, or opinion of the federal financial supervisory agency concerning the safety and soundness of this financial institution.

INSTITUTION'S CRA RATING: This institution is rated Satisfactory.

- The bank's average loan to deposit ratio is reasonable.
- The bank originates a majority of its loans by number within its assessment area (AA).
- The bank has reasonable penetration of loans to businesses of different sizes.
- The bank has reasonable penetration of loans to individuals of different income levels.

SCOPE OF EXAMINATION

We evaluated The First National Bank of Northfield's (FNB's) Community Reinvestment Act (CRA) performance using small bank procedures. This evaluation entailed a full-scope review of the bank's designated AA. We evaluated quarterly loan-to-deposit ratios to assess the bank's performance over this timeframe. We assessed the bank's lending performance by selecting primary products based on the number and dollar volume of loans originated between January 1, 2012 and December 31, 2013. Based on this analysis, we determined commercial and residential real estate loans are the bank's primary products. We selected a random sample of 20 loans from each primary product type in order to evaluate lending activities within the AA. The following table shows the bank's primary products as determined by loan originations and purchases.

| Loan Originations and Purchases in 2012 and 2013 | | |
|---|--------------------|---------------------|
| <i>Loan Type</i> | <i>Volume by #</i> | <i>Volume by \$</i> |
| Commercial | 27.44% | 55.13% |
| Consumer | 39.96% | 5.32% |
| Real Estate | 24.13% | 30.21% |
| Ag | 8.47% | 9.33% |

DESCRIPTION OF INSTITUTION

FNB is a \$153 million, full-service bank located in Northfield, MN. The community of Northfield is located in Rice County, about 40 miles south of Minneapolis, MN. FNB Northfield is owned by Heywood Bancshares, a one-bank holding company located in Northfield.

The bank offers a wide range of loan and deposit products, which are designed to meet the community's needs. Commercial loan totals as of the December 31, 2013 call report equaled approximately \$50 million (32.67 percent), followed by residential real estate at \$37 million (24.18 percent), agriculture at \$10 million (6.54 percent), and

consumer loans at \$2 million (1.31 percent). The loans total \$100 million, accounting for approximately 65.36 percent of the bank's total assets.

There are no known financial or legal impediments that would affect FNB's ability to meet the credit needs within its communities. The last CRA performance evaluation was conducted as of June 30, 2008 and resulted in a satisfactory rating.

DESCRIPTION OF ASSESSMENT AREA(S)

FNB's AA consists of seven contiguous census tracts (CTs) in northern Rice County. The AA includes the cities of Northfield and Dundas. Two of the CTs in the AA are middle-income while the other five CTs are upper-income. The AA includes the CTs where the bank's two branches in Northfield are located. The bank's AA meets regulatory requirements and does not reflect discrimination. The following table shows demographic information for Rice County AA:

| DEMOGRAPHIC AND ECONOMIC CHARACTERISTICS OF RICE COUNTY AA | |
|---|------------|
| Population | |
| Number of Families | 7,283 |
| Number of Households | 10,342 |
| % of Low-Income Families | 9.20% |
| % of Moderate-Income Families | 11.20% |
| % of Middle-Income Families | 21.20% |
| % of Upper-Income Families | 58.40% |
| Geographies | |
| Number of Census Tracts | 7 |
| % Low-Income Census Tracts | 0 |
| % Moderate-Income Census Tracts | 0 |
| % Middle-Income Census Tracts | 28.57% (2) |
| % Upper-Income Census Tracts | 71.43% (5) |
| <i>Median Family Income (MFI)</i> | |
| 2010 MFI for AA | \$58,135 |
| 2013 FFIEC-Adjusted MFI | \$61,700 |
| Economic Indicators | |
| 2012 Unemployment Rate | 6.40% |
| 2010 Median Housing Value | \$248,142 |
| % of Households Below Poverty Level | 7.50% |

Source: 2010 U.S. Census data with updated information when available

The bank has two full service branches and one stand-alone drive up facility located in Northfield, MN. The main branch is located downtown and the second full-service branch is located on the south side of the city. The bank also services five ATM's all located in Northfield. The ATM's are located at each branch, as well as one each at St.

Olaf College and Carleton College. Deposit-taking ATM's include the downtown branch and the drive-up facility.

Unemployment levels in Rice County are slightly higher than the statewide average. According to the U.S. Bureau of Labor Statistics, the 2012 unemployment rate for Rice County is 6.40 percent, while the state unemployment rate was 5.60 percent for this time period.

There are eleven financial institutions with a presence in FNB's AA as of June 2013, per the FDIC deposit market share report. FNB ranks third in deposit share among those institutions, with Wells Fargo NA, and The State Bank of Faribault ranking first and second, respectively. The bank has \$126 million in deposits in the market for a deposit market share of 13.28 percent.

The local economy of the AA is stable and healthy. Primary industry sectors of the AA are construction, education, retail, and other professional services. Major employers in the area include Carleton College, St. Olaf College, and Malt-O-Meal. As of 2013, the AA had a population of approximately 32,000. Homeownership trends are stable with 70.43 percent of housing in the AA comprised of owner-occupied units. The median housing value is \$248,142 according to the 2010 census.

We contacted a local economic development organization in the AA to discuss the local economy and credit needs of the community. Our community contact stated that the community banks are active in the community and have great relationships with local businesses. However, the contact did discuss the need for lessened lending requirements in order to meet community needs, especially to start-up businesses to help build their equity levels.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

Loan-to-Deposit Ratio

The FNB's loan-to-deposit ratio (LTD) is reasonable given the bank's size, financial condition, and AA credit needs. The bank's quarterly average LTD ratio is 73.43 percent for the 23 quarters since the previous CRA evaluation. The ratio ranged from a high of 81.38 percent during the fourth quarter 2008 and a low of 63.86 percent during the first quarter of 2012. The following table demonstrates FNB's average LTD as compared to two other similarly situated financial institutions. Similarly situated banks are those operating in Rice County with assets ranging from \$150 million to \$250 million.

| Loan-to-deposit Ratio Institution (Headquarters) | Assets as of 12/31/13 (\$000s) | Average LTD Ratio (%) |
|---|-----------------------------------|--------------------------|
| Community Resource Bank (Northfield) | \$237,069 | 82.23% |
| Premier Bank Minnesota (Farmington) | \$172,327 | 74.99% |
| The First National Bank of Northfield (Northfield) | \$152,733 | 73.43% |

Source: Call Report data as of December 31, 2013.

Lending in Assessment Area

The bank originates a majority of its loans inside their AA. Based on a sample of primary product types, FNB originated 68 percent of loans by number within their AA. Although the bank originated a majority of loans by dollar volume outside of its AA, we attributed this to a low volume of large dollar commercial loans which were made outside of the bank's AA. The loan samples were randomly determined from loan originations between January 1, 2012 and December 31, 2013. The following table shows loans originated inside and outside FNB's AA by number and dollar volume:

| Lending in Rice County AA | | | | | | | | | | |
|---------------------------|-----------------|---------------|-----------|---------------|-----------|-------------------------|---------------|-----------------|---------------|------------------|
| Loan Type | Number of Loans | | | | | Dollars of Loans (000s) | | | | |
| | Inside | | Outside | | Total | Inside | | Outside | | Total (\$000) |
| | # | % | # | % | | \$(000) | % | \$(000) | % | |
| Commercial | 13 | 65.00% | 7 | 35.00% | 20 | \$1,737 | 16.00% | \$9,124 | 84.00% | \$10,861 |
| Real Estate | 14 | 70.00% | 6 | 30.00% | 20 | \$1,928 | 63.00% | \$1,109 | 37.00% | \$3,037 |
| Total | 27 | 68.00% | 13 | 32.00% | 40 | \$3,665 | 26.37% | \$10,233 | 73.63% | \$13,898 |

Source: Home mortgage and commercial loan samples.

Lending to Borrowers of Different Incomes and to Businesses of Different Sizes

Borrower Distribution of Loans in the Rice County AA

The distribution of borrowers reflects reasonable penetration among individuals of different income levels given the demographics of the Rice County AA. Our random sample of 20 real estate loans indicated that the percentage of loans to low- and moderate-income individuals is comparable to families in the respective income levels within the AA. The bank's performance in lending to low-income borrowers was below the demographic comparator, however the combined lending to low-and moderate-income borrowers equals the percentage of low- and moderate-income families in the AA. The following table shows loans originated inside their AA by number of loans:

| Borrower Distribution of Residential Real Estate Loans in Rice County AA | | | | | | | | |
|---|------------------|----------------------|------------------|----------------------|------------------|----------------------|------------------|----------------------|
| Borrower Income Level | Low | | Moderate | | Middle | | Upper | |
| Loan Type | % of AA Families | % of Number of Loans | % of AA Families | % of Number of Loans | % of AA Families | % of Number of Loans | % of AA Families | % of Number of Loans |
| Real Estate Loans | 9.20% | 5.00% | 11.20% | 15.00% | 21.20% | 30.00% | 58.40% | 50.00% |

Source: Loan sample; 2010 US Census Data

FNB has reasonable penetration of lending to businesses of different sizes. Our random sample of 20 commercial loans indicated that 75 percent of loans by number and 66.28 percent of loans by dollar amount in the AA were to businesses with revenues of less than \$1 million. This compares to the AA demographic of a 78.64 percent of AA businesses with revenues less than \$1 million. The following table shows the bank's lending performance as compared to the area demographics:

| Borrower Distribution of Loans to Businesses in the (Name of AA) Commercial | | | | |
|--|--------------|--------------|---------------------|-------|
| Business Revenues (or Sales) | ≤\$1,000,000 | >\$1,000,000 | Unavailable/Unknown | Total |
| % of AA Businesses | 78.64% | 3.30% | 18.06% | 100% |
| % of Bank Loans in AA by # | 75.00% | 15.00% | 10.00% | 100% |
| % of Bank Loans in AA by \$ | 66.28% | 32.60% | 1.12% | 100% |

Source: Loan sample; Dunn and Bradstreet Data 2013

Geographic Distribution of Loans

The geographic distribution of loans did not provide a meaningful analysis as the AA consists entirely of middle- and upper-income CTs.

Responses to Complaints

The bank has not received any complaints regarding its CRA performance since the last CRA evaluation dated June 30, 2008.

Fair Lending or Other Illegal Credit Practices Review

Pursuant to 12 C.F.R. 25.28(c), in determining a national bank's (bank) or Federal savings association's (FSA) CRA rating, respectively, the OCC considers evidence of discriminatory or other illegal credit practices in any geography by the bank or FSA, or in any assessment area by an affiliate whose loans have been considered as part of the bank's or FSA's lending performance.

We found no evidence of discriminatory or other illegal credit practices inconsistent with helping to meet community credit needs.