



SMALL BANK

Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

PUBLIC DISCLOSURE

December 03, 2007

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

First National Bank of Bosque County
Charter Number: 13675

P.o. Box 278
Valley Mills, TX 76689

Office of the Comptroller of the Currency

San Antonio North
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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.

Summarize the major factors supporting the institution's rating.

- First National Bank of Bosque County (FNB) demonstrates good lending performance. The bank's loan-to-deposit (LTD) ratio has averaged 60% during the evaluation period and is in line with the local peer bank average of 59%.
- A substantial majority of FNB's loans have been made within its assessment area. Information gathered during this review indicated that 83% of the bank's loans are within its assessment area (AA).
- FNB has demonstrated a willingness to extend loans to individuals of varying incomes and to businesses of different sizes. Lending to low- and moderate-income borrowers is satisfactory and in line with the opportunities to extend credit in the bank's Assessment Areas.
- There have been no complaints with respect to FNB's Community Reinvestment Act (CRA) performance.

SCOPE OF EXAMINATION

We performed a full scope small bank CRA examination. This included an evaluation of the characteristics and appropriateness of the bank's delineated Assessment Areas (AA) and a review of the bank's financial condition and ability to provide credit and other services in its AA's. We evaluated the bank's record of lending in its AA's during the time frame from January 2005 through September 30, 2007. We evaluated the bank's lending for 1-4 residential purchases, and loans to small businesses. We sampled small commercial loans to assess lending to small businesses. The bank had external auditors test its HMDA register for data integrity of Home Mortgage Disclosure Act reports. These HMDA reports were used in our analysis of the bank's lending to different income groups within its AA's.

DESCRIPTION OF INSTITUTION

FNB is a \$93 million community bank headquartered in Valley Mills, Texas, which is 25 miles west of Waco, Texas. FNB has three branch offices located within 20 miles of the main office. One branch is located in Clifton, Texas, approximately 10 miles Northwest of Valley Mills in Bosque County. This office was established in June 1990. The second branch is located in Meridian, Tx, which is 10 miles further Northwest of Clifton. This branch was established in December of 2005. The third branch, "The Ranch House," is located in McLennan County, between Valley Mills and Waco, Texas. The Ranch House branch opened in June 1995. FNB also has seven automated teller machines (ATMs) located throughout both assessment areas. FNB is 100% owned by a one-bank, locally owned holding company, Valley Mills Financial Corporation.

The loan portfolio comprises 51% of the bank's total assets and the loan to deposit ratio is 60.4%. Lending products include residential real estate, consumer, and commercial loans. The following chart details the breakdown of FNB's loan portfolio as of September 30, 2007.

Table 1 – LOAN PORTFOLIO COMPOSITION		
Loan Category	\$ (000)	%
Residential Real Estate Loans	20,638	40
Commercial Loans	9,343	18
Commercial Real Estate Loans	4,734	9
Construction & Land Development Loans	1,270	2
Farmland Loans	4,187	8
Agricultural Loans	1,233	2
Consumer Loans	10,665	20
Other	232	0
Total	52,302	100

Source: Institution Consolidated Reports of Condition as of 9/30/2007

No legal impediments or other factors hinder the bank's ability to provide credit. Based on its financial condition, the stable local economy, product offerings, and competition, FNB has the ability to meet the various credit needs in its community. Prior rating of CRA performance for this bank in April 2002 was Outstanding.

DESCRIPTION OF ASSESSMENT AREA(S)

FNB has two AA's, one of which consists of all the census tracts in Bosque county, and the second, located within the Waco Metropolitan Statistical Area (MSA), consists of five census tracts in the western part of McLennan county and includes part of the West side of Waco, Tx.

Waco Assessment Area

This AA includes one middle-income tract and four upper-income tracts, which are part of the Waco MSA in McLennan County. Based on 2000 Census data, the AA has a population of 17,924. According to the 2000 housing data provided in the census, there are 5,171 households. The Median Family Income level for the Waco MSA is \$51,731.

Table 2	
DEMOGRAPHIC AND ECONOMIC CHARACTERISTICS OF WACO-MSA AA	
Population	
Number of Persons	17,924
Number of Families	3,697
Number of Households	5,171
Geographies	
Number of Census Tracts	5
% Low-Income Census Tracts	0
% Moderate-Income Census Tracts	0
% Middle-Income Census Tracts	20%
% Upper-Income Census Tracts	80%
<i>Median Family Income (MFI)</i>	
2000 MFI for AA	51,731
2007 HUD-Adjusted MFI	49,100
Economic Indicators	
Unemployment Rate	1.29%
2007 Median Housing Value	\$82,760
% of Owner-occupied Properties	\$94.67
% of Households Below Poverty Level	11.38%

Bosque County Assessment Area

This AA includes two upper income census tracts and four middle income tracts located in Bosque County. Based on the 2000 Census data, the AA has a population of 17,204. According to the housing data as provided in the census, there are 8,644 housing units in this area. The AA in Bosque county is a predominately middle income area, but it is a relatively higher income area compared to other rural areas of Texas. Income information from the United States Census data for 2000 reveals that the median family income (MFI) level for this area is \$42, 222. For all non-metropolitan areas in Texas this was \$35,800 in 2001.

Table 3	
DEMOGRAPHIC AND ECONOMIC CHARACTERISTICS OF NON-MSA AA	
Population	
Number of Persons	17,204
Number of Families	5,831
Number of Households	6,726
Geographies	
Number of Census Tracts	6
% Low-Income Census Tracts	0%
% Moderate-Income Census Tracts	0%
% Middle-Income Census Tracts	67%
% Upper-Income Census Tracts	33%
<i>Median Family Income (MFI)</i>	
2000 MFI for AA	42,222
2007 HUD-Adjusted MFI	43,100
Economic Indicators	
Unemployment Rate	2.36%
2007 Median Housing Value	\$61,710
% of Owner-occupied Properties	77.72%
% of Households Below Poverty Level	13.44%

Local economic conditions reflect steady growth in population and economic activity in both AA's. Three community contacts, including the Valley Mills city manager, local newspaper publisher, and the county judge, all agreed the area is undergoing steady economic growth. They also said the quality of banking services in the AA's was satisfactory and could not identify any unmet credit needs.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

Loan-to-Deposit (LTD) Ratio

FNB's LTD ratio is good, given its asset size, financial condition, and lending opportunities in the AA. Since the last CRA examination, the LTD ratio has decreased slightly from 64.1% in April 2002 to 60.4% at September 30, 2007. The average LTD ratio over the past 17 quarters was 60.4%. The average LTD ratio of three similarly situated banks

headquartered in the local area was 59% during this same time period. The asset size and LTD ratio for FNB and its competing banks are listed below.

Table 4 Institution	Assets as of 9/30/07 (000s)	Average LTD Ratio (%)
First Security State Bank, Cranfills Gap	67,537	43.51
First National Bank, McGregor	92,227	73.66
First National Bank, Moody	117,885	61.22
<i>First National Bank of Bosque County</i>	<i>100,916</i>	<i>60.44</i>

Lending in Assessment Area

A substantial majority of the bank’s loans are made within its AA, both MSA and non-MSA. In order to assess performance for this criterion, we reviewed a sample of 30 commercial loans made from 2005 through year to date 2007. We also incorporated an analysis of all mortgage-related loans originated in 2005 through 2007, that were reported on the Home Mortgage Disclosure Act (HMDA) Loan Application Register.

Our analysis determined that 83% of the number and 72% of the dollar amount of 1-4 family residential loans and small commercial loans were made within the AA. This distribution of loans is similar to internal bank reports and indicates that FNB is committed to meeting the credit needs in its local community.

Table 5 - Lending in Assessment Area									
Number of Loans					Dollars of Loans				
	Inside		Outside			Inside		Outside	
	#	%	#	%		\$ (\$000)	%	\$	%
Total	1,815	83	370	17	Total	32,699	72	13,028	28

Source: US Census Data; Bank Records

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

FNB’s loan portfolio reflects a good distribution of mortgage and consumer loans to individuals of various income levels and businesses of different sizes within the AA. In order to assess the bank’s performance, we used HMDA information relative to mortgage-related loans originated in 2005 through June 2007, census data, and samples of bank loans to small businesses.

Our analysis determined that FNB has adequate amount of lending to all applicants,

regardless of their income category. Our analysis of mortgage loans made to low and moderate income families reflected an adequate volume, given the make-up of the Bosque County AA. According to census demographic information, approximately 14% of families in this area are low-income families. Our sample and HMDA data indicated that 5.8% of all mortgage-related loans originated in the Bosque County AA were made to low-income families. This volume of lending is satisfactory given limited number of homes available at prices for which low-income families could qualify. The following tables reflect the bank's performance in the metropolitan and non-metropolitan regions of their AA.

Table 6								
BORROWER DISTRIBUTION OF 1-4 FAMILY REAL ESTATE – Non-MSA								
Borrower Income Level	LOW		MODERATE		MIDDLE		UPPER	
% of AA Families	14.42		16.20		21.69		47.69	
LOANS BY YEAR	% of Number	% of Amount	% of Number	% of Amount	% of Number	% of Amount	% of Number	% of Amount
2005-2007	8.27	5.12	15.70	13.97	23.14	15.42	52.89	65.49

Source: US Census Data; Bank Records

We found similar performance in the AA located in the Waco MSA. Again lending rates to low and moderate income families were somewhat lower than their presence in the AA, but the amount of lending is acceptable, given the limited number of qualified applicants and the limited number of properties in the price ranges that they can afford.

Table 7								
BORROWER DISTRIBUTION OF 1-4 FAMILY REAL ESTATE – Waco-MSA								
Borrower Income Level	LOW		MODERATE		MIDDLE		UPPER	
% of AA Families	14.03		11.69		20.56		53.45	
LOANS BY YEAR	% of Number	% of Amount	% of Number	% of Amount	% of Number	% of Amount	% of Number	% of Amount
2005-2007	5.77	1.37	9.62	4.18	21.15	16.11	63.46	78.34

Source: US Census Data; Bank Records

FNB originates a satisfactory number of commercial loans to small businesses (revenues less than 1 million). Management continues to focus on providing loans that will enhance the local economy. The following charts reflect our analysis of our sample

of commercial-related loans originated during 2005 through 2007 in both AA's. Community leaders contacted noted that the AA's credit needs are being well served by local banks, including FNB.

Table 8 - Borrower Distribution of Loans to Businesses/Farms in Non-MSA		
Business Revenues (or Sales)	≤\$1,000,000	>\$1,000,000
% of AA Businesses*	96.79	3.21
% of Bank Loans in AA by #	100	0.00
% of Bank Loans in AA by \$	100	0.00

Source: US Census Data; Bank Record

Table 9 - Borrower Distribution of Loans to Businesses/Farms in Waco MSA		
Business Revenues (or Sales)	>\$1,000,000	≤\$1,000,000
% of AA Businesses*	4.78	95.26
% of Bank Loans in AA by #	13.33	86.67
% of Bank Loans in AA by \$	24.87	75.13

Source: US Census Data; Bank Record

Geographic Distribution of Loans

As previously mentioned, all the census tracts located within FNB's AA are classified as middle- or upper-income census tracts. Therefore, an analysis of loan distribution by geographic area would not be meaningful.

Responses to Complaints

FNB has received no complaints relating to the bank's performance under the CRA.

Fair Lending or Other Illegal Credit Practices Review

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

