

PUBLIC DISCLOSURE

September 9, 2002

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

St. Michaels Bank
280624
P. O. Box 70
St. Michaels, Maryland 21601

Federal Reserve Bank of Richmond
P. O. Box 27622
Richmond, Virginia 23261

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 RATING

INSTITUTION'S CRA RATING: St. Michaels Bank is rated "**SATISFACTORY.**"

The following table indicates the performance level of St. Michaels Bank with respect to the lending, investment, and service tests.

PERFORMANCE LEVELS	<u>ST. MICHAELS BANK</u>		
	PERFORMANCE TESTS		
	Lending Test*	Investment Test	Service Test
Outstanding			
High Satisfactory	X		X
Low Satisfactory		X	
Needs to Improve			
Substantial Noncompliance			

* The lending test is weighted more heavily than the investment and service tests in determining the overall rating.

The major factors supporting the institution's rating include:

- Overall lending activity is consistent with the bank's capacity and market presence.
- A substantial majority of the institution's small business, consumer unsecured, and residential real estate loans were originated within the bank's assessment area.
- Lending to businesses with revenues of \$1 million or less is considered excellent. The overall geographic distribution of small business lending is good.

- Although the geographic and borrower distribution of consumer unsecured and residential real estate loans is varied, overall, the performance is considered good.
- The bank has originated an adequate level of community development loans demonstrating responsiveness to community credit needs.
- The level of qualified community development investments has improved since the previous evaluation and is considered adequate relative to available opportunities and bank capacity.
- Delivery systems and branch locations are accessible to all segments of the assessment area.
- An adequate level of community development services was identified.
- The bank has not received any complaints regarding its CRA performance since the previous evaluation.

INSTITUTION

DESCRIPTION OF INSTITUTION

St. Michaels Bank operates five full-service offices in Talbot County, Maryland. The institution is headquartered in the Town of St. Michaels and is a subsidiary of Mercantile Bankshares Corporation, a multibank holding company located in Baltimore, Maryland. As of June 30, 2002, the bank had \$203 million in assets of which 88.4% were loans. Various credit and deposit products are available through the institution including commercial loans, consumer loans, and residential mortgage loans. The loan portfolio, as of June 30, 2002, was comprised of 69.6% real estate secured (including consumer and business), 22.6% commercial/agricultural, 7.3% consumer, and .5% other. The bank has not opened or closed any branches since the previous evaluation. The institution's previous CRA rating was Satisfactory.

DESCRIPTION OF ASSESSMENT AREA

The assessment area has been designated as Talbot County, Maryland, and contains nine block numbering areas (BNAs). Of the nine BNAs, one is moderate-income, four are middle-income, and four are upper-income. There are no low-income

geographies within the market. According to the 1990 census data, the assessment area has a population of 30,549 and a median housing value of \$116,978. The owner-occupancy rate for the assessment area is 59% and is slightly higher than that for the nonmetropolitan areas of Maryland at 52%. The poverty rate for the assessment area is 6.4%, which is lower than that for the nonmetropolitan areas of Maryland at 8%. The 2001 median family income for nonmetropolitan areas of Maryland is \$52,700.

The following table provides demographics for the Talbot County assessment area.

Assessment Area Demographics								
Income Categories	Tract Distribution		Families by Tract Income		Families < Poverty Level as % of Families by Tract		Families by Family Income	
	#	%	#	%	#	%	#	%
Low-income	0	0%	0	0%	0	0%	1,452	16.2%
Moderate-income	1	11.2%	764	8.5%	137	17.9%	1,360	15.2%
Middle-income	4	44.4%	4,396	49.2%	263	6.0%	1,903	21.3%
Upper-income	4	44.4%	3,785	42.3%	169	4.5%	4,230	47.3%
Total Assessment Area	9	100%	8,945	100%	569	6.4%	8,945	100%
	Housing Units by Tract	Housing Types by Tract						
		Owner-occupied		Rental		Vacant		
		#	%	%	#	%	#	%
Low-income	0	0	0%	0%	0	0%	0	0%
Moderate-income	1,404	455	5.3%	32.4%	858	61.1%	91	6.5%
Middle-income	6,918	4,207	48.7%	60.8%	2,010	29.1%	701	10.1%
Upper-income	6,375	3,974	46%	62.3%	1,173	18.4%	1,228	19.3%

Total Assessment Area	14,697	8,636	100%	58.8%	4,041	27.5%	2,020	13.7%
	Total Businesses by Tract		Businesses by Tract & Revenue Size					
			Less Than or = \$1 Million		Over \$1 Million		Revenue Not Reported	
	#	%	#	%	#	%	#	%
Low-income	0	0%	0	0%	0	0%	0	0%
Moderate-income	266	12.2%	242	12.8%	16	9.5%	8	6.2%
Middle-income	1,282	58.8%	1,089	57.8%	118	70.2%	75	57.7%
Upper-income	634	29%	553	29.4%	34	20.3%	47	36.1%
Tract not reported	0	0%	0	0%	0	0%	0	0%
Total Assessment Area	2,182	100%	1,884	100%	168	100%	130	100%
	Percentage of Total Businesses:			86.3%		7.7%		6%

Talbot County is primarily rural and is located on the Eastern Shore of Maryland. Employment opportunities are provided by tourism, agriculture, and manufacturing. Major employers are Black and Decker, Memorial Hospital, and Allen Family Foods. As of August 2002, the unemployment rates for Talbot County and the State of Maryland are 2.9% and 4.2%, respectively.

SCOPE OF EXAMINATION

The review of the bank's lending activity includes loans reported as required by the CRA regarding small business/small farm loans originated or purchased from January 1, 2000, to December 31, 2001. In addition, the review includes sampled consumer unsecured and residential real estate loans extended from July 1, 2001, to December 31, 2001. Community Development loans, qualified investments and services were considered for the period starting January 1, 2000, to December 31, 2001.

CRA performance was evaluated using the interagency examination procedures developed by the Federal Financial Institution's Examination Council. The institution's ratings are based on performance in the bank's only assessment area.

CONCLUSIONS WITH RESPECT TO PERFORMANCE TESTS

LENDING TEST

The lending test is rated high satisfactory overall based on lending activity, distribution of lending, and community development lending. Area demographics, Dun & Bradstreet (D&B) economic data, and market aggregate information are used as proxies for demand when evaluating the bank's performance. Aggregate data for 2000 is used since 2001 data is not yet available. Aggregate data includes St. Michaels Bank and all reporting institutions that originated loans of the type considered within St. Michaels' assessment area. During 2000 and 2001, the institution did not originate any farm loans.

Lending Activity:

The institution primarily serves its market through direct lending and offers a variety of credit products. The loan-to-deposit ratio is one measure of a bank's lending activity relative to its capacity. During a 16-quarter period ending June 30, 2002, the quarterly average loan-to-deposit ratio for all banks headquartered in nonmetropolitan areas of Maryland and of similar asset size to St. Michaels Bank ranged from 75.3% to 87.8%. The bank's average loan-to-deposit ratio for the same 16-quarter period is 113.6%. No barriers to the bank's ability to lend were noted.

Various loan products are available through the institution including consumer, residential mortgage, home equity, and commercial loans. Mortgage loans offered by the bank include construction-only financing, as well as a one-time closing construction/permanent product (in conjunction with the bank's affiliate, Mercantile Mortgage Corporation). In addition, the bank offers home purchase, refinance, and home equity loans with 15- or 30-year terms and a three- or five-year balloon. Home equity lines of credit are also offered.

Small Business Administration (SBA) loans are offered by St. Michaels Bank and are included in the small business totals below. From January 2000 through August 2002, the bank extended eight SBA loans totaling approximately \$1.1 million.

Assessment Area Concentration:

The institution's lending volume for small business loans extended from January 1, 2000, to December 31, 2001, as well as sampled consumer unsecured and residential real estate loans extended from July 1, 2001, to December 31, 2001, are represented in the following table.

Lending Inside and Outside the Assessment Area								
	Inside				Outside			
	#	%	\$('000s)	%	#	%	\$('000s)	%
Consumer Unsecured	200	79.7%	\$2,343	79.3%	51	20.3%	\$610	20.7%
Residential Real Estate	39	67.2%	\$8,307	72.7%	19	32.8%	\$3,127	27.3%
Sampled consumer unsecured and real estate loans are for the period July 1, 2001 through December 31, 2001.								
Small Business	556	90.7%	\$39,812	82.6%	57	9.3%	\$8,371	17.4%
Small business loans are for the period January 1, 2000, through December 31, 2001								

Note: Affiliate loans are not included.

As depicted above, the majority of consumer unsecured (79.7%), residential real estate (67.2%), and small business loans (90.7%) were originated within the assessment area. Overall, the bank originated a substantial majority of loans within its assessment area.

Geographic Distribution:

The following tables present data about the bank's lending. Discussion of the bank's performance follows each table. As previously noted, there are no low-income BNAs in the assessment area.

Distribution of Small Business Loans by Income Level of Geography

	Moderate -Income	Middle- Income	Upper- Income	Total
Total Number of Loans	61	283	212	556
Percentage of Total Loans	11%	50.9%	38.1%	100%
Total Amount of Loans (000's)	\$3,811	\$18,840	\$17,161	\$39,812
Percentage of Total Amount	9.6%	47.3%	43.1%	100%

The bank's level of lending to small businesses (11%) in the moderate-income geography exceeds the 2000 market aggregate penetration in the BNA (8.2%). Additionally, D&B statistics indicate that 12.2% of businesses within the assessment area are located within the moderate-income geography. The bank's geographic penetration with respect to small business loans is considered good.

Distribution of Consumer Unsecured Loans by Income Level of Geography

	Moderate -Income	Middle- Income	Upper- Income	Total
Total Number of Loans	9	93	98	200
Percentage of Total Loans	4.5%	46.5%	49%	100%
Total Amount of Loans (000's)	\$76	\$1,045	\$1,222	\$2,343
Percentage of Total Amount	3.2%	44.6%	52.2%	100%

The bank extended 4.5% of the sampled consumer unsecured loans within the moderate-income geography. This level of lending is lower than the percentage of area families residing in the moderate-income BNA (8.5%). The bank's lower level of lending is possibly attributed to the significant percentage of families within the geography who are living below the poverty level (17.9%). The poverty rate within the entire market is much lower at 6.4%. The geographic distribution of consumer unsecured loans is considered adequate.

Distribution of Residential Real Estate Loans by Income Level of Geography

	Moderate -Income	Middle- Income	Upper- Income	Total
Total Number of Loans	1	16	22	39
Percentage of Total Loans	2.6%	41%	56.4%	100%
Total Amount of Loans (000's)	\$230	\$2,254	\$5,823	\$8,307
Percentage of Total Amount	2.8%	27.1%	70.1%	100%

The percentage of residential real estate loans made within the moderate-income BNA (2.6%) is somewhat lower than the percentage of owner-occupied housing units (5.3%) in such area. However, as previously mentioned, the percentage of families below the poverty level in this area (17.9%) is significantly higher than the percentage of families below the poverty level in the market (6.4%). Therefore, this level of real estate lending is adequate.

Distribution by Borrower Income and Revenue Size of the Business:

The tables that follow present data about bank lending to businesses of different sizes and to borrowers of different incomes. Discussion of the bank's performance follows each table.

Distribution of Lending
by Loan Amount and Size of Business

	\$0 - \$100,000		>\$100,000 TO \$250,000		> \$250,000		TOTAL	
Number Total Revenues ≤ \$1 Million	381	68.5%	53	9.5%	31	5.6%	465	83.6%
Number Total Revenues > \$1 Million	70	12.6%	15	2.7%	6	1.1%	91	16.4%
Totals	451	81.1%	68	12.2%	37	6.7%	556	100%

Based on recent D&B data, 91.8% of businesses within the assessment area that reported revenue data have annual revenues of \$1 million or less. According to aggregate small business data, at least 50.3% of all small business loans reported within the market were to businesses with revenues of \$1 million or less. The remaining loans were extended to businesses having revenues in excess of \$1 million per year or revenue data was not reported. As illustrated in the table, 83.6% of the small business loans were provided to entities with revenues of \$1 million or less. Furthermore, 68.5% of the loans were to borrowers with revenues not exceeding \$1 million and in amounts of \$100,000 or less. This level of small business lending is considered excellent.

Distribution of Consumer Unsecured Loans by Income Level of Borrower

Of the 200 consumer unsecured loans sampled within the assessment area, 49 did not include income data and, therefore, are excluded from the analysis.

	Low- Income	Moderate -Income	Middle- Income	Upper- Income	Total
Total Number of Loans	58	49	20	24	151
Percentage of Total Loans	38.4%	32.5%	13.2%	15.9%	100%
Total Amount of Loans (000's)	\$290	\$461	\$368	\$313	\$1,432
Percentage of Total Amount	20.3%	32.2%	25.7%	21.8%	100%

The level of consumer unsecured lending to low- and moderate-income residents (38.4% and 32.5%) exceeds the proportion of both low-income (16.2%) and moderate-income (15.2%) families within the assessment area. This distribution reflects excellent penetration among low- and moderate-income borrowers.

Distribution of Residential Real Estate Loans by Income Level of Borrower

Of the 39 real estate loans sampled within the assessment area, 15 did not contain income data and, therefore, are not included in the analysis.

	Low- Income	Moderate -Income	Middle- Income	Upper- Income	Total
Total Number of Loans	3	7	7	7	24
Percentage of Total Loans	12.4%	29.2%	29.2%	29.2%	100%
Total Amount of Loans (000's)	\$326	\$584	\$704	\$2,715	\$4,329
Percentage of Total Amount	7.5%	13.5%	16.3%	62.7%	100%

In cases when income was known, 12.4% and 29.2% of real estate loans were extended to low- and moderate-income individuals, respectively. The bank's level of lending to low-income borrowers is somewhat lower than the proportion of such families (16.2%) within the assessment area, while the level of lending to moderate-income borrowers is higher than the proportion of such families (15.2%) within the assessment area. This distribution of lending to low- and moderate-income borrowers is considered good.

Overall, the borrower and geographic distribution of loans is considered good.

Community Development Lending:

St. Michaels Bank extended one community development loan during the evaluation period:

- A construction loan in the amount of \$1.2 million to the Easton Housing Authority was made. The funding was provided to initiate a neighborhood revitalization project whereby 12 single-family homes will replace a series of dilapidated row houses. The homes will be offered for sale to low- and moderate-income families. Other partners for this project include the State of Maryland (Community Development Block Grant and HOTSPOTS Rural Development Programs) and the Federal Home Loan Bank of Atlanta (provides buydown assistance monies).

The overall level of lending within this assessment area, as evaluated for the geographic distribution, borrower distribution, and level of community development loans is considered good taking into account the bank's market strategy, area demographic data, and aggregate data.

INVESTMENT TEST

The institution's level of responding to community development needs through its investment activities is rated low satisfactory. Qualified investments include multifamily development revenue bonds totaling \$500,000 issued by the Maryland Department of Housing and Community Development. The bonds are being sold to finance the construction of a multifamily rental housing project to be located in the City of Baltimore. The housing project will contain units designated for low- and moderate-income residents. Other investments include contributions to several causes that assist low- and moderate-income residents within Talbot County.

SERVICE TEST

The bank's performance under the service test is rated high satisfactory. Delivery systems, branch and ATM locations, and hours of operation are accessible and convenient to all portions of the assessment area. No branches have been opened or closed since the previous examination.

Retail Services:

Accessibility of Delivery Systems

Delivery systems are accessible to all portions of the assessment area. ATMs are available, and, through a network, provide customers with 24-hour nationwide access. Furthermore, bank-by-mail and 24-hour account access services are offered.

Branch Locations and Hours of Operation

St. Michaels Bank has five offices, of which one (20%) is located in the market's only moderate-income geography. This branch recently began offering Saturday hours. Branch locations and business hours are considered convenient and meet the needs of the assessment area.

Community Development Services:

The bank offers low cost checking and savings accounts. It also collects rents for the Easton Housing Authority for tenants of an apartment complex located in the moderate-income geography within Talbot County. Low- and moderate-income families reside in the apartments. The level of community development services is considered adequate.

COMPLIANCE WITH ANTIDISCRIMINATION LAWS AND REGULATIONS

No credit practices inconsistent with the substantive provisions of the fair housing and fair lending laws and regulations were identified. Adequate policies, procedures, and training programs have been developed to support nondiscrimination in lending activities.

CRA APPENDIX A

SCOPE OF EXAMINATION

A full discussion of the scope of the examination is contained in the narrative section of this evaluation.

LIST OF ASSESSMENT AREAS AND TYPE OF EXAMINATION:

ASSESSMENT AREA	TYPE OF EXAMINATION
Talbot County	Full Scope

CRA APPENDIX B

GLOSSARY

Aggregate lending: The number of loans originated and purchased by all reporting lenders in specified income categories as a percentage of the aggregate number of loans originated and purchased by all reporting lenders in the metropolitan area/assessment area.

Block numbering area ("BNA"): A statistical subdivision of a county for grouping and numbering blocks in nonmetropolitan counties where local census statistical area committees have not established census tracts. A BNA does not cross county lines.

Census tract: A small subdivision of metropolitan and other densely populated counties. Census tract boundaries do not cross county lines; however, they may cross the boundaries of metropolitan statistical areas. Census tracts usually have between 2,500 and 8,000 persons, and their physical size varies widely depending upon population density. Census tracts are designed to be homogeneous with respect to population characteristics, economic status, and living conditions to allow for statistical comparisons.

Community development: Affordable housing (including multifamily rental housing) for low- or moderate-income individuals; community services targeted to low- or moderate-income individuals; activities that promote economic development by financing businesses or farms that meet the size eligibility standards of the Small Business Administration's Development Company or Small Business Investment Company programs (13 CFR 121.301) or have gross annual revenues of \$1 million or less; or, activities that revitalize or stabilize low- or moderate-income geographies.

Consumer loan(s): A loan(s) to one or more individuals for household, family, or other personal expenditures. A consumer loan does not include a home mortgage, small business, or small farm loan. This definition includes the following categories: motor vehicle loans, credit card loans, home equity loans, other secured consumer loans, and other unsecured consumer loans.

Family: Includes a householder and one or more other persons living in the same household who are related to the householder by birth, marriage, or adoption. The number of family households always equals the number of families; however, a family household may also include non-relatives living with the family. Families are classified by type as either a married-couple family or other family, which is further classified into "male householder" (a family with a male householder and no wife present) or "female householder" (a family with a female householder and no husband present).

Full review: Performance under the lending, investment and service tests is analyzed considering performance context, quantitative factors (for example, geographic distribution, borrower distribution, and total number and dollar amount of investments), and qualitative factors (for example, innovativeness, complexity and responsiveness).

Geography: A census tract or a block numbering area delineated by the U. S. Bureau of the Census in the most recent decennial census.

Home Mortgage Disclosure Act ("HMDA"): The statute that requires certain mortgage lenders that do business or have banking offices in a metropolitan statistical area to file annual summary reports of their mortgage lending activity. The reports include data such as race, gender and income of applications, amount of loan requested, and disposition of the application (for example, approved, denied, and withdrawn).

Home mortgage loans: Includes home purchase and home improvement loans as defined in the HMDA regulation. This definition also includes multifamily (five or more families) dwelling loans, loans for the purchase of manufactured homes and refinancings of home improvement and home purchase loans.

Household: Includes all persons occupying a housing unit. Persons not living in households are classified as living in group quarters. In 100 percent tabulations, the count of households always equals the count of occupied housing units.

Limited review: Performance under the lending, investment and service tests is analyzed using only quantitative factors (for example, geographic distribution, borrower distribution, total number and dollar amount of investments, and branch distribution).

Low-income: Individual income that is less than 50 percent of the area median income, or a median family income that is less than 50 percent, in the case of a geography.

Market share: The number of loans originated and purchased by the institution as a percentage of the aggregate number of loans originated and purchased by all reporting lenders in the metropolitan area/assessment area.

Metropolitan area ("MA"): Any primary metropolitan statistical area ("PMSA"), metropolitan statistical area ("MSA") or consolidated metropolitan statistical area ("CMSA") as defined by the Office of Management and Budget, with a population of 250 thousand or more, and any other area designated as such by the appropriate federal financial supervisory agency.

Middle-income: Individual income that is at least 80 percent and less than 120 percent of the area median income, or a median family income that is at least 80 percent and less than 120 percent, in the case of a geography

Moderate-income: Individual income that is at least 50 percent and less than 80 percent of the area median income, or a median family income that is at least 50 percent and less than 80 percent, in the case of a geography.

Multifamily: Refers to a residential structure that contains five or more units.

Other products: Includes any unreported optional category of loans for which the institution collects and maintains data for consideration during a CRA examination. Examples of such activity include consumer loans and other loan data an institution may provide concerning its lending performance.

Owner-occupied units: Includes units occupied by the owner or co-owner, even if the unit has not been fully paid for or is mortgaged.

Qualified investment: A qualified investment is defined as any lawful investment, deposit, membership share or grant that has as its primary purpose community development.

Rated area: A rated area is a state or multistate metropolitan area. For an institution with domestic branches in only one state, the institution's CRA rating would be the state rating. If an institution maintains domestic branches in more than one state, the institution will receive a rating for each state in which those branches are located. If an institution maintains domestic branches in two or more states within a multistate metropolitan area, the institution will receive a rating for the multistate metropolitan area.

Small loan(s) to business(es): A loan included in "loans to small businesses" as defined in the Consolidated Report of Condition and Income ("Call Report") and the Thrift Financial Reporting ("TFR") instructions. These loans have original amounts of \$1 million or less and typically are either secured by nonfarm or nonresidential real estate or are classified as

commercial and industrial loans. However, thrift institutions may also exercise the option to report loans secured by nonfarm residential real estate as "small business loans" if the loans are reported on the TFR as nonmortgage, commercial loans.

Small loan(s) to farm(s): A loan included in "loans to small farms" as defined in the instructions for preparation of the Call Report. These loans have original amounts of \$500 thousand or less and are either secured by farmland, or are classified as loans to finance agricultural production and other loans to farmers.

Upper-income: Individual income that is more than 120 percent of the area median income, or a median family income that is more than 120 percent, in the case of a geography.