



PUBLIC DISCLOSURE

SEPTEMBER 9, 2013

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

**FARMERS STATE BANK
RSSD# 376657**

**118 WEST 1st STREET
STANBERRY, MISSOURI 64489**

**Federal Reserve Bank of Kansas City
1 Memorial Drive
Kansas City, Missouri 64198**

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.

TABLE OF CONTENTS

Institution's CRA Rating	2
Scope of Examination	2
Description of Institution	2
Description of Assessment Area	3
Conclusions with Respect to Performance Criteria	5

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

Farmers State Bank (the bank) has a satisfactory record of meeting the credit needs of its assessment area (AA), including small businesses and small farms, consistent with its resources and operating philosophy. Four of the five criteria used to evaluate a small bank's lending performance under the Community Reinvestment Act (CRA) were relevant to this review and are listed as follows:

- Net Loan-to-Deposit (NLTD) Ratio
- Lending Inside the AA
- Geographic Distribution of Loans Among Tracts of Different Income Levels
- Lending to Businesses and Farms of Different Revenue Sizes

The fifth core criterion used to assess a small bank's CRA performance, the bank's responsiveness to CRA-related complaints, was not evaluated as the bank has not received any of these complaints since the previous CRA examination.

SCOPE OF EXAMINATION

The bank's CRA performance was evaluated using the Federal Financial Institutions Examination Council Interagency Small Bank Examination Procedures. Conclusions for each performance criterion were based on data compiled from a sample of loan files for two of the bank's product lines. The product lines chosen were determined through discussions with management, a review of the bank's June 30, 2013 Report of Condition and Income (Call Report), and a review of the number of loan originations since the previous CRA examination on August 17, 2009. Loan products evaluated include statistical samples of 43 commercial loans from a universe of 55 loans originated since the prior CRA examination through August 1, 2013, as well as 34 agricultural loans from a universe of 99 loans originated in a six-month period between February 1, 2013 and August 1, 2013.

Interviews were also conducted with members of the local community to determine the specific credit needs, opportunities, and local market conditions within the bank's AA and to help evaluate the bank's responsiveness in helping to meet those needs.

DESCRIPTION OF INSTITUTION

The main office of the bank is located at 118 West 1st Street in Stanberry, Missouri, a community with a population of approximately 1,200 residents located in Gentry County. The main office has a full-service automated teller machine (ATM). In addition to the main office, the bank has a cash-dispensing ATM at 409 Alanthus Avenue in Stanberry.

The June 30, 2012, Federal Deposit Insurance Corporation (FDIC) Deposit Market Share Report indicates that the bank, with \$49.4 million in deposits and a market share of 6.9 percent,

ranks fifth out of nine FDIC-insured institutions operating in its AA of Gentry and Nodaway Counties, Missouri. The bank maintains a larger market share (30.7 percent) in Gentry County, where the bank is located, which ranks the bank first of six banks in the county.

The analysis of the bank's CRA performance considers the bank's financial capacity, local economic conditions, and demographics, including the competitive environment in which it operates. Based on its financial condition, size, resources, and credit product offerings, the bank has the ability to meet the credit needs of its AA. The bank had assets of \$58.3 million and loans of \$27.7 million as of the June 30, 2013 Call Report. Table 1 illustrates the composition of the bank's loan portfolio by product type.

TABLE 1 FARMERS STATE BANK LOAN PORTFOLIO		
Loan Type	Amount \$(000)	Percent of Total
Agricultural	17,439	62.9
Residential Real Estate	5,071	18.3
Commercial	3,840	13.9
Consumer	1,364	4.9
Gross Loans	27,714	100.0

DESCRIPTION OF THE BANK'S ASSESSMENT AREA

The bank's designated AA includes all of Gentry County (two middle-income census tracts) and the eastern-most part of Nodaway County (one upper-income census tract). Both census tracts in Gentry County have been designated as underserved middle-income nonmetropolitan tracts due to their remote and rural nature.

The city of Stanberry is located in an area of northern Missouri that is dominated by agricultural and ranchland operations. As such, the local economy is relatively volatile and dependent upon factors such as annual weather conditions, market prices, and government paid farm subsidies. The United States Department of Agriculture (USDA) 2007 Census of Agriculture reports that Gentry and Nodaway Counties contained 839 and 1,540 farms, respectively. Other major non-agricultural employers in the area include: manufacturers, Johnson Controls in St. Joseph and Kawasaki in Maryville, retail stores, Dollar General in Stanberry and Albany and Wal-Mart in Maryville, medical centers, Northwest Medical Center in Albany, and, higher education centers, Maryville University. Community contacts stated that there are also many self-employed individuals in the area and that most people in rural areas have some form of commute for work, usually between 10 to 40 minutes each way.

The bank's AA is homogeneous, with a 96.5 percent White, non-Hispanic population. Based on 2010 Census data, the AA population was 12,212, virtually unchanged from the 12,187 reported on the 2000 Census. The AA median family income (MFI) of \$50,512 is approximately 10.0 percent higher than the Missouri statewide rural MFI of \$45,840. There is a lower concentration

of low- to moderate-income (LMI) families in the AA (32.1 percent) compared to those in the Missouri statewide rural areas (38.3 percent), and there are less AA families below the poverty line at 9.8 percent as compared to 12.4 percent of families in the Missouri statewide rural areas.

In 2010, the AA housing stock was older, with a median age of 44 years, compared to the Missouri statewide rural median age of 34 years. The median housing value of the AA was \$84,546 compared to \$94,828 for the Missouri statewide rural areas. Despite the lower median household value in the AA, the affordability of housing in the AA is still lower, with a housing affordability ratio¹ of 47.7 percent compared to 38.0 percent for the statewide rural areas. Two community contacts indicated that they feel housing in the area is affordable and that homes sell fairly quickly after going on the market.

As stated earlier, agriculture comprises a large portion of the AA's economy. The major crops grown in the AA are soybeans, forage (land used for hay, grass, and green chop), and corn. Hogs and cattle make up the largest share of livestock inventory. According to the USDA, the number of farming operations in the AA increased 7.3 percent between 2002 and 2007 from 2,217 to 2,379 farming operations. This 2007 data is the latest available until the USDA 2012 Census of Agriculture is published. One community contact indicated that, in his opinion, smaller farms are being consolidated into larger farming operations, which would suggest an overall decline in the total number of farm operations since 2007.

Members of the community were interviewed to gain perspective on the local economy and the AA credit needs. A county clerk and executive director of an agricultural agency stated that local economic conditions have held steady when compared to the national economic downturn given the dominance of agricultural activities and their healthy conditions in the area. Currently, the AA main credit needs are agricultural activity financing and funding to maintain local infrastructure (roads, facilities, bridges, etc.). In addition, contacts felt that communities would benefit from attracting more businesses to create jobs and healthcare facilities to serve the aging population.

¹ Affordability rates are calculated using the median household income and median housing values, with the lower rates indicating less affordable housing.

The following Table 2 provides a summary of the bank's AA demographics.

TABLE 2 FARMERS STATE BANK AA 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	0	0.0	458	15.6
Moderate-income	0	0.0	0	0.0	0	0.0	487	16.5
Middle-income	2	66.7	1,741	59.1	162	9.3	672	22.8
Upper-income	1	33.3	1,204	40.9	127	10.5	1,328	45.1
Total AA	3	100.0	2,945	100.0	289	9.8	2,945	100.0
	Housing Units by Tract	Housing Type by Tract						
		Owner-occupied			Rental		Vacant	
		#	% by tract	% by unit	#	% by unit	#	% by unit
Middle-income	3,232	2,046	60.4	63.3	624	19.3	562	17.4
Upper-income	1,994	1,344	39.6	67.4	412	20.7	238	11.9
Total AA	5,226	3,390	100.0	64.9	1,036	19.8	800	15.3
	Total Businesses by Tract		Businesses by Tract & Revenue Size					
			Less Than or = \$1 Million		Over \$1 Million		Revenue Not Reported	
	#	%	#	%	#	%	#	%
Middle-income	392	64.5	345	63.9	21	75.0	26	65.0
Upper-income	216	35.5	195	36.1	7	25.0	14	35.0
Total AA	608	100.0	540	100.0	28	100.0	40	100.0
Percentage of Total Businesses:				88.8		4.6		6.6
	Total Farms by Tract		Farms by Tract & Revenue Size					
			Less Than or = \$1 Million		Over \$1 Million		Revenue Not Reported	
	#	%	#	%	#	%	#	%
Middle-income	158	53.6	158	53.6	0	0.0	0	0.0
Upper-income	137	46.4	137	46.4	0	0.0	0	0.0
Total AA	295	100.0	295	100.0	0	0.0	0	0.0
Percentage of Total Farms:				100.0		0.0		0.0

Based on 2010 Census tract boundaries, 2010 American Community Survey data, and 2012 Dun & Bradstreet (D&B) data.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

The bank's record of meeting the credit needs of its AA is considered satisfactory based on the lending performance in its designated AA. Data utilized for the analysis included the bank's performance data, area demographic information, and input obtained from members of the local community.

Net Loan-to-Deposit Ratio

The bank's NLTD ratio is considered reasonable in context of the bank's size, financial condition, and the credit needs of its AA. Since the previous CRA examination in 2009, the bank's 16-quarter average NLTD ratio declined from 69.1 percent to 54.6 percent. Deposits increased by approximately 16 percent, while loans increased only 1 percent. This NLTD ratio is below the state of Missouri, statewide rural area, and U.S. aggregate NLTD ratios of 76.7 percent, 75.5 percent, and 72.5 percent, respectively. The bank explained that they have been losing some of their best loans to borrower-owned lending cooperatives due to the favorable rates and terms offered by these institutions. In addition, the bank operates in a community dominated by farming operations that have been performing well, resulting in more cash to deposit and less need for credit. This is supported by data from four peer institutions of most similar asset size and loan portfolio mix located in nearby rural counties, with NLTD ratios ranging from 41.5 percent to 57.1 percent, which are similar to the bank's NLTD ratio of 54.6 percent.

Lending Inside the Assessment Area

The bank's record of lending inside its AA is considered reasonable. Based on the statistical sample of loans reviewed during the examination, the bank originated a majority of its loans within its AA. Table 3 illustrates the two loan products, commercial and agricultural loans, which were reviewed for the analysis. Of the 77 loans reviewed, 60 (or 77.9 percent) were made to borrowers located within the bank's AA. Only those loans originated inside the AA were considered for the remaining analyses.

TABLE 3 SUMMARY OF LENDING PERFORMANCE								
Lending within the AA								
Bank Loans	Inside AA				Outside AA			
	#	\$(000)	#%	\$%	#	\$(000)	#%	\$%
Commercial	31	1,424	72.1	70.6	12	593	27.9	29.4
Agricultural	29	1,083	85.3	96.9	5	35	14.7	3.1
Total Loans	60	2,507	77.9	80.0	17	628	22.1	20.0

Lending Distribution by Income Level of Geographies

This performance criterion evaluates the bank's distribution of loans among geographies of various income levels, primarily in LMI geographies. The bank's commercial and agricultural lending activity was compared to the percentage of all businesses and farms located in each income level tracts. Because the bank's AA does not have any LMI geographies, this analysis focuses on the bank's level of lending in middle-income tracts, as summarized in Table 4. Overall, the bank had a reasonable penetration of commercial and agricultural loans in the middle-income tracts.

TABLE 4 DISTRIBUTION BY INCOME LEVEL OF GEOGRAPHIES					
Census Tract Income Level	Commercial Loans				% of Businesses ¹
	#	\$(000)	#%	\$%	
Middle	31	1,424	100.0	100.0	63.9
Upper	0	0	0.0	0.0	36.1
Census Tract Income Level	Agricultural Loans				% of Farms ¹
	#	\$(000)	#%	\$%	
Middle	25	1,052	86.2	97.1	53.6
Upper	4	31	13.8	2.9	46.4

¹ Based on 2012 D&B data.
(Note: Total percentages shown may vary by 0.1 percent due to automated rounding differences.)

Commercial Loans

The bank originated all of the 31 commercial loans in the two middle-income tracts and none in the upper-income census tract. This exceeds the 63.9 percent of businesses located in the middle-income geographies and represents an excellent penetration of loans in the middle-income tracts.

Agricultural Loans

The bank's penetration of agricultural loans in the middle-income tracts was 86.2 percent by number and 97.1 percent by the dollar volume of loans. Both figures exceed the 53.6 percent of farms located in the middle-income geographies of the bank's AA and indicate a reasonable penetration of loans in those tracts.

Distribution by Revenue Size of Businesses and Farms

This performance criterion evaluates the bank's distribution of lending to businesses and farms of different revenue sizes, focusing primarily on small businesses and small farms with gross annual revenues of \$1 million or less. Emphasis is placed on the number of originations to small businesses and farms rather than the dollar volume within the AA to better represent the number of applicants served. Table 5 summarizes the bank's results.

TABLE 5 DISTRIBUTION BY REVENUE SIZE OF BUSINESSES AND FARMS					
Business Revenue	Commercial Loans				% of Businesses by Revenue ¹
	#	\$(000)	#%	\$%	
\$1MM or less	31	1,424	100.0	100.0	88.8
Over \$1MM	0	0	0.0	0.0	4.6
Farm Revenue	Agricultural Loans				% of Farms by Revenue ¹
	#	\$(000)	#%	\$%	
\$1MM or less	29	1,083	100.0	100.0	100.0
Over \$1MM	0	0	0.0	0.0	0.0

¹ Based on 2012 D&B data. Table does not include businesses where the income is unknown.
(Note: Total percentages shown may vary by 0.1 percent due to automated rounding differences.)

Commercial Loans

The bank's level of loans to small businesses is considered reasonable. As shown in Table 5, all of the bank's commercial loans were originated to small businesses, defined as businesses with gross revenues of \$1 million or less. This compares favorably to the 88.8 percent of businesses in the bank's AA that are classified as small businesses.

Agricultural Loans

The bank's level of loans to small farms is considered reasonable. As depicted in Table 5, all of the bank's agricultural loans were extended to small farms, defined as farms with gross revenues of \$1 million or less. This compares favorably to the 100.0 percent of farms in the bank's AA, which meet the definition of small farm.

FAIR LENDING OR OTHER ILLEGAL CREDIT PRACTICES REVIEW

An evaluation of the bank's fair lending activities was conducted during the examination to determine compliance with the substantive provisions of the antidiscriminatory laws and regulations, including the Equal Credit Opportunity Act and the Fair Housing Act. A review of the bank's policies and procedures, credit applications, loans and denials, and staff interviews revealed no prohibited practices designed to discourage loan applicants. In addition, the bank has not engaged in any illegal credit practices inconsistent with helping to meet the credit needs of its community.