

GENERAL INFORMATION

The Community Reinvestment Act (“CRA”) requires each federal financial supervisory agency to use its authority when examining financial institutions subject to its supervision to assess the institution’s record of meeting the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with the safe and sound operation of the institution. Upon conclusion of such examination, the agency must prepare a written evaluation of the institution’s record of meeting the credit needs of its community.

This document is an evaluation of the CRA performance of Hand County State Bank, Miller, South Dakota, prepared by the Federal Reserve Bank of Minneapolis, the institution’s supervisory agency, as of October 28, 1997. The agency rates the CRA performance of an institution consistent with the provisions set forth in Appendix A to 12 CFR Part 228.

INSTITUTION’S CRA RATING: This institution is rated “Outstanding.”

Several factors support rating the bank’s CRA performance outstanding. First, the bank originated a very high percentage of its consumer loans to low- and moderate-income borrowers, commercial loans to small businesses, and agricultural loans to small farms. Second, the bank’s net loan-to-deposit ratio is good, and the bank has originated one community development loan since the last evaluation. Finally, the bank owns a large qualified community development security and participates in community development services.

DESCRIPTION OF INSTITUTION

The bank is able to fulfill the credit needs of its community given its size, financial condition, and product offerings. The bank was rated outstanding in serving the credit needs of its community at its previous CRA evaluation. The bank's main office is in Miller, South Dakota. The bank is open Monday through Friday from 9:00 a.m. to 3:00 p.m. and Saturday from 9:00 a.m. to noon. Its drive-up teller service is available Monday through Friday from 8:30 a.m. to 4:30 p.m. and Saturday from 8:30 a.m. to 12:30 p.m. The bank operates one cash-dispensing automated teller machine ("ATM"), which is also in Miller and is located one block from the bank's main office. The bank does not operate any branch offices.

According to the September 30, 1997, Report of Condition ("ROC"), the bank had total assets of approximately \$50.2 million. Since the last evaluation, the bank's total assets have remained stable. According to the December 31, 1995, ROC, the bank's total assets were approximately \$51.2 million. Between December 31, 1995, and September 30, 1997, the bank's total deposits decreased approximately 1%, while net loans decreased 8%. The following table shows the changes to the bank's deposits and net loans based on quarterly ROC data since the last evaluation.

QUARTERLY CHANGES TO NET LOANS AND DEPOSITS		
Period	Net Loans	Deposits
January 1, 1996, to March 31, 1996	(11%)	-
April 1, 1996, to June 30, 1996	-	(2%)
July 1, 1996, to September 30, 1996	-	1%
October 1, 1996, to December 31, 1996	6%	(1%)
January 1, 1997, to March 31, 1997	(11%)	4%
April 1, 1997, to June 30, 1997	7%	(1%)
July 1, 1997, to September 30, 1997	2%	(2%)

Bank management attributed the most recent 11% decrease in net loans to the seasonal credit needs of the bank's borrowers, most of whom are farmers, as well as the severe winter of 1996-1997. A severe winter weakens the local economy and reduces the level of credit demanded by residents, farmers, and business owners. As of September 30, 1997, the composition of the bank's loan portfolio was 73% agricultural, 12% commercial, 12% consumer, and 3% consumer real estate loans. The bank's loan mix reflects the demand for specific types of credit by residents, farmers, and business owners in the assessment area.

The bank offers a variety of loan products to serve the credit needs of residents, farmers and business owners of the assessment area. It extends conventional agricultural, commercial, residential real estate, home improvement, home rehabilitation, and consumer loans. To service the needs of agricultural and commercial borrowers, the bank also participates in government-sponsored loan programs through the Small Business Administration ("SBA"), Farm Service Agency ("FSA"), and South Dakota Department of Agriculture ("SDDA"). With respect to the latter agency, the bank participates in the Beginning Farm Bond Program, which helps new farmers finance agricultural real estate acquisitions at below-market interest rates. To increase local residents' access to residential real estate loan programs, the bank has established an informal referral arrangement with another financial institution that has experience in originating loans through a wide variety of state and federal loan programs. Pursuant to this arrangement, the bank has made a number of referrals. As a convenience for the referred applicants, the other financial institution has agreed that loan closings may take place locally. For mobile home loan applicants, the

bank has established a referral arrangement with a finance company. Finally, the bank also purchases loans from motor vehicle, building supply, farm product, and equipment dealers.

DESCRIPTION OF HAND COUNTY STATE BANK'S ASSESSMENT AREA

The bank's assessment area consists of two block numbering areas ("BNA") in Hand County in east-central South Dakota. The assessment area is a very sparsely populated and relatively large geographical area. Only 4,272 residents live in the assessment area according to 1990 U.S. Census data. The bank and its ATM are located in BNA 9757, which surrounds the city of Miller. The surrounding area of Hand County is in BNA 9756.

CRA divides income levels into four categories: low, moderate, middle, and upper. Because the bank's assessment area is not in a metropolitan statistical area, the categorization of a borrower or BNA's income is determined relative to the statewide nonmetropolitan median family income. Low-income individuals have incomes of less than 50% of the statewide nonmetropolitan median family income, while moderate-income individuals have incomes of at least 50% but less than 80% of this amount. Middle-income individuals have incomes of at least 80% but less than 120% of the statewide nonmetropolitan median family income, and individuals with incomes of 120% or more of this amount are defined as upper-income individuals. According to 1990 census data, the statewide nonmetropolitan median family income is \$25,547. This figure is used to determine a BNA's income classification. The adjusted statewide nonmetropolitan median family income for 1997 is \$34,500. This figure is used to determine a borrower's income level. According to 1990 census data, the median family income for the bank's assessment area is \$22,674, which is notably less than South Dakota's nonmetropolitan median family income.

As previously mentioned, the bank's assessment area has two BNAs. BNA 9757 is a middle-income geography, and BNA 9756 is a moderate-income geography. Approximately 2,219 people, representing 52% of the assessment area's population, live in moderate-income BNA 9756. The median family income of BNA 9756 is \$20,434, which is 79.99% of the statewide nonmetropolitan median family income. At 79.99%, BNA 9756's median family income is at the top of the range for classification as moderate income. Representing 48% of the assessment area's population, 2,053 people reside in middle-income BNA 9757. The median family income in this BNA is 97.3% of the statewide nonmetropolitan median family income.

According to the 1990 U.S. Census data, the assessment area has 1,644 households and 1,213 families. Approximately 27% of the assessment area's households are low-income, 16% are moderate-income, 22% are middle-income, and 35% are upper-income. Low-income families represent 22% of the assessment area's total families. Moderate-income families make up another 21% of the assessment area's families, whereas middle- and upper-income families represent about 26% and 31% of the assessment area's families, respectively. The assessment area also has a large number of elderly residents and individuals age 17 years and younger. According to 1990 census data, these two age groups represent 48% of the assessment area's population. Typically, elderly residents and individuals under 17 years of age have little demand for credit.

The assessment area has 319 households and 162 families with incomes below the poverty level. These households and families represent approximately 19% and 13% of the assessment area's households and families, respectively. The percentage of households with incomes below the poverty level is higher in the assessment area than in South Dakota's nonmetropolitan areas. According to the census data, 18% of

the households and 14% of the families in the state's nonmetropolitan areas have incomes below the poverty level.

During the evaluation, examiners contacted a local resident who is familiar with the assessment area's economy and credit needs. Information obtained from the community contact and bank management was used in evaluating the bank's CRA performance.

Hand County has an agriculture-based economy. Local farmers raise a variety of grain crops, including spring wheat, winter wheat, soybeans, sunflowers, and corn. Livestock operations are also a significant sector of the county's economy; cows, calves, and cattle are the primary livestock commodities. According to bank management and the community contact, the assessment area's economic condition is fair. South Dakota experienced one of the most severe winters on record during this past year. Extremely low temperatures, high winds, and heavy snowfall resulted in significant cattle losses and infrastructure damage. Coupled with low beef prices, these adverse conditions negatively affected livestock producers' cash flows. During the spring of 1997, beef prices increased, somewhat alleviating livestock producers' cash flow problems. In the spring of 1997, however, the area flooded. The flooding not only caused significant damage to area roadways, but also resulted in a late spring planting season. Due to these adversities, the entire state was declared a federal disaster area. The community contact indicated that area farmers and ranchers would be applying for federal disaster relief payments through an appropriations bill targeted at livestock losses.

The bank's assessment area is served by one other financial institution, First State Bank Miller, which has its main office in Miller. Another financial institution, American State Bank, operates near the assessment area in Wessington Springs, South Dakota.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

The bank's performance in fulfilling the assessment area's credit needs is outstanding. Much of the analysis on the following pages is based on a statistical sample of 98 consumer loans and 96 small farm and business loans originated in the six months before the evaluation. The criteria detailed below were reviewed to determine the bank's CRA rating. In assigning the overall rating, the greatest weight was placed on the assessment of the bank's lending to borrowers of different income levels and to farms and businesses of different sizes in conjunction with the bank's community development activities, which include one loan, one large investment, and several services.

LOAN-TO-DEPOSIT RATIO ANALYSIS

The bank's net loan-to-deposit ratio exceeds the standards for satisfactory performance based on its consistently high level, its comparison to local competitors, and the demand for loans in the assessment area. For the period between December 31, 1995, and September 30, 1997, the bank's quarterly average net loan-to-deposit ratio is 68.8%. The following chart shows the bank's net loans and deposits since December 31, 1995.

Date	Net Loans (In thousands)	Deposits (In thousands)	Net Loan-to-Deposit Ratio
December 31, 1995	\$30,672	\$40,645	75.5%
March 31, 1996	\$27,407	\$40,707	67.3%
June 30, 1996	\$27,277	\$39,783	68.6%
September 30, 1996	\$27,291	\$40,299	67.7%
December 31, 1996	\$29,020	\$39,897	72.7%
March 31, 1997	\$25,794	\$41,620	62.0%
June 30, 1997	\$27,529	\$41,063	67.0%
September 30, 1997	\$28,185	\$40,362	69.8%

As shown above, the bank's deposits have remained stable, but net loans have fluctuated since the last evaluation. Much of the fluctuation in the size of the bank's net loan portfolio is due to the seasonal credit demands of local farmers and ranchers. However, as previously mentioned, the economic conditions of the assessment area are merely fair, and the community contact stated that credit demand declines when the local economy weakens.

As discussed in the Description of the Assessment Area section, the bank has one competitor in the assessment area. The other competitor has its main office in Wessington Springs, which is approximately 40 miles southeast of Miller. The following table shows the total assets and quarterly average net loan-to-deposit ratios for the bank and its local competitors. The quarterly average net loan-to-deposit ratios are based on ROC data for December 31, 1995, to June 30, 1997.

Bank Name	Total Assets June 30, 1997 (In thousands)	Quarterly Average Net Loan-to-Deposit Ratio
Hand County State Bank Miller, South Dakota	\$50,364	68.7%
First State Bank Miller Miller, South Dakota	\$79,384	70.2%
American State Bank Wessington Springs, South Dakota	\$68,020	64.4%

The bank's quarterly average net loan-to-deposit ratio from December 31, 1995, to June 30, 1997, is 68.7%. Although the bank is smaller than both of its local competitors, its quarterly average net loan-to-deposit ratio ranks as the second highest. As such, the bank's average net loan-to-deposit ratio appears good in relation to its competitors.

According to the Uniform Bank Performance Report ("UBPR") data, the bank's net loan-to-deposit ratio was 67.04% as of June 30, 1997. The bank's national peer group had an average net loan-to-deposit ratio of 66.24% as of the same date. The bank's ratio places it in the 51st percentile compared with its peers. The UBPR data also show that the bank's June 30, 1997, net loans-to-assets ratio was 54.66%. The average net loans-to-assets ratio for similarly sized banks in South Dakota was 60.91%. These data show that the bank commits relatively fewer assets to loans than other similarly sized banks operating in the state.

Although opportunities to extend community development loans are limited in the bank's assessment area, the bank has originated one community development loan since the last evaluation. The bank originated an interest-free loan to a local nonprofit organization that serves primarily low-income families. Given the very few opportunities to finance community development activities in the assessment area, the bank's loan origination to the nonprofit organization is highly commendable.

The bank's net loan-to-deposit ratio is good in relation to its local competitors and reasonable in relation to its national peers. The community contact indicated that there are no unmet credit needs in Hand County and could not identify any community development projects in the assessment area. However, the contact stated that the local banks are very responsive to community credit needs. For instance, Miller's banks joined to assist the county's farmers following the severe winter of 1996-1997. Their assistance included originating low-interest rate loans and extending maturity dates on existing loans. Additionally, the bank extended one community development loan since the last evaluation. For these reasons, the bank's net loan-to-deposit ratio exceeds the standards for satisfactory performance.

COMPARISON OF CREDIT EXTENDED INSIDE AND OUTSIDE THE ASSESSMENT AREA

The bank's performance in lending within its assessment area meets the standards for satisfactory performance. Examiners reviewed a sample of bank loans to determine the percentage of loans made in the assessment area. The results of the loan sample revealed that the bank makes a majority of its loans in its assessment area. The following table shows the percentage of loans by total number and total dollar amount made in the assessment area.

PERCENTAGE OF LOANS IN THE ASSESSMENT AREA		
Loan Type	Total Number of Loans	Total Amount of Loans
Consumer	72	63
Small Farm and Business	58	55

As discussed previously, the bank purchases dealer paper from several businesses. Most of the dealers from whom the bank purchases loans are located in the assessment area; however, the dealers' service areas extend beyond Hand County's borders. Since the dealers serve customers from a larger geographical area than the assessment area, the bank's loan portfolio includes numerous loans to borrowers outside the assessment area. The loan data disclosed in the table reflects the fact that the bank purchases loans from dealers who serve a larger geographical area than the bank's assessment area.

By acquiring dealer paper, the bank not only services the credit needs of the dealers' customers but also services the financial needs of the dealers. Despite the fact that the dealers serve customers from an area larger than the assessment area, the bank extends a majority of its consumer and small farm and business loans inside the assessment area. Therefore, the bank's lending meets this category's standards for satisfactory performance.

LENDING TO BORROWERS OF DIFFERENT INCOME LEVELS AND TO BUSINESSES OF DIFFERENT SIZES

The bank's level of lending to individuals of different incomes and to farms and businesses of different sizes significantly exceeds the standards for satisfactory performance. In assessing the bank's performance in this category, the greatest weight was placed on the bank's small farm and business loans because 73% of the bank's loan portfolio is agricultural credits while 12% is commercial credits.

As discussed previously, CRA classifies borrowers' incomes into four categories: low, moderate, middle, and upper. According to 1990 U.S. Census data, the assessment area's median household and family incomes are \$19,310 and \$22,674, respectively. The following table shows the percentage of consumer loans made to borrowers of different income levels.

DISTRIBUTION OF ASSESSMENT AREA LOANS BY BORROWER INCOME LEVEL*				
Loan Type	Low Income	Moderate Income	Middle Income	Upper Income
Consumer Loans				
Total Number of Loans	55%	28%	11%	6%
Total Amount of Loans	31%	47%	15%	7%
*Income level is determined based on South Dakota's 1997 nonmetropolitan median family income of \$34,500.				

The data in the table show that the bank originated 83% of its consumer loans to low- and moderate-income borrowers. The percentage of loans to low- and moderate-income individuals significantly exceeds the representation of low- and moderate-income households and families in the assessment area. Low- and moderate-income households comprise 27% and 16% of the assessment area's population, respectively. Low- and moderate-income families both represent 22% of the assessment area's population. The number and amount of bank loans to low- and moderate-income borrowers is very good relative to the representation of such households and families in the assessment area, according to the 1990 U.S. Census data. However, the community contact stated that Hand County residents are less well off financially today than seven years ago. Consequently, the U.S. Census data might understate the number of low- and moderate-income households and families in the assessment area today.

The bank originates many small-dollar-amount consumer loans that often have short terms. Bank management explained that these loans are a means to fulfill the credit needs of low- and moderate-income individuals. The high percentage of consumer loans to low- and moderate-income borrowers probably reflects the bank's willingness to extend small, short-term consumer loans. Since consumer loans comprise 12% of the bank's loan portfolio, the fact that the bank originated 83% of these loans to low- and moderate-income borrowers is very commendable.

The bank also made 98% of the sampled small farm and business loans to entities with gross annual revenues of less than \$1,000,000. The regulation defines small farm loans as agricultural credits of \$500,000 or less and small business loans as commercial credits of \$1,000,000 or less. The analysis of small farm and business loans to entities with gross annual revenues of \$1,000,000 or less indicates that 95% of the total number and 48% of the total dollar amount involved loans of \$100,000 or less. The remaining 5% of total number and 52% of the total amount involved loans with original amounts of greater than \$100,000 but less than or equal to \$1 million. As the data show, the bank's performance with respect to small farm and business loans to entities with gross annual revenues of \$1,000,000 or less is strong. However, this performance at least in part reflects that the fact that the assessment area has few, if any, large farms and businesses.

To service the credit needs of local farms and businesses, the bank offers loans through SBA, FSA, and SDDA programs. As previously discussed, the SDDA Beginning Farm Bond Program provides low-interest-rate financing for the acquisition of real property. Participation in the SBA, FSA, and SDDA programs enhances the bank's ability to service the credit needs of small farms and businesses in the assessment area.

Although the bank's small farm and business lending is strong, this performance appears to reflect the agricultural and commercial markets in the assessment area. The bank's performance with respect to extending consumer loans to low- and moderate-income borrowers is very strong. Given the bank's lending to low- and moderate-income borrowers; its willingness to extend small, short-term consumer loans; and the concentration of small farm and business loans to entities with gross annual revenues of \$1,000,000 or less, the bank's performance exceeds this category's standards for satisfactory performance.

GEOGRAPHIC DISTRIBUTION OF LOANS

The bank's lending to individuals, farms, and businesses in BNAs of different income levels meets the standards for satisfactory performance. As discussed previously, the assessment area has one moderate-income BNA and one middle-income BNA. The median family incomes in BNAs 9756 and 9757 are 79.99% and 97.3% of the statewide nonmetropolitan family income, respectively. As previously noted, BNA 9756's median family income is at the top of the range for classification as moderate income.

The bank and Miller are both located in BNA 9757. BNA 9757 is surrounded by the assessment area's moderate-income area, BNA 9756. The total population of the assessment area is 4,272; 52% of the population lives in the moderate-income BNA, and 48% lives in the middle-income BNA. The following chart shows the distribution of loans by type and BNA.

DISTRIBUTION OF LOANS BY BNA INCOME LEVEL		
Loan Type	Moderate-Income BNA	Middle-Income BNA
Consumer		
Total Number of Loans	18%	82%
Total Amount of Loans	18%	82%
Small Farm and Business		
Total Number of Loans	21%	79%
Total Amount of Loans	5%	95%
*The assessment area does not have any low- or upper-income BNAs.		

As shown in the above chart, the bank has made the majority of its consumer and small farm and business loans in the assessment area's middle-income BNA. This distribution is reasonable for several reasons. First, the bank is located in the middle-income BNA. Second, BNA 9757 represents 48% of the assessment area's population. Third, Miller is the commercial center for Hand County; consequently, most of the commercial loan demand would originate from commercial entities in the middle-income BNA. For these reasons and given the fact that the moderate-income area's median family income is 79.99%, the distribution of the bank's lending in the assessment area meets this category's standard for satisfactory performance.

INVESTMENTS

The bank has limited opportunities to make qualified community development investments as defined by Regulation BB in the assessment area. Nonetheless, the bank holds one qualified community development investment security with a value over \$850,000. By acquiring this security, the bank supported a community development project that serves the needs of low- and moderate-income people in the assessment area. In addition to the community development investment, the bank has made qualified community development donations since the last evaluation. The bank made qualified donations to a local task force; two nonprofit, service organizations; and a school.

Prior to the last evaluation, the bank made a donation to the South Dakota Community Foundation (“SDCF”) to establish the Miller Area Community Foundation (“MACF”). SDCF invested the bank’s donation, and each year 5% of the earnings are donated to Miller-area nonprofit organizations. In 1996, the MACF awarded donations to three local service organizations that serve various needs of low- and moderate-income people.

The bank’s sizable community development investment and its grant activity are particularly commendable in light of the bank’s relatively small size. Accordingly, the investment activity warrants an outstanding rating.

SERVICES

The bank has engaged in community development services since the last evaluation that further enhance its CRA performance. By organizing a monthly support program with another local financial institution, the bank helped local ranchers and farmers manage the problems caused by the severe weather conditions of the recent winter. During the monthly meetings, ranchers and farmers received financial guidance and information about managing stress.

Many bank officers and employees serve local community development organizations. One officer serves on the local economic development corporation’s board of directors. This officer is also the chairman of the development corporation’s finance committee. Using his financial expertise, the officer assists the development corporation’s programs to finance community development projects in the assessment area. Another employee serves on the board of directors for the local housing authority that manages affordable housing issues for low- and moderate-income individuals.

To service the deposit needs of low- and moderate-income people, the bank offers checking and savings accounts with no maintenance fees and very low minimum-balance requirements.

GENERAL

The evaluation did not reveal any violations of the substantive provisions of the fair lending and fair housing laws and regulations; however, it did reveal a violation of the technical provisions of Regulation B--Equal Credit Opportunity Act. Bank management promised to establish procedures to correct the violation. The bank has not received any CRA-related complaints since the last evaluation.

PUBLIC DISCLOSURE

October 28, 1997
Date of Evaluation

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

Hand County State Bank
Name of Depository Institution

094609900000
Identification Number of Institution

Miller, South Dakota
Address of Institution

Federal Reserve Bank of Minneapolis
90 Hennepin Avenue
Minneapolis, Minnesota 55480-0291

NOTE: 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.