



PUBLIC DISCLOSURE

August 30, 2004

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

**THE STATE BANK
RSSD# 502157**

**P.O. BOX 539
WINFIELD, KANSAS 67156**

**Federal Reserve Bank of Kansas City
925 Grand Boulevard
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.

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GENERAL INFORMATION

The Community Reinvestment Act (CRA) requires each federal financial supervisory agency to assess the institution's record of meeting the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound operations. Upon conclusion of each examination, the agency must prepare a written evaluation of the institution's record of meeting its community's credit needs.

This document is an evaluation of the CRA performance of The State Bank (bank), Winfield, Kansas, prepared by the Federal Reserve Bank of Kansas City (Reserve Bank), the institution's supervisory agency, as of August 30, 2004. The Reserve Bank rates the CRA performance of an institution consistent with the provisions set forth in Appendix A to 12 CFR Part 228.

Definitions for many of the terms used in this performance evaluation can be found in Section 228.12 of Regulation BB. For convenience, a "Glossary of Common CRA Terms" is attached at the end of this performance evaluation.

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

The bank has a satisfactory record of helping to meet the credit needs of its entire assessment area, in a manner consistent with its resources and capabilities. Four of the five criteria used in evaluating small bank CRA performance are relevant to this review and are as follows:

- Loan-to-Deposit Ratio;
- Lending Inside the Assessment Area;
- Lending to Borrowers of Different Income Levels and to Businesses of Different Revenue Sizes; and,
- Lending by Income Level of Geography.

The bank's responsiveness to complaints under the CRA, the fifth core criteria, was not evaluated because bank has not received any CRA complaints since the previous examination. U.S. Census Bureau Data for 2000, Dun & Bradstreet Geodemographic Data for 2003, data supplied by the Bureau of Labor Statistics, and other economic and employment data were used to develop the performance context, which assists in determining the reasonableness of the bank's lending levels and loan distribution within its assessment area (area). Interviews with members of the local community provided additional information about the area's credit needs and local financial institutions' abilities to meet those needs.

The bank's net loan-to-deposit (NLTD) ratios for the most recent eight quarters, ending March 31, 2004, were averaged to eliminate seasonal fluctuations and compared to similarly situated competitors. The remaining core criteria were evaluated based on a statistically derived sample of commercial and residential real estate loans, which represent the bank's

major products. The major products were determined through discussions with management, a review of the bank's Report of Condition and Income (Call Report), and a review of the volume of loan originations since the last CRA examination in August 1999.

Summary of Findings:

- The bank's loan-to-deposit ratio was reasonable.
- A majority of the bank's lending activity occurred within its assessment area.
- The distribution of loans to borrowers of different income levels and businesses of different revenue sizes was reasonable.
- The distribution of lending by geography was reasonable given the demographic and economic factors impacting the bank's assessment area.

DESCRIPTION OF INSTITUTION

The bank is located in Winfield, Kansas, which is the county seat of Cowley County, Kansas. Cowley County's population is 36,291 according to the 2000 U.S. Census. Cowley County is located in the south central part of Kansas, abutting Oklahoma to the south. The 2000 U.S. Census indicates the city of Winfield has a population of 11,931. The only other town with a population of more than 1,000 residents in the county is Arkansas City at 12,762. Winfield is a rural area approximately 40 miles south of Wichita, Kansas, and 14 miles north of the Oklahoma border.

The bank currently operates from three central locations in Winfield. The main office is located at 823 Main. A full-service branch is located at 321 East 10th and a drive-in facility at 121 West 9th. Deposit-taking Automated Teller Machines (ATMs) are located at the branch and drive-in facility. In addition, a cash dispensing ATM is located in the student union at Southwestern College.

Based on its financial condition, size, and product offerings, the bank has the ability to meet the credit needs of its area. The bank had total assets of \$98,566 million, with gross loans of \$51,121 million, as of the March 31, 2004 Call Report. Since the last CRA examination, total assets increased by 50 percent and net loans increased by 61 percent. The growth is attributed, in part, to the acquisition of the Commerce Bank branch in Winfield and Arkansas City in June 2002. Although the bank is predominantly a commercial and residential real estate lender, it also offers agricultural and consumer loan products. Table 1 illustrates the distribution of the bank's loan portfolio according to the March 31, 2004 Call Report.

Table 1 THE STATE BANK LOAN PORTFOLIO DISTRIBUTION		
Loan Type	Amount (\$000)	Percent of Total
Commercial	22,953	44.9
Multiple and 1- to 4-family real estate	17,785	34.8
Farmland or agricultural	5,798	11.3
Consumer	4,412	8.6
Other	173	0.4
TOTAL	51,121	100.0

No legal or financial factors exist that would hinder the bank's ability to meet the credit needs of its assessment area. The Reserve Bank last reviewed the bank's CRA performance on August 23, 1999, when a rating of Outstanding was assigned.

DESCRIPTION OF THE BANK'S ASSESSMENT AREA

The bank's assessment area consists of all of Cowley County. The area is predominately rural, comprised of two moderate- and nine middle-income tracts. The bank is located in a middle-income tract. Although a large percentage of families in the area are considered upper-income, there are a significant number of low- and moderate- income families. Census data shows that nearly 40 percent of the families in the area are upper-income, compared to 36.2 percent combined for low- and moderate-income families. In addition, the area has a higher percentage of families living below the poverty level at 9.2 percent, compared to the statewide rural area at 8.0 percent.

The area's market for banking is competitive. There are two banks headquartered in Winfield, and three banks headquartered in Arkansas City that compete for loans. Federal Deposit Insurance Corporation information from June 30, 2003 indicates that bank has a 14.5 percent market share of the deposits in Cowley County, placing it third out of eight financial institutions, and a total of nineteen offices throughout the county.

Demographic information from the 2000 U.S. Census indicates the area's unemployment rate of 7.8 percent is nearly double that of the statewide rural area at 4.4 percent. One member of the local community discussed the recent closing of a Boeing facility and its adverse consequences for the community, while another discussed the recent reopening of a packing plant as a source of economic strength. These members see the need for smaller industries to locate in Cowley County to sustain the local economy.

Although housing in the area is generally more affordable than other areas of the state, its housing stock is older. This is evidenced by a median age of housing units of 47 years, compared to the statewide rural area average of 43 years. The area's median housing value is

\$55,221, which is \$5,955 less than the statewide rural area average. The affordability of housing is measured by the affordability ratio, a figure obtained by dividing an area's median household income by its median housing value. The housing affordability ratio inside the bank's area was 61 percent, which was higher than the statewide rural areas as a whole at 56 percent. Of the area's total housing units, 63.5 percent was owner-occupied, 26.1 percent was rental units, and 10.4 percent was vacant units. Southwest College, which is located in Winfield, accounts for the majority of total persons living in group quarters at 4.2 percent.

Economic information indicates that local banks may have more difficulty penetrating the moderate-income tracts. Only 11.2 percent of the area's population resides in the moderate-income tracts. The unemployment rate in the moderate-income tracts is notably higher at 10.7 percent compared to the 7.5 percent in the middle-income tracts. Housing data for the moderate-income tracts shows that only 44 percent of the households are owner-occupied; 37.2 percent are rental units; and, the vacancy rate is double that of the middle-income tracts. Moreover, the median age of housing stock in the moderate-income tracts is 61 years, while the median age in the middle-income tracts is 45 years. Consequently, while the area's housing is more affordable, the moderate-income tracts have limited population, a higher level of unemployment, older housing stock, and a higher percentage of rental and vacant units, which may lower demand and desirability for residential real estate loans in the respective tracts.

Major employers in Cowley County include a General Electric repair center with 700 employees, the Cowley County Community College with a staff of 415, and the William Newton Hospital that employs just over 300 workers. One member of the community indicated that aviation, agriculture, and economic development play integral roles in the local economy. While the region felt some consequences of the national recession with the closing of Boeing Aviation, the community remained relatively stable. Economic development organizations also work together to promote employment opportunities in both Winfield and Arkansas City.

Overall, the community contacts emphasized that the bank and other area financial institutions make a strong effort to serve the credit needs of the community. While area banks work very well together in offering competitive lending to existing and potential small businesses in the area, they did discuss the need for more employment opportunities and affordable housing in Winfield. Table 2 provides detailed information about the area compared to the statewide rural area of Kansas.

**Table 2
ASSESSMENT AREA CHARACTERISTICS**

Tract Summary		
Total Number of Tracts	11	
Number of Moderate-Income Tracts	2	
Number of Middle-Income Tracts	9	
Income Summary		
	Area	Kansas –rural
2000 Median Family Income	\$43,511	\$42,114
Percent Low-Income Families	18.4	17.1
Percent Moderate-Income Families	17.8	19.4
Percent Middle-Income Families	24.0	25.0
Percent Upper-Income Families	39.8	38.5
Unemployment Summary		
	Area	Kansas -rural
Labor Force Population	17,815	589,117
Percent of Population in Labor Force	63.5	65.3
Percent Unemployment	7.8	4.4
Population and Housing Information		
	Area	Kansas-rural
Total Population	36,291	1,167,355
Population Change 1990 to 2000	(799)	22,709
Percentage Population Change 1990 to 2000	(6.3)	2.0
Percentage of Families Below Poverty	9.2	8.0
Percentage of Population Age 25 to 64	48.2	47.4
Percentage of Population Age 65 and Over	15.9	16.0
Total Housing Units	15,673	506,606
Percentage Owner-Occupied Units to Total Units	63.5	63.7
Percentage Rental Units to Total Units	26.1	25.6
Percentage Vacant Units to Total Units	10.4	11.0
Median Housing Value	\$55,221	\$61,176
Median Gross Rent	\$417	\$416
Housing Affordability Ratio	61.0	56.0

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

Examiners evaluated bank’s CRA performance by comparing its NLTD ratio to similarly situated financial institutions. The examination also analyzed bank’s level of loans originated inside its area; its loan distribution among borrowers of different income levels and businesses of different revenue sizes; and its distribution of loans by income level of geography. Bank’s responsiveness to CRA complaints was not evaluated because no CRA-related complaints involving the bank have been received since the previous examination. Members of the

community confirmed that financial institutions in the area adequately meet the community's credit needs.

Loan-to-Deposit Ratio

Bank's NLTD ratio is reasonable given its financial condition, economic conditions, and the credit needs of its area. Since the last examination, the bank's average NLTD ratio was 77.7 percent. Bank's loan-to-deposit ratio was impacted by an acquisition that occurred in June 2002, and over the most recent eight quarters, its NLTD average was 66.6 percent. The bank's NLTD ratio was slightly lower than the average similarly situated competitor banks, whose averages ranged from 69.4 percent to 79.8 percent. In addition, bank's NLTD average for the last eight quarters fell below both the state peer average and the national peer average of 71.2 percent and 68.6 percent, respectively.

Loans Within the Bank's Assessment Area

Based on a sample of loans reviewed during the examination, a majority of the bank's lending occurred within its assessment area. The analysis was based on a sample of 56 residential real estate loans and 46 commercial loans. By number, the bank originated 80.4 percent (45 of 56) of its residential real estate loans and 76.1 percent (35 of 46) of its commercial loans inside its area. By dollar volume, bank originated 83.7 percent of its residential real estate loans and 58.6 percent of its commercial loans inside the area. While the bank's overall performance by dollar volume is lower, more weight is afforded to the number of loans as it is a better indicator of the number of people benefiting from the loan products. Table 3 indicates the loans originated inside the assessment area.

Table 3 LOANS INSIDE THE BANK'S ASSESSMENT AREA					
Loan Type	Total Sample	Number In Area	Percent	Dollar Volume (\$000)	Percent
Residential Real Estate	56	45	80.4	2,268	83.7
Small Business	46	35	76.1	2,339	58.6
All Loans Reviewed	102	80	78.4	4,607	68.7

Distribution of Lending Among Borrowers of Different Income Levels and Businesses of Different Revenue Sizes

Residential Real Estate Loans:

The bank's lending distribution to borrowers of different income levels is reasonable. The bank made 35.6 percent (16 of 45) of the sampled residential real estate loans to low- and moderate-income borrowers. Low- and moderate-income borrowers comprise 36.2 percent of the area's families, according to 2000 U.S. Census data. Therefore, the bank's loan distribution to low- and moderate-income borrowers closely mirrors the area's demographics. Table 4 indicates the distribution of bank's real estate loans by borrower income level.

Table 4		
DISTRIBUTION OF RESIDENTIAL REAL ESTATE LOANS BY BORROWER INCOME LEVEL		
Area Median Family Income*		\$43,511
Income Level of Borrower	Percent of Residential Real Estate Loans Reviewed	Percent of Families Within Assessment Area**
Low (<50 percent of median)	17.8	18.4
Moderate (50 to <80 percent of median)	17.8	17.8
Middle (80 to <120 percent of median)	20.0	24.0
Upper (=>120 percent of median)	44.4	39.8
Totals	100.0	100.0

* Area Median-Family Income is based on the 2003 HUD estimated median family income.

**The percentage of families in Assessment Area is based on 2000 Census data.

Small Business Loans:

The bank's lending to small businesses is also reasonable. Of the sampled business loans originated inside the bank's assessment area, 88.6 percent (31 of 35) were made to businesses with revenues under \$1 million. According to Dun & Bradstreet Business Geodemographic Data for 2003, 89.1 percent of the area's businesses were small. Moreover, bank made 85.7 percent (30 of 35) of its loans to small businesses in amounts of \$100M or less, which are amounts typically needed by small businesses. The bank's small business lending activity reflects its recognition of the need for small-dollar business credit and its commitment to meeting the needs of numerous small retail and service-oriented businesses in

the assessment area. The bank also provides flexible lending practices through its participation in government-insured loan programs, such as the SBA, Farm Service Agency, the Cowley County Economic Development Agency (CCEDA), and the state of Kansas totaling over \$2,240,000. Members of the community confirmed that local financial institutions are meeting the credit needs of small businesses. Tables 5 and 6 illustrate the lending distribution by business revenue and loan size.

Table 5 LENDING DISTRIBUTION BY BUSINESS REVENUE SIZE					
Size of Small Business	Loans by Number	% of Loans	Dollar Volume (\$000s)	% of Loans by Dollar Volume	% of Businesses in Area
Revenues <= \$1 million	31	88.6	1,461	62.4	89.1
Revenues > \$1 million	4	11.4	879	37.6	8.6
Not Reported	0	0	0	0	2.3
Grand Total	35	100.0	2,340	100.0	100.0

Table 6 Distribution of Small Business Originations by Loan Size				
Loan Size	Number	Percent	Dollar Amount (\$000)	Percent
\$0 - \$100M	30	85.7	722	30.9
>\$100M to <= \$250M	3	8.6	464	19.8
> \$250M to <= \$1,000M	2	5.7	1,153	49.3
Grand Total	35	100.0	2,339	100.0

Distribution of Lending Among Geographies of Different Income Levels

Residential Real Estate Loans:

Although residential real estate lending in moderate-income geographies is weak, the bank's geographic distribution of loans was considered reasonable given the area's economic and demographic factors. The bank's performance was compared to the percentages of owner-occupied housing in the assessment area tracts. All of the bank's residential real estate loan originations in the sample were in middle-income tracts; however, 91.5 percent of the area's owner-occupied housing units were located in those tracts. In addition, limited lending opportunities, strong competition in Arkansas City, and the distance from the bank's facilities impact the bank's ability to lend in the moderate-income tracts.

Small Business Loans:

The bank's small business lending in the moderate-income tracts reflects some penetration and is considered reasonable, given economic and demographic factors and strong competition in the area. The bank originated 2.9 percent of the sampled business loans in the area's moderate-income tracts. According to Dun & Bradstreet Geodemographic Data for 2003, 18.9 percent of the area's businesses are located in the moderate-income tracts. Bank management indicated that the availability of desirable small business lending in the moderate-income tracts is limited.

COMPLIANCE WITH ANTIDISCRIMINATION LAWS AND REGULATIONS

The bank is in compliance with the substantive provisions of the antidiscrimination laws and regulations. A review of bank policies, credit applications, loans, denials, and interview procedures revealed no prohibited practices designed to discourage loan applicants.

GLOSSARY OF COMMON CRA TERMS

(For additional information, please see the Definitions section of Regulation BB at 12 CFR 228.12.)

Assessment Area – The geographic area(s) delineated by the bank and used in evaluating the bank’s record of helping to meet the credit needs of its community. The assessment area must include the geographies where the main office, branches, and deposit-taking automated tellers machines are located. The assessment area must consist only of whole geographies, may not reflect illegal discrimination, and may not arbitrarily exclude low- or moderate-income geographies.

Block Numbering Areas (BNAs) – BNAs are geographic entities similar to census tracts. Metropolitan areas are most often delineated into census tracts, while rural areas are delineated into BNAs.

Census Tracts – Census tracts are small, relatively permanent geographic entities within counties delineated by a committee of local data users. Generally, census tracts have between 2,500 and 8,000 residents and boundaries that follow visible features.

Community Development – Includes affordable housing (including multifamily rental housing) for low- and moderate-income individuals, community services targeted to low- and moderate-income individuals, activities that promote economic development by financing businesses or farms that have gross annual revenues of \$1 million or less, or activities that revitalize or stabilize low- or moderate-income geographies.

Community Development Loan – A loan that has community development as its primary purpose and (except in the case of a wholesale or limited-purpose bank).

1. Has not been reported or collected by the bank or an affiliate as a home mortgage, small business, small farm, or consumer loan, unless it is a multifamily dwelling loan and
2. Benefits the bank’s assessment area(s) or a broader statewide or regional area that includes the bank’s assessment area(s).

Community Development Service – A service that has as its primary purpose community development, is related to the provision of financial services, has not been considered in the evaluation of the bank’s retail banking services, benefits the banks assessment area(s) or a broader statewide or regional area that includes the bank’s assessment area and has not been claimed by other affiliated institutions.

Consumer Loans – Loans to individuals for household, family and other personal expenditures. These loans do not include real estate-secured loans.

Dun & Bradstreet Data – Data collected by Dun & Bradstreet regarding types of businesses and their respective gross annual revenues. The data can be sorted by geographies.

Geography – A census tract or a block numbering area.

Income Level – Both geographies and individuals can be described in terms of their income levels. In MSAs, the level is based on the MSA median income. In nonMSA areas, the level is based on the statewide, nonMSA median income.

Low-Income – Less than 50 percent of the area median income

Moderate-Income – At least 50 percent and less than 80 percent of the area median income

Middle-Income – At least 80 percent and less than 120 percent of the area median income

Upper-Income – At least 120 percent or more of the area median income

Metropolitan Statistical Area (MSA) - The general concept of an MSA is that of a core area containing a large population nucleus, together with adjacent communities having a high degree of economic and social integration with that core. Generally, a single city with at least 50,000 inhabitants or an urbanized area with a total population of at least 100,000 would meet the definition of an MSA.

Qualified Investment – A lawful investment, deposit, membership share or grant that has as its primary purpose community development.

Small Business – A business with gross annual revenues of \$1 million or less.

Small Business Loan – A loan with an original amount of \$1 million or less that has been reported in the Consolidated Report of Condition and Income in the category “Loans secured by nonfarm nonresidential properties” or “Commercial and industrial loans.”

Small Farm – A farm with gross annual revenues of \$1 million or less.

Small Farm Loan – A loan with an original amount of \$500,000 or less that has been reported in the Consolidated Report of Condition and Income in the category “Loans secured by farmland” or “Loans to finance agricultural production and other loans to farmers.”