



SMALL BANK

Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

PUBLIC DISCLOSURE

March 19, 2012

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

First National Bank of Bosque County
Charter Number: 13675

P.O. Box 278
Valley Mills, TX 76689

Office of the Comptroller of the Currency
Southern District
San Antonio – North Field Office
10001 Reunion Place, Suite 250
San Antonio, Texas 78216

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 the safe and sound operation of the institution. This evaluation is not, nor should it be construed as, an assessment of the financial condition of this institution. The rating assigned to this institution does not represent an analysis, conclusion, or opinion of the federal financial supervisory agency concerning the safety and soundness of this financial institution.

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

The performance under the Community Reinvestment Act (CRA) for the First National Bank of Bosque County (FNB) reflects an overall satisfactory level in meeting the community's credit needs within its assessment areas (AAs). This rating is based on findings noted through analysis of the lending test performance factors relative to the "Small Bank" evaluation criteria. The following summarizes the bank's performance:

- FNB demonstrates good lending performance. The bank's loan-to-deposit (LTD) ratio has averaged 61% during the evaluation period and compares favorably with the local peer bank average of 52%.
- A substantial majority of FNB's loans have been made within its AA. Our sample indicated that 79% of the bank's loans are made within its AA.
- FNB demonstrates a reasonable distribution of loans to borrowers of different income levels and businesses of different sizes.
- There have been no complaints with respect to FNB's CRA performance.

SCOPE OF EXAMINATION

We performed a small bank CRA examination of FNB of Bosque County, using financial data as of December 31, 2011. The examination included an evaluation of the characteristics and appropriateness of FNB's delineated AAs and a review of its financial condition and ability to provide credit and other services in its AAs. We evaluated the record of lending in its AAs for the period from January 2008 through December 31, 2011. Our analysis of lending performance included all residential lending activity during the evaluation period. We also sampled commercial loans to assess lending to small businesses. Your external auditors tested the Home Mortgage Disclosure Act (HMDA) register for data integrity of HMDA reports, and found no significant errors. These reports were utilized for our analysis.

DESCRIPTION OF INSTITUTION

FNB is a \$100.6 million community bank headquartered in Valley Mills, Texas, which is 25 miles west of Waco, Texas. FNB has three branch offices located within 20 miles of the main office. One branch is located in Clifton, Texas, approximately 10 miles Northwest of Valley Mills in Bosque County. This office was established in June 1990. The second branch is located in Meridian, Texas, which is 10 miles farther Northwest of Clifton. This branch was established in December of 2005. The third branch - "The Ranch House" - is located in McLennan County, between Valley Mills and Waco, Texas. The Ranch House branch opened in June 1995. FNB also has three automated teller machines (ATMs) located throughout both AAs. However, these ATMs do not accept deposits. FNB is 100% owned by a one-bank, locally owned holding company, Valley Mills Financial Corporation.

The loan portfolio comprises 53% of total assets. The LTD ratio is 59.1%, as of December 31, 2011. Lending products include residential real estate, commercial, and consumer loans. The table on the following page details the breakdown of FNB's loan portfolio as of December 31, 2011.

Loan Type	Dollar Amount \$ (000)	% of Total Loans (Dollar Amount)
Real Estate Residential (1-4)	\$19,505	36%
Commercial and Industrial	\$9,130	17%
Consumer	\$8,593	16%
Commercial Real Estate	\$4,950	9%
Agricultural Loans	\$3,689	7%
Construction & Land Development Loans	\$3,988	8%
Farmland Loans	\$3,984	7%
Other	\$141	0%
Total	\$53,980	100%

Source: December 31, 2011 Report of Condition

No legal impediments or other factors hinder the bank's ability to provide credit. Based on its financial condition, the stable local economy, product offerings, and competition, FNB has the ability to meet the various credit needs in its community. The prior rating of CRA performance for FNB in December 2007 was "Satisfactory."

DESCRIPTION OF ASSESSMENT AREA(s)

FNB has two AAs. One consists of all the census tracts in Bosque County and the second, located within the Waco Metropolitan Statistical Area (MSA), consists of five census tracts. These census tracts are in the western part of McLennan County and include part of the west side of Waco, Texas.

Bosque County Assessment Area

This AA includes two upper-income and five middle-income tracts located in Bosque County. Based on the 2000 Census data, the AA has a population of 17,204. According to the housing data as provided in the Census, there are 6,711 housing units in this area. The AA in Bosque County is a predominately middle-income area, but it is a relatively higher income area compared to other rural areas of Texas. Income information from the 2000 United States Census reveals that the median family income (MFI) for this area is \$40,992. For all non-MSAs in Texas, this was \$35,800 in 2001.

DEMOGRAPHIC AND ECONOMIC CHARACTERISTICS OF BOSQUE COUNTY ASSESSMENT AREA	
Population	
Number of Families	4,869
Number of Households	6,711
Geographies	
Number of Census Tracts	7
% Low-Income Census Tracts	0%
% Moderate-Income Census Tracts	0%
% Middle-Income Census Tracts	71%
% Upper-Income Census Tracts	29%
Median Family Income (MFI)	
2000 MFI for AA	\$40,992
2011 HUD-Adjusted MFI	\$48,600
2010 HUD-Adjusted MFI	\$46,500
2009 HUD-Adjusted MFI	\$45,600
Economic Indicators	
Unemployment Rate	2.85%
2011 Median Housing Value	\$59,109
% of Households Below Poverty Level	13.99%

Source: 2000 Census Data; Department of Housing and Urban Development

Waco Assessment Area

This AA includes one middle-income and four upper-income census tracts, which are part of the Waco MSA in McLennan County. Based on 2000 Census data, the AA has a population of 17,942. According to the 2000 housing data provided in the Census, there are 6,856 households. The MFI level for the Waco MSA is \$51,731. Specific demographic data for FNB's sole AA, McLennan County, is detailed on the table below.

DEMOGRAPHIC AND ECONOMIC CHARACTERISTICS OF MCLENNAN COUNTY ASSESSMENT AREA WACO MSA	
Population	
Number of Families	5,010
Number of Households	6,856
Geographies	
Number of Census Tracts	5
% Low-Income Census Tracts	0%
% Moderate-Income Census Tracts	0%
% Middle-Income Census Tracts	20%
% Upper-Income Census Tracts	80%
Median Family Income (MFI)	
2000 MFI for AA	\$51,731
2011 HUD-Adjusted MFI	\$54,000
2010 HUD-Adjusted MFI	\$51,900
2009 HUD-Adjusted MFI	\$51,700
Economic Indicators	
Unemployment Rate	1.67%
2011 Median Housing Value	\$82,760
% of Households Below Poverty Level	11.38%

Source: 2000 Census Data; Department of Housing and Urban Development

Local economic conditions reflect steady growth in population and economic activity in both AAs. FNB’s competitors include numerous financial institutions such as national and state chartered banks and credit unions serving both AAs. We contacted a local economic development official to obtain additional information about local communities. Our conversation did not reveal a shortage of lending services within the AA.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

Loan-to-Deposit Ratio

FNB's LTD ratio of 59.06% as of December 31, 2011, is reasonable considering the bank's performance context, which includes its capacity to lend, market competition, demographic and economic factors, and lending opportunities available in the AAs. The average LTD ratio over the last 17 quarters of 61.17%, covering the time since the prior CRA examination, is also reasonable. The quarterly LTD ratio has ranged from a low of 56.79% at December 31, 2008, to a high of 63.51% at September 30, 2010. We compared average LTD ratios between FNB and five similarly situated banks in the chart below. As illustrated in the table below, FNB's average LTD ratio is second highest on the list and compared favorably with the peer average of 51.83% for the same time period.

<i>Institution</i>	<i>Assets As Of December 31, 2011</i>	<i>Average LTD Ratio %</i>
First National Bank, McGregor	\$117,587	96.61%
<i>FNB of Bosque County</i>	<i>\$100,558</i>	<i>61.17%</i>
First National Bank, Moody	\$45,176	57.12%
First Security State Bank, Cranfills Gap	\$91,282	45.11%
Pointwest Bank, West	\$80,859	36.28%
The State National Bank in West, West	\$60,680	24.01%

*Source: Institution Consolidated Reports of Condition *As of December 31, 2011*

Lending in Assessment Area

A substantial majority of FNB's loans are made within its AAs, therefore exceeding the standard for satisfactory performance under this criterion. Assessing performance of this area included analyzing the number and dollar amount of 1-4 family residential loans reported on the HMDA Loan Application Register (LAR) between 2008 and 2011. Additionally, we reviewed a sample of 40 commercial loans extended since the prior CRA examination to make this determination.

As illustrated in the following table, our analysis of both home and commercial lending showed that FNB originated 79% by number and 76% by dollar amount within its defined AA. This included both MSA and non-MSA AAs.

Table 1 Lending in Assessment Area								
LOAN TYPE	In Assessment Area				Out of Assessment Area			
	#	%	\$ (000s)	%	#	%	\$ (000s)	%
Home Purchase	79	75.24	\$4,974	71.06	26	24.76	\$2,026	28.94
Home Improvement	44	81.48	\$1,468	85.1	10	18.52	\$257	14.9
Home Refinance	38	82.61	\$2,858	75.57	8	17.39	\$924	24.43
Commercial	32	80	\$2,488	82.79	8	20	\$517	17.21
Total Reviewed	193	78.78	\$11,788	75.99	52	21.22	\$3,724	24.01

Source: Data reported under HMDA; Commercial loan sample

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

Overall, the bank demonstrates satisfactory loan penetration among businesses of different sizes and borrowers of different income levels. Our analysis found some areas indicate excellent penetration, while others demonstrate satisfactory penetration. The results of our assessment of borrower distribution weighed more heavily on FNB's CRA performance since its AAs do not include any low- or moderate-income (LMI) geographies.

We assessed FNB's performance under this criterion by utilizing HMDA/LAR information for residential mortgage loans originated or purchased between 2008 and 2011. We also included samples of loans to businesses, 2000 Census data, and Dun and Bradstreet data. The tables below summarize lending dispersion among the various levels of income or revenue for individuals or businesses, respectively, for each of the bank's AAs.

Our analysis of residential mortgage loans made to borrowers within the Bosque County AA indicated reasonable loan penetration among all income categories including LMI. According to Census demographic information, approximately 14% of families are considered below poverty level. As illustrated below, HMDA data indicated that residential real estate lending to low-income borrowers was below AA demographics. However, residential real estate lending to moderate-income borrowers compared favorably with AA demographics, particularly number of loans originated - *approximately 20%*.

Table 2 Borrower Distribution of Residential Real Estate Loans in Bosque County Assessment Area								
Borrower Income Level	Low		Moderate		Middle		Upper	
% of AA Families	15.75%		17.15		21.61		45.49	
	% of # of Loans	% of Amount	% of # of Loans	% of Amount	% of # of Loans	% of Amount	% of # of Loans	% of Amount
Total	4.13	1.43	19.83	12.59	19.01	12.94	52.07	62.63

Source: Data reported under HMDA; U.S. Census Data

We found similar performance in the AA located in the Waco MSA. According to Census demographic information, approximately 11% of families are considered to be below poverty level. Based on the HMDA and Census data for residential mortgage loans, lending to moderate-income borrowers was above AA demographics. Meanwhile, lending to low-income borrowers was below AA demographics.

Table 2A Borrower Distribution of Residential Real Estate Loans in Waco-MSA Assessment Area								
Borrower Income Level	Low		Moderate		Middle		Upper	
% of AA Families	14.03%		11.96%		20.56%		53.45%	
	% of # of Loans	% of Amount	% of # of Loans	% of Amount	% of # of Loans	% of Amount	% of # of Loans	% of Amount
Total	7.50	4.92	17.5	12.04	20.00	22.01	55.00	61.03

Source: Data reported under HMDA; U.S. Census Data

We considered FNB’s capacity to lend, market competition, economic factors, and lending opportunities available in the AAs. This allowed us to determine reasonable loan penetration related to residential mortgage lending among all income categories including LMI.

The following two tables summarize the results of our commercial loan sample. Our sample consisted of 40 commercial loans; 20 for each AA. The analysis included a sample of loans originated during 2008 through 2011 to determine level of distribution among businesses of different sizes. FNB originated a satisfactory number of commercial loans to small businesses. This demonstrated reasonable penetration under this performance criterion for both AAs. Small businesses are defined as having annual gross revenues of \$1 million or less.

Table 2B Borrower Distribution of Loans to Businesses in Bosque Co AA				
Business Revenues (or Sales)	≤\$1,000,000	>\$1,000,000	Unavailable/ Unknown	Total
% of AA Businesses	70.23%	1.78%	27.99%	100%
% of Bank Loans in AA by #	80.00%	20.00%	0.00%	100%
% of Bank Loans in AA by \$	1,443,558	135,686	0.00%	100%

Source: Commercial loan sample; Dun and Bradstreet data

Table 2C Borrower Distribution of Loans to Businesses in Waco-MSA				
Business Revenues (or Sales)	≤\$1,000,000	>\$1,000,000	Unavailable/ Unknown	Total
% of AA Businesses	73.08%	1.62%	25.30%	100%
% of Bank Loans in AA by #	60.00%	40.00%	0.00%	100%
% of Bank Loans in AA by \$	734,380	692,056	0.00%	100%

Source: Commercial loan sample; Dun and Bradstreet data

Geographic Distribution of Loans

As previously mentioned, FNB's defined AAs consist of only middle- and upper-income census tracts. Therefore, an analysis of loan distribution by geographic area would not be meaningful at this time.

Responses to Complaints

FNB received no complaints relating to its performance under the CRA.

Fair Lending or Other Illegal Credit Practices Review

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