



Comptroller of the Currency
Administrator of National Banks

SMALL BANK

PUBLIC DISCLOSURE

June 4, 2001

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

**Bay Cities National Bank
Charter Number 22654**

**1333 South Pacific Coast Highway
Redondo Beach, CA 90277**

**Comptroller of the Currency
Southern California North Field Office
550 North Brand Boulevard Suite 500
Glendale, CA 91203**

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 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 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 **Bay Cities National Bank** prepared by **The Office of the Comptroller of the Currency (OCC)**, the institution's supervisory agency, as of **June 4, 2001**. The agency rates the CRA performance of an institution consistent with the provisions set forth in Appendix A to 12 C.F.R. Part 25.*

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

Bay Cities National Bank has a satisfactory record of meeting credit needs within the community. The following supports this rating:

- The geographic distribution of loans is satisfactory.
- The bank originates loans to borrowers of different income levels and businesses of different sizes. The distribution of loans is consistent with the assessment area demographics.
- A majority of loans have been originated within the bank's assessment area.
- The loan-to-deposit ratio meets the standards for a satisfactory rating.
- The bank complies with the provisions of the antidiscrimination laws and regulations.
- The bank has received no written complaints associated with its CRA performance.

DESCRIPTION OF INSTITUTION

Founded in 1982, Bay Cities National Bank (“BCNB” or “the bank”) is an independent commercial bank headquartered in Redondo Beach, California, 25 miles southwest of downtown Los Angeles. BCNB is held by a single bank holding company, Peninsula Banking Group (PGB), which is, in turn, 90 percent owned by Community First Financial Group (CFFG). CFFG is a multi-bank holding company based in English, Indiana with reported assets of \$354 million as of December 31, 2000. CFFG also owns two other banks in Indiana.

BCNB operates three branches: the main office in Redondo Beach, a branch in downtown San Pedro and a branch in the suburban shopping center in the city of Rolling Hills. A fourth branch is approved, and it will open on July 9, 2001, in the new Information Technology Center in Redondo Beach. The offices provide various credit and deposit products and services to consumers and small businesses. The bank has extended operating hours Fridays and Saturdays and the branches are readily accessible to customers throughout the assessment area. Each branch has an Automated Teller Machine (ATM). The 24-hour ATMs allow customers to transfer funds, deposit money, make balance inquiries, and withdraw money. There were no branch openings or closings since the previous CRA examination.

We rated the bank’s CRA performance “Satisfactory” at our last evaluation, dated February 21, 1997. BCNB’s has no financial or legal impediments that will affect its ability to help meet the credit needs of its assessment area. As of the bank’s March 31, 2001 general ledger, it has \$155 million in assets, \$141 million in deposits and \$10 million in shareholders equity.

BCNB is a business-oriented bank that primarily focuses on lending to small businesses, professionals and developers of commercial property. The bank participates in the Small Business Administration’s (SBA) “7(a) Loan Guaranty Program” and “Low Doc” loan programs for small business. Competition for loans and deposits remains strong from local branches of large money center banks and other financial institutions. The combined business portfolio accounts for 92 percent of the bank’s loans outstanding. Although consumer loans are a smaller part of the loan portfolio, we also reviewed them as the next largest loan type, to help determine the bank’s overall lending performance. As of March 31, 2001, net loans represented 53 percent of total assets. Table 1 shows the composition the loan portfolio as of March 31, 2001.

LOAN PORTFOLIO COMPOSITION (Dollars outstanding as of March 31, 2001)		
Loan Type	Volume (\$000’s)	% \$ Volume
Commercial Real Estate	48,867	59%
Commercial / Industrial	10,530	13%
Multifamily Real Estate	9,146	11%
SBA Loans	7,450	9%
Residential Real Estate	4,635	5%
Consumer	1,516	2%
Other	837	1%
Total	82,981	100%

Table 1

DESCRIPTION OF THE SOUTH BAY ASSESSMENT AREA:

BCNB's assessment area is located in the southwest sector of the Los Angeles Metropolitan Statistical Area. This area is commonly known as "The South Bay." The assessment area encompasses the cities of Rolling Hills, Rolling Hills Estates, Palos Verdes Estates, Rancho Palos Verdes, and parts of the cities of Redondo Beach, Manhattan Beach, Hermosa Beach, Torrance, Lomita, and San Pedro. The Palos Verdes peninsula is a bedroom community characterized by its attractiveness to high net worth individuals and professionals. It is considered to be one of the most affluent communities in the country. The community's major employment sectors are business and professional services (including software development and international trade services), health services, retail trade, manufacturing, and motion picture and television production. Major employers include Boeing, Computer Sciences Corp., Hughes Electronics Corp., Mattel Inc., and Merisal Inc. The assessment area meets the requirements of the regulation and does not arbitrarily exclude low- and moderate-income geographies.

The assessment area is comprised of 82 contiguous census tracts. The following table details the number and percentage of census tracts by income level within the bank's assessment area.

Assessment Area Characteristics				
Income Level	Number of Census Tracts	Percent of Total Census Tracts	Number of Families	Percentage of families
Low	1	1%	1,413	1%
Moderate	3	4%	3,386	3%
Middle	15	18%	19,840	19%
Upper	62	76%	81,289	77%
N/A*	1	1%	0	0
Total	82	100%	105,928	100%

Table 2

**1990 Census reported no income and no families residing in this tract*

The 1990 Census reported a total population of 408,000 within the assessment area. The 2000 population of the assessment area is estimated at over 500,000. A strong economy and job market contributed to the increase in population. The U.S. Bureau of Labor Statistics estimated the 1999 unemployment rate at 2.2 percent, well below the national average of 4.3 percent. The updated Department of Housing and Urban Development (HUD) median family income for these census tracts was \$62.5 thousand, and the 1990 median housing value was \$371 thousand.

We reviewed four recent community contacts performed by the OCC, the FDIC, and Federal Reserve Bank. We also performed one new community contact with a local economic development partnership. The contacts we reviewed included organizations that promote small business development and affordable housing. One of the contacts stated that there are no credit needs that have not been satisfied by the area's financial institutions at this time. However, smaller loan amounts up to \$500 thousand are most often needed for many small businesses in the area. Another community contact indicated that availability of capital is not the primary concern. Rather, it is how to access capital that needs attention. More pre-qualification and technical assistance to educate applicants on the process of preparing loan applications is needed. Another commenter indicated that the increased use of credit scoring systems has an adverse impact on clients seeking loans, since the cut-off scores are often set too high. They

would like to see more local lenders participate in SBA programs available to small business owners.

CONCLUSIONS ABOUT PERFORMANCE CRITERIA

Geographic Distribution of Loans

- The geographic distribution of loans to businesses is satisfactory.

The distribution of loans among the geographies meets the standard for satisfactory performance. We did not identify any gaps in the bank’s loan distribution.

We reviewed 207 business loans made over the past two years to determine their distribution in the bank’s assessment area. The business loan originations showed that the distribution reasonably reflects the demographics of the area. Although the number and volume of loans in low- and moderate-income areas was low, the percent of businesses located in these tracts was similarly low. Of the total business loans made in 1999 and 2000, approximately 4 percent (by number) and 3 percent (by dollar) of the originations were to borrowers residing in low- and moderate-income census tracts. The small size of the bank, combined with its limited branch network, limits the bank’s ability to equally serve its entire assessment area. Despite this limitation, in 1999 the bank originated loans in all four of the low- and moderate-income tracts. In 2000, they originated loans in all four of these tracts in one of the four quarters.

Table 3 reflects the distribution of all business loans by census tract.

Distribution of Business Loans by Census Tract Income Level					
Income Level of Tract	% of Businesses in AA	Business Loans			
		Number	Percent	\$000	Percent
Low-Income	1%	5	2.4%	1,002	2.2%
Moderate-Income	4%	3	1.4%	111	0.3%
Middle-Income	18%	43	20.8%	3,842	8.6%
Upper-Income	76%	156	75.4%	39,667	88.9%
N/A*	1%	-	-	-	-
Total	100%	207	100%	44,642	100%

Table 3

** 1990 census reported no income and no families living in this tract.*

We also reviewed 114 consumer loans made over the same two-year period. Table 4 shows approximately the same geographic distribution patterns as for the business loans. While the bank’s primary focus involves business lending, they do occasionally grant consumer loans, primarily to depositors, or as an accommodation to principals or employees of the bank’s business customers. Additionally, the bank has chosen not to emphasize residential mortgages or home improvement loans. Consequently, they only granted four home improvement loans and one residential refinance loan over the past three years. Competition for residential loans is very strong in the South Bay area, and the bank does not have the resources to participate in this specialized market. While there were no consumer loans made during the review period in the

one low-income census tract, this tract comprises a very small percentage of the families living in the entire assessment area. Moreover, a portion of the tract is adjacent to the Port of Los Angeles, which includes heavy industrial sites, shipping terminals, and undeveloped land. Loan opportunities in the low- and moderate-income census tracts are limited. These tracts contain only 1.7 percent of owner occupied housing, and 7.8 percent of renter occupied housing, compared to 98.3 percent and 92.2 percent respectively, for the middle and upper income tracts.

Distribution of Consumer Loans by Census Tracts for 1999-2000						
Income Level of Tract	Number of families	Percent of Families	Number of Loans	Percent of Loans	\$000	Percent of Loans
Low-Income	1,413	1%	0	0	0	0
Moderate-Income	3,386	3%	4	3.5%	56	2.9%
Middle-Income	19,840	19%	21	18.4%	208	10.7%
Upper-Income	81,289	77%	89	78.1%	1,686	86.4%
N/A*	0		0			
Total	100%	100%	114	100%	1,950	100%

Table 4

** 1990 Census reported no income and no families residing in this tract.*

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

- The distribution of loans to businesses of different sizes is satisfactory. The distribution of loans to consumers of different incomes is below demographics, but is adequate since this is not the bank's primary lending focus.

Based on data collected by the bank, distribution of loans is measured by two product types, business loans and consumer. Since the dominant lending activity is in business loans, we focused on lending to businesses of different sizes.

Management provided us with information on business loans originated in the assessment area for the eight quarters beginning January 1, 1999, to December 31, 2000. This is representative of BCNB's lending activity since the last CRA examination in February 1997. Of the 207 business loans originated since January 1999, the bank granted a majority of the number of loans and dollar amount of loans to those businesses with gross annual revenues of less than \$1 million. Table 5 shows the percentage of loans made to businesses under and over the \$1 million threshold.

Lending to Businesses Based of Revenue Size of Business					
Gross Revenue Size	% of Businesses in assessment area	Business Loan Originations			
		Number	Percent	\$000	Percent
≤\$1 Million*	78%	127	61%	26,777	60%
>\$1 Million	17%	80	39%	17,844	40%
Total	95% **	207	100%	44,620	100%

Table 5

** Represents "Small business loans", loans to a business with annual revenues of \$1 million or less*
*** Five percent of businesses in the assessment area did not report income information*

The percentage of loans to businesses with revenues of less than \$1 million is somewhat lower than the business demographics of the area. However, we considered that BCNB's performance is reasonable in view of the bank's small size, and the extensive competition in the local market. Additionally, the size of loans made to businesses shows that the bank supports smaller businesses with small loan requirements. Very small business loans were identified as an area of need by one of our community contacts. As shown in Table 6, over the last eight quarters, 60 percent of business loans made to firms with revenues of less than \$1 million were made in amounts of \$100 thousand or less. And, another 20 percent of the number of loans were made in amounts between \$100 thousand and \$250 thousand. Table 6 depicts the overall distribution of small business loans made within the assessment area over the past two years.

Loan Size Analysis by Number of Loans							
Year	Business Loans	Number ≤\$100,000	% of Loans ≤\$100,000	Number \$100,000 to \$250,000	% of loans \$100,000 to \$250,000	Number \$250,000 to \$1 Million	% of loans \$250,000 to \$1 Million
1999	117	60	51%	28	24%	23	20%
2000	90	65	72%	14	16%	7	8%
Total	207	125	60%	42	20%	30	15%

Table 6

Lending in Assessment Area

- The bank's level of lending within its assessment area meets the standard for satisfactory performance.

BCNB originated the majority of its loans by number and dollar amount within its assessment area. The loans reflected in the table below include all loans originated by BCNB between April 1, 1997, and December 31, 2000. All of this data was collected by the bank and tabulated by its consultant. Table 7 shows loan distribution in and out of BCNB's assessment area.

Total Loans Originated Within the Assessment Area		
Total Loans by Number and Dollars (\$000)	Number and Dollar Amount (\$000) Within Assessment Area	Percent of Total Loans Made Within Assessment Area
839	597	71%
\$134,510	\$81,792	61%

Table 7

In order to determine the distribution of the bank's primary loan product, business lending, we reviewed a random sample of 92 business loans made between April 1, 2000 and September 30, 2000. The sample reasonably correlates with the actual data for total loans made since the last examination. Although the bank's lending within the assessment area meets the standard for satisfactory performance, the numbers are low. Several factors contribute to this lower than expected lending performance.

- Over 50 percent of SBA loans were made outside the assessment area.

Management provided us with information on SBA loans originated since 1999. The data shows that of the 25 loans funded aggregating \$3.9 million, nearly half (by number) and 63 percent by dollar amount were made outside the bank’s assessment area. Also, two of the loans totaling \$993 thousand outside the area were in low- and moderate-income areas. Further investigation showed that nearly all of the subject businesses are domiciled in the South Bay area, but they lie just outside the demarcation line of several BCNB census tracts. Two of the businesses are in Lawndale, two in Torrance, and one each in Carson, Gardena, Hawthorne, Westchester, and Wilmington. Each of these businesses is within two miles or less from the bank’s assessment area boundary. Most of these customers have established bank accounts with BCNB. We also found that a number of the small business loans made outside the assessment area follow the same pattern as the SBA loans.

- Geographical makeup of the South Bay region.

In the South Bay, virtually all of the cities run together, and other than major arterials or freeways, there are few physical boundaries between cities. The bank seeks to market to customers within the assessment area, and it does not use loan brokers to attract SBA loans. However, BCNB advertises in SBA publications, which sometimes results in SBA referrals of businesses that are located just outside the bank’s assessment area. Additionally, BCNB is one of only a few community banks in the area providing start up loans, under the SBA “Low Doc” loan program. This capability also results in occasional loan applications from outside the area. Over the last nine quarters, the bank has only granted three SBA loans to borrowers domiciled more than 10 miles away from the bank’s headquarters. These were in Santa Monica, Pacific Palisades and Long Beach. Community contacts indicate that the South Bay is considered within the marketing territory of these three cities. The SBA referred all of these loans based on BCNB’s lending capabilities. The following table shows the distribution inside and outside the assessment area for business loans only.

Sample of Business Loans Originated Within the Assessment Area April 1 - September 30, 2000		
Total Business Loans by Number and Dollars (\$000)	Number and Dollar Amount (\$000) Within the Assessment Area	Percent of Total Loans Made Within Assessment Area
92	59	64%
\$16, 411	\$10,105	62%

Table 8

Loan-to-Deposit Ratio

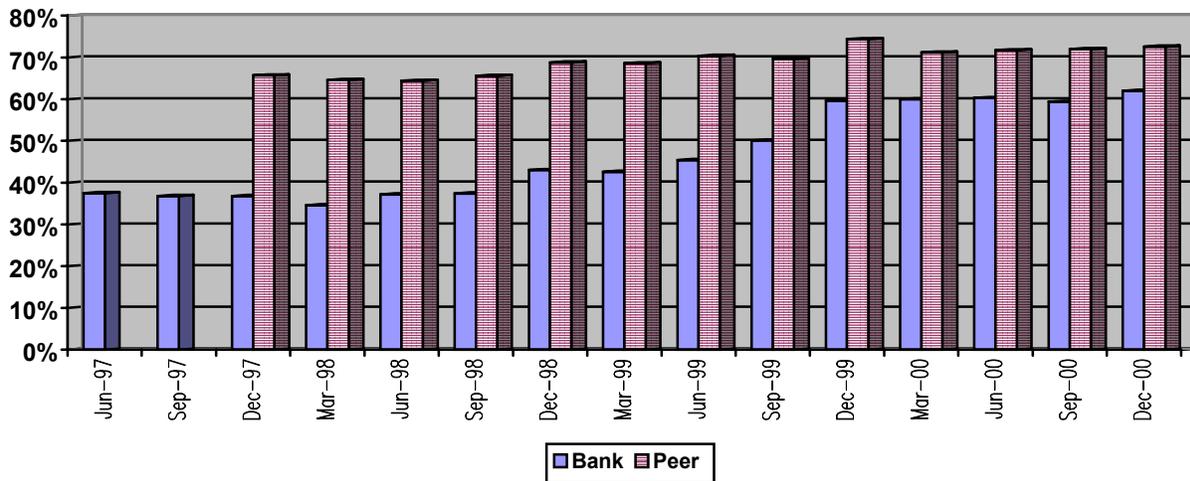
- BCNB’s loan-to-deposit (LTD) ratio meets the standard for satisfactory performance.

Our conclusion is based on the bank’s size, loan delivery capabilities and improvement in the LTD ratio over the past four years. We also considered the needs within the assessment area, and the highly competitive South Bay banking market.

We calculated the average LTD ratio for the 15 quarters ended December 31, 2001. BCNB’s quarterly average LTD ratio during this period is 47 percent. The average LTD ratio for 16 other

similarly sized commercial banks headquartered in Los Angeles County is 70 percent. During these 15 quarters, the bank's LTD ratio rose substantially from 35 percent on March 31, 1998, to 62 percent at December 31, 2000. Part of the reason for BCNB's lower average ratio stems from restricted loan growth during the early part of the assessment period. Between June 1997 and December 1998, BCNB's LTD ratio averaged only 37 percent. This period of low loan growth was attributed to prior loan problems that the bank had to work out of. In the meantime, deposit growth outpaced new loan growth. Since late 1998, the bank has steadily increased its LTD ratio by averaging 55 percent for the quarters between January 1999 and December 2000. This improving trend is continuing with an average LTD ratio of 60 percent for the full year 2000.

Quarterly Loan-to-Deposit Ratios



Fair Lending Review

We analyzed 1997-2000 Small Business lending data, 1998-2000 Home Mortgage Disclosure Act submissions, public comments, and consumer complaint information, according to the OCC's risk based fair lending approach. Based on an analysis of the information, there was no basis for the OCC to conduct a comprehensive fair lending examination in connection with the CRA evaluation this year. The most recent comprehensive fair lending exam was performed in 1999.

Responses to Complaints

BCNB did not receive any written complaints associated with its CRA performance.

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