



SMALL BANK

Comptroller of the Currency
Administrator of National Banks
Washington, DC 20219

PUBLIC DISCLOSURE

October 28, 2004

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

**Stearns Bank Holdingford National Association
Charter Number 23457**

**Main Street
Holdingford, MN 56340**

**Comptroller of the Currency
North Dakota & NW Minnesota
3211 Fiechtner Drive, SW
Fargo, ND 58103**

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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Institution's CRA Rating: Satisfactory

Stearns Bank Holdingford National Association's lending performance reflects a satisfactory response to community credit needs. Factors contributing to this rating include the following:

- The loan-to-deposit ratio is reasonable.
- The bank originated the majority of its loans inside its assessment area.
- The bank's lending to borrowers of different incomes and businesses of different sizes is comparable to the demographic information of the assessment area.
- The geographic distribution of loans throughout the AA is not reasonable.

Description of Institution

Stearns Bank Holdingford National Association (Stearns Bank) is a \$52.5 million bank located in central Minnesota. The bank is owned by Stearns Financial Services, Inc., located in St. Cloud, Minnesota. Stearns Financial Services, Inc. is a multi-bank holding company with total assets of \$1.1 billion as of June 30, 2004. The affiliated banks are located in St. Cloud, Evansville, and Upsala, Minnesota and in Scottsdale, Arizona. The bank has no branches and two automated teller machines.

The bank has experienced a decline in assets since December 31, 2001 when total assets were \$62.8 million. This decline in assets is attributed to a significant decrease in the bank's investment portfolio. However, the bank's loan portfolio has grown over this same time period. The bank purchases a significant amount its loans from Stearns Bank National Association, St. Cloud, Minnesota and to a lesser extent from Stearns Bank Arizona National Association. As of September 30, 2004, total loans and leases were \$41.9 million with participations purchased of \$34.6 million. The bank also relies on holding company management to obtain funding. Roughly 60% of bank deposits are from sources outside of its assessment area.

Stearns bank offers traditional banking products and services. The bank's primary lending focus is commercial loans and leases. Net loans represent 90.9% of total assets. The following table represents the composition of the bank's loan portfolio.

Table 1: Loan Portfolio Composition 6/30/04	\$ (000)	%
Business (including RE)	35,835	75.1%
Residential Real Estate	2,002	4.2%
Farm (including RE)	1,516	3.2%
Consumer Loans	1,460	3.0%
Leases	6,923	14.5%
Total	47,736	100%

There are no legal or financial impediments that restrict the bank's ability to meet the credit needs of the community. Stearns Bank was rated Satisfactory at the last CRA examination dated March 11, 1999.

Description of Stearns Bank's Assessment Area

Stearns Bank's assessment area (AA) consists of 22 contiguous census tracts (CTs) in central Minnesota. The AA includes 18 CTs located in the St. Cloud, Minnesota Metropolitan Statistical Area (number 4106), and 4 CTs in Morrison County. The AA includes 1 low-income census tract, 2 moderate-income census tracts, 16 middle-income census tracts, and 3 upper-income census tracts. The AA meets the requirements of the regulation and does not exclude any low- or moderate-income geographies. The total population of the AA is 99,623, with a large share of the population in St. Cloud.

The bank is located in a small rural community southeast of St. Cloud. The local economy is reliant on small businesses and farms. Many residents commute to nearby St. Cloud for employment. Information from the Bureau of Labor Statistics lists the 2003 unemployment rate for Stearns and Morrison Counties at 3.9% and 6.8% respectively. The average unemployment rate for Minnesota is 5.0%.

Stearns Bank has significant competition from other financial institutions. There are 27 other financial institutions in the bank's AA. There are a few similarly sized financial institutions located throughout the AA, but competition is primarily from larger banks in St. Cloud.

Community contacts were made with various city and county organizations and non-profit community services organizations. These contacts were performed by the OCC and various other banking agencies. The contacts indicated a need for affordable housing in the rural areas, including both rental units and homes for purchase. The need for small business loans is higher within the city of St. Cloud.

The demographics of the AA are illustrated in Table 2 on the following page. The information is based on the 2000 census data information unless otherwise noted.

Table 2: Demographic and Economic Characteristics of AA	
<i>Population</i>	
Number of Families	23,412
Number of Households	36,553
Number of Low-Income Families	3,671
% of Low-Income Families	15.7%
Number of Moderate-Income Families	4,580
% of Moderate-Income Families	19.6%
Number of Middle-Income Families	6,126
% of Middle-Income Families	26.2%
Number of Upper-Income Families	9,035
% of Upper-Income Families	38.6%
<i>Geographies</i>	
Number of Census Tracts/BNA	22
% Low-Income Census Tracts/BNA	4.5%
% Moderate-Income Census Tracts/BNA	9.1%
% Middle-Income Census Tracts/BNA	72.7%
% Upper-Income Census Tracts/BNA	13.6%
<i>Median Family Income (MFI)</i>	
2000 MFI for AA	\$50,465
<i>Economic Indicators</i>	
Unemployment Rate	4%
2004 Median Housing Value	\$99,651
% of Households Below Poverty Level	10.8%

Loan Sampling

The bank's primary loan types were determined by taking all loans originated/purchased for the time period from January 1, 2002 to June 30, 2004. Table 3 depicts the number and volume of loans originated and purchased.

Table 3: Loan Products	#	%	\$ (000)	%
Farm Loans	69	12%	\$1,655	3%
Business Loans	125	21%	\$46,904	85%
Consumer Loans	333	56%	\$2,839	5%
Residential Real Estate Loans	67	11%	\$4,092	7%
Total	594	100%	\$55,490	100%

Source: Loans originated during the evaluation period January 1, 2002 to June 30, 2004

For the purpose of this evaluation, the primary loan types are business loans and consumer loans. These two products combine for 77% of the number of loans and 90% of the dollar amount of loans originated/purchased during this timeframe. Due to the large volume of business loans, greater emphasis will be placed on the bank's business lending performance in determining the bank's overall rating.

Due to changes in the composition of the bank's AA from the 1990 and 2000 census we conducted two loan samples of each primary product in order to evaluate the geographic distribution of loans. Loans made in 2002 are compared to 1990 geographic boundaries and loans made in 2003 and 2004 are compared to 2000 geographic boundaries. A total of 39 business loans and 40 consumer loans were sampled.

The bank accurately reports the location of each of its loans on its internal loan system. After checking the location accuracy of some loans, we relied on this data to determine the bank's lending in the assessment area.

Conclusions about Performance Criteria

Loan-to-Deposit Ratio

Stearns Bank's loan-to-deposit (LTD) ratio meets the standard for satisfactory performance given the size, financial condition, assessment area needs, and local economic conditions. The bank's quarterly LTD ratio averaged 82.23% over the past 22 quarters. The LTD ratio has ranged from 57.15% in the 2nd quarter of 1999 to 104.95% in the 2nd quarter of 2004.

The bank's LTD ratio ranks 4th in comparison with 7 other banks that operate within the bank's AA and are of similar size. The average LTD ratios of these comparable institutions range from 63.97% to 98.0%.

Lending in Assessment Area

Stearns Bank meets the standard for satisfactory performance for lending within its AA. Seventy-five percent of the number and 25% of the dollar volume of loans are originated within the AA.

The dollar volume of loans made within the AA is considerably lower than the number of loans made within the AA due to the significant volume of large business loans that are purchased from the holding company, which originate outside of the bank's AA. The bank is meeting the credit needs of its AA as shown by the number of loans within the AA in Table 4 on the following page.

Table 4: Total Loans Originated or Purchased from January 1, 2002 to June 30, 2004								
	IN ASSESSMENT AREA				OUT OF ASSESSMENT AREA			
LOAN TYPE	#	%	\$ (000s)	%	#	%	\$ (000s)	%
Farm Loans	62	90%	\$1,572	95%	7	10%	\$83	5%
Business Loans	53	42%	\$6,173	13%	72	58%	\$40,731	87%
Consumer Loans	275	83%	\$2,354	83%	58	17%	\$485	17%
Residential Real Estate Loans	55	82%	\$3,515	86%	12	18%	\$577	14%
Total Reviewed	445	75%	\$13,614	25%	149	25%	\$41,876	75%

Source: Loans originated during the evaluation period January 1, 2002 to June 30, 2004.

Other Loan Data

The bank refers customers to its lead bank for secondary market residential real estate loans. During the evaluation period, the bank referred 98 loans for a total dollar volume of \$11.4 million.

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

The bank's lending to businesses of different sizes and to borrowers of different income levels meets the standard for satisfactory performance.

Borrower Distribution of Business Loans

Lending to small businesses meets the demographics of the AA. Of the loans included in our sample, 68% of the number and 13% of the dollar volume are to businesses with revenues of less than \$1 million. The demographic information indicates that 63.35% of the businesses in the AA have revenues in this category as shown in the table below. While the number of loans made to businesses with revenues of less than \$1 million compares favorably to the demographics of the AA, the dollar volume of loan made does not due to the bank purchasing large business loans from the holding company. The following table illustrates the bank's borrower distribution of business loans in the AA.

Table 5: Borrower Distribution of Loans to Businesses				
Business Revenues (or Sales)	≤\$1,000,000	>\$1,000,000	Unavailable/ Unknown	Total
% of AA Businesses	63.35%	6.3%	30.35%	100%
% of Bank Loans in AA by #	68%	32%	0	100%
% of Bank Loans in AA by \$	13%	87%	0	100%

Source: Loan sample; Dunn and Bradstreet data.

Borrower Distribution of Consumer Loans

The borrower distribution of consumer loans to low- and moderate-income families exceeds the demographics of the AA. The following chart illustrates that 25% of the number and 21% of the dollar volume of loans sampled are to low-income families and 40% of the number and 55% of the dollar volume of loans sampled are to moderate-income families. The demographic information indicates that 22.6% of the families in the AA are low-income and 17.4% are moderate-income. The following table depicts the bank's consumer loan lending patterns in the AA compared to demographic data.

Table 6: Borrower Distribution of Consumer Loans								
Borrower Income Level	LOW		MODERATE		MIDDLE		UPPER	
% of AA Households	22.6%		17.4%		21.6%		38.3%	
Loan Sample	% of Number	% of Amount						
Total	25%	21%	40%	55%	15%	10%	17.5%	13%

Source: Sample of 40 consumer loans originated from January 1, 2002 to June 30, 2004. (1 loan did not report income)

Geographic Distribution of Loans

Stearns Bank's geographic distribution of loans throughout the AA does not meet the standard for satisfactory performance.

Business Loans

The bank's geographic distribution of business loans is not reasonable. The bank's performance does not meet the demographics of the AA. In both 2002 and 2003, no loans were made in the AA's low- or moderate-income tracts. It is difficult for the bank to make loans in these tracts as they are not located close to the bank and are served by other financial institutions. The following tables depict the bank's lending pattern to businesses in the AA.

Table 7: 2002 Geographic Distribution of Business Loans								
Census Tract Income Level	LOW		MODERATE		MIDDLE		UPPER	
% of AA Businesses	7%		3%		74%		16%	
LOANS BY YEAR	% of Number	% of Amount						
2002	0	0	0	0	100%	100%	0	0

Source: Sample of 19 business loans made in 2002 in the bank's AA.

Table 8: 2003 thru June 30, 2004 Geographic Distribution of Business Loans								
Census Tract Income Level	LOW		MODERATE		MIDDLE		UPPER	
% of AA Businesses	8%		9%		60%		23%	
LOANS BY YEAR	% of Number	% of Amount						
2003 thru 6/30/04	0	0	0	0	80%	48%	20%	52%

Source: Sample of 20 business loans made in 2003 and 2004 in the bank's AA.

Consumer Loans

The bank's geographic distribution of consumer loans is reasonable. The bank's performance is near the demographics of the AA. In both 2002 and 2003, no loans were made in the AA's low- and moderate-income tracts. These tracts are located in the southeastern portion of the AA, well away from the bank. The limited numbers of families in these tracts, combined with their distance from the bank, mitigate the lack of loans being made within these tracts. The following tables illustrate the bank's consumer loan lending in the AA.

Table 9: 2002 Geographic Distribution of Consumer Loans								
Census Tract Income Level	LOW		MODERATE		MIDDLE		UPPER	
% of AA Households	1%		3%		83%		13%	
LOANS BY YEAR	% of Number	% of Amount						
2002	0	0	0	0	100%	100%	0	0

Source: Sample of 20 consumer loans made in 2002 in the bank's AA.

Table 10: 2003 thru June 30, 2004 Geographic Distribution of Consumer Loans								
Census Tract Income Level	LOW		MODERATE		MIDDLE		UPPER	
% of AA Households	1%		5%		72%		22%	
LOANS BY YEAR	% of Number	% of Amount						
2003 thru 6/30/04	0	0	0	0	100%	100%	0	0

Source: Sample of 20 consumer loans made in 2003 and 2004 in the bank's AA.

Responses to Complaints

Stearns Bank has not received any complaints relating to the bank's CRA performance since the previous examination.

Fair Lending or Other Illegal Credit Practices Review

We found no evidence of illegal discrimination or other illegal credit practices.