



PUBLIC DISCLOSURE

January 27, 2014

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

The First National Bank of Grayson
Charter Number 12982

200 S. Carol Malone Boulevard
Grayson, Kentucky 41143

Office of the Comptroller of the Currency

4419 Pheasant Ridge Road
Suite 300
Roanoke, Virginia 24014

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.

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

Major factors supporting this institution's rating include:

- The bank's quarterly average loan-to-deposit ratio is reasonable based on the bank's size, financial condition, area credit needs, and relevant competitive factors;
- A majority of the bank's loans are made within its assessment area (AA);
- The distribution of loans reflects excellent penetration among borrowers of different incomes given the demographics of the AA;
- The bank's geographic distribution of loans within its AA reflects reasonable dispersion throughout the AA.

SCOPE OF EXAMINATION

This Performance Evaluation assesses the institution's performance under the Lending tests for Small Banks. First National Bank of Grayson (FNB Grayson) was evaluated under the Small Bank examination procedures, which includes a lending test. The lending test evaluates the bank's record of meeting the credit needs of its assessment areas (AA) through its lending activities. The evaluation period under the Lending Test covers the bank's performance from January 1, 2009 through December 31, 2011.

Based upon the bank's business strategy and the loans originated or purchased during the evaluation period, we determined that home mortgage loans and consumer loans are the bank's primary loan products. We selected a sample of 40 home mortgage loans and 40 consumer loans originated during the evaluation period. We selected these samples using the numerical sampling process from bank reports listing loans originated during the evaluation period.

DESCRIPTION OF INSTITUTION

FNB Grayson is a \$219 million locally owned community bank headquartered in Grayson, Kentucky that services the counties of Carter, Elliott, and Morgan. FNB Grayson, established in 1926, is a wholly owned subsidiary of First Grayson Bancorp, Inc., a one-bank holding company. FNB Grayson has a main office and six branches. The main office is located in a middle-income census tract in Carter County. The Grayson, Olive Hill, Rush, and Willard Branches are also located in middle-income census tracts in Carter County. The Sandy Hook Branch is located in a middle-income census tract in Elliott County. The West Liberty Branch is located in a middle-income census tract in Morgan County.

Full service banking is provided at the main office and at each branch, which includes drive through and lobby service. Extended banking hours are available during the business week and on Saturday at all seven locations. Automated Teller Machines (ATMs) are also located at the main office and at each branch. Three additional ATMs are also located offsite at two gas stations/convenience stores and at a local university. No branches have been opened or closed since the last examination.

As of December 31, 2011, FNB Grayson reported \$114 million in net loans, \$193 million in total deposits, and Tier One Capital of \$18 million. The bank had total assets of \$221 million for a net loans to total assets ratio of 51.58 percent. Deposits represent 87 percent of total assets. The bank's loan portfolio consists of consumer loans (32 percent), residential real estate loans (30 percent), non-farm non-residential loans (22 percent), commercial and industrial loans (10 percent), and construction and development loans (3 percent). According to the bank's strategic plan and conversations with bank management, residential mortgage loans and consumer loans are the bank's primary loan products.

Numerous national, state, and savings banks provide deposit and lending competition. According to the Federal Depository Institution Corporation's (FDIC) Deposit Market Share Report, as of June 30, 2013, FNB Grayson ranked first out of nine institutions in the AA with 33.28 percent of deposits. Competitors in this market include The Commercial Bank of Grayson, ranking second with 23.88 percent of deposits and Commercial Bank, headquartered in West Liberty, Kentucky, ranking third with 19.19 percent of deposits.

There are no known legal, financial or other factors impeding FNB Grayson's ability to help meet the needs of its community. FNB Grayson received a satisfactory CRA rating at its last CRA performance evaluation dated March 3, 2009.

DESCRIPTION OF ASSESSMENT AREA(S)

FNB Grayson has defined the counties of Carter, Elliott, and Morgan as its AA. These counties are located in the northeastern region of Kentucky. Since the counties are not included in a Metropolitan Statistical Area (MSA) and are homogenous, we combined all three counties for our analysis. The bank's AA totals 14 census tracts. It is comprised of three moderate-income tracts (21 percent) and 11 middle-income tracts (79 percent). There are no low-income tracts or upper-income tracts. Carter County contains seven census tracts, all of which are middle-income tracts. Elliott County contains one moderate-income census tract and one middle-income census tract. Morgan County contains two moderate-income census tracts and three middle-income census tracts. Although the overall AA is not considered a distressed or underserved area, 11 of the 14 census tracts are designated as distressed or underserved tracts. The bank's AA complies with the regulation and does not arbitrarily exclude low- or moderate-income areas.

According to the 2000 US Census data, the population of the AA is approximately 47,585. The AA contains 13,284 families and 17,768 households. Demographics indicate that approximately 27 percent of the families are categorized as low-income, 18 percent as moderate-income, 20 percent as middle-income, and 35 percent as upper-income. Updated 2011 median family income was \$43,000 for the AA, and the median value of a home was \$47,483. There are 20,128 housing units with owner-occupied units at 71 percent, rental-occupied units at 17 percent, and vacant-housing units at 12

percent in the AA. Approximately 4,336 or 24 percent of households are below the poverty level standard.

The local economy of the bank's AA is diverse with retail, manufacturing, and service industries providing the majority of employment opportunities. The bank's AA is also located within commutable distances to employment sources in Ohio and West Virginia.

Carter County is located in northeastern Kentucky. According to the 2000 US Census data, the population of Carter County is approximately 26,889, comprising 18 percent urban population and 82 percent rural population. Its boundaries are Greenup, Boyd, Lawrence, Elliott, Rowan, and Lewis Counties. The county seat is Grayson. The county's top industries by distribution of employees are retail trade, manufacturing, accommodation and food services. According to the Bureau of Labor Statistics, the December 2013 unemployment rate for Carter County was 10.50 percent compared to the state unemployment rate at 8.0 percent and the national unemployment rate at 6.7 percent.

Elliott County lies in the foothills of the Appalachian Mountains in northeastern Kentucky. According to the 2000 U.S. Census data, the population of Elliott County is approximately 6,748, comprising 14 percent urban population and 86 percent rural population. Its boundaries are Carter, Lawrence, Morgan, and Rowan Counties. The county seat is Sandy Hook. The land is characterized by rolling hills and mountainous terrain, much eroded by early mining and logging operations. A state penitentiary just north of Sandy Hook contributes to the local economy and other counties. The county's top industries by distribution of employees are retail trade, healthcare and social assistance, accommodation and food services. According to the Bureau of Labor Statistics, the December 2013 unemployment rate for Elliott County was 10.10 percent compared to the state unemployment rate at 8.0 percent and the national unemployment rate at 6.7 percent.

Morgan County is located in east central Kentucky. According to the 2000 US Census data, the population of Morgan County is approximately 13,948, comprising 20 percent urban population and 80 percent rural population. Its boundaries are Rowan, Elliott, Menifee, Wolfe, Magoffin, Johnson, and Lawrence Counties. West Liberty is the county seat. A state penitentiary located in West Liberty is a strong contributor to the local economy. The county's top three industries by distribution of employees are public administration, healthcare and social assistance, and retail trade. According to the Bureau of Labor Statistics, the December 2013 unemployment rate for Morgan County was 10.90 percent compared to the state unemployment rate at 8.0 percent and national unemployment rate at 6.7 percent.

COMMUNITY CONTACT

We conducted one community contact during this examination with the Director of the East Carter County Youth Services Center. The Youth Services Center serves Carter County. Our contact identified mortgage loans and basic checking accounts as credit needs for community. The contact also indicated that the financial institutions within the AA are readily accessible and adequately meet the local residential lending needs.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

The performance under the Lending Test is considered "Satisfactory." The bank's loan-to-deposit ratio is reasonable, and a majority of loans are originated inside the AA. The bank's borrower distribution reflects reasonable penetration among borrowers of different incomes. Geographic distribution reflects reasonable dispersion throughout the census tracts of different income levels.

Loan-to-Deposit Ratio

FNB Grayson's quarterly average net loan-to-deposit (LTD) ratio is reasonable given the bank's size, financial condition, area credit needs, and relevant competitive factors. The LTD ratio meets the standards for satisfactory performance. The bank's quarterly average loan-to-deposit ratio for the twenty consecutive quarters (1Q2009 - 4Q2013) is 60.56 percent. The bank's quarterly LTD ratios ranged from a quarterly low of 53.47 percent at March 31, 2011 to a quarterly high of 70.81 percent at December 31, 2013. The peer quarterly average LTD ratio is 66.44 percent using the same timeframe. The peer group is a custom peer of 6 similarly situated banks in Kentucky.

Institution Name	Average Loan to Deposit Ratio, Twenty Quarters beginning March 31, 2009
Citizens National Bank of Paintsville	75.99%
Kentucky Bank	76.35%
Commercial Bank	41.29%
Bank of the Mountains	80.37%
The Citizens Bank	75.34%
The Commercial Bank of Grayson	49.32%

Lending in Assessment Area

The bank's lending in its AA meets the standard for satisfactory performance. A majority of FNB Grayson's primary loan products were originated within the bank's AA. Of the 40 loans sampled for our review, 33 loans or 82.5 percent were located within the bank's AA.

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

The distribution of loans reflects excellent penetration among individuals of different income levels, and FNB Grayson’s record of lending to borrowers of different incomes meets the standard for satisfactory performance.

FNB Grayson’s borrower distribution of residential mortgage loans is reasonable. In our analysis of lending to low-income borrowers, we took into consideration the lack of affordability for low-income individuals to purchase a home. Our sample included four loans to low-income borrowers and four loans to moderate income borrowers. The distribution of real estate mortgage loans to low-income borrowers (20 percent) is less than the percentage of low-income families for the AA of (27 percent). The distribution of real estate mortgage loans to moderate income borrowers (20 percent) exceeds the percentage of moderate income families in the AA at 18 percent.

Table 1 below reflects the distribution by borrower income level of residential mortgage loans.

Table 1 - Borrower Distribution of Residential Real Estate Loans in FNB of Grayson Non MSA AA		
Borrower Income Level	% of AA Families	% of Number of Loans
Low	27%	20%
Moderate	18%	20%
Middle	20%	25%
Upper	35%	35%

FNB Grayson’s borrower distribution of consumer loans is reasonable. The percentage of loans made to low-income borrowers (35 percent) exceeds the percentage of low-income households in the AA (32 percent). The percentage of loans made to moderate-income borrowers (20 percent) exceeds the percentage of moderate-income households in the AA (17 percent).

Table 2 below reflects the distribution by borrower income level of consumer loans.

Table 2 - Borrower Distribution of Consumer Loans in FNB of Grayson Non MSA AA		
Borrower Income Level	% of AA Households	% of Number of Loans
Low	32%	35%
Moderate	17%	20%
Middle	18%	30%
Upper	33%	15%

Geographic Distribution of Loans

The bank's geographic distribution of loans reflects reasonable dispersion throughout the AA, and FNB Grayson's performance meets the standard for satisfactory performance. No conspicuous gaps or areas of low penetration were identified.

We considered the demographic characteristics of moderate-income geographies in evaluating geographic distribution of mortgage loans in the AA. We considered the percentage of owner-occupied housing units in these geographies as well as the percentage of rental properties in the AA. These are limiting factors that adversely impact the bank's ability to make mortgage loans to individuals residing in moderate-income geographies. We also considered the number of competitors making loans in this market.

FNB Grayson's geographic dispersion of residential mortgage loans is reasonable. There are no low-income geographies in the AA. The distribution of loans to borrowers in moderate-income geographies (10 percent) was lower than the percentage of owner-occupied housing in moderate-income tracts (16 percent). The bank's performance is considered reasonable when taking into consideration the relatively low level of owner-occupied housing units in moderate-income tracts; the competition from other institutions; the limited road networks in mountainous regions of southern Elliot and southwestern Morgan counties; the location of the bank's branches in relation to the three moderate-income geographies; and the bank's lending in the eleven underserved and/or distressed middle-income geographies.

Table 3 reflects the distribution by geographic income level of residential mortgage loans.

Table 3 - Geographic Distribution of Residential Real Estate Loans in FNB of Grayson Non MSA AA		
Census Tract Income Level	% of AA Owner Occupied Housing	% of Number of Loans
Low	0%	0%
Moderate	16%	10%
Middle	84%	90%
Upper	0%	0%

FNB Grayson's geographic distribution of consumer loans is reasonable. There are no low-income geographies in the AA. The percentage of home mortgage loans made in moderate-income geographies is below the ratio of owner-occupied housing units in the census tracts. However, when taken into consideration the relatively limited number of households in moderate-income geographies, the location of the bank's branches in relation to the moderate-income geographies, and the lending done in the eleven

middle-income distressed and/or underserved geographies, the bank’s geographic distribution of consumer loans is reasonable.

Table 4 below reflects the distribution by geographic income level of consumer loans.

Table 4 - Geographic Distribution of Consumer Loans in FNB of Grayson Non MSA AA		
Census Tract Income Level	% of AA Households	% of Number of Loans
Low	0%	0%
Moderate	15%	5%
Middle	85%	95%
Upper	0%	0%

Responses to Complaints

There were no complaints regarding the bank’s CRA performance during the evaluation period.

Fair Lending or Other Illegal Credit Practices Review

Pursuant to 12 C.F.R. 25.28(c), or 12 C.F.R. 195.28(c), in determining a national bank’s (bank) or Federal savings association’s (FSA) CRA rating, respectively, the OCC considers evidence of discriminatory or other illegal credit practices in any geography by the bank or FSA, or in any assessment area by an affiliate whose loans have been considered as part of the bank’s or FSA’s lending performance.

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