



SMALL BANK

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

PUBLIC DISCLOSURE

May 13, 2004

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

**Grayson National Bank
Charter Number 10834**

**113 West Main Street
Independence, VA 24348**

**Comptroller of the Currency
Virginia Field Office
3800 Electric Road Suite 204
Roanoke, VA 24018**

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 Outstanding based on the following information:

- The bank's loan-to-deposit ratio is more than reasonable.
- A substantial majority of the bank's loans were originated within their assessment areas.
- Analysis reflects more than reasonable penetration among individuals of different income levels.
- The geographic distribution of loans reflects reasonable dispersion throughout the assessment areas.
- No public complaints related to CRA have been filed since the last CRA examination.

DESCRIPTION OF INSTITUTION

Grayson National Bank (GNB) is a subsidiary of Grayson Bankshares, a one-bank holding company. There have not been any major changes in the bank's corporate structure since the last CRA examination. GNB received an outstanding CRA rating at its last CRA performance evaluation dated March 9, 1998. This evaluation period covers March 10, 1998 to March 31, 2004. However, the loan samples do not include any loans originated during 2003. The loan sample used in this evaluation was taken from loans originated from January 1, 2000 to December 31, 2002. Loans originated in 2003 must be evaluated using year 2000 census data. Loans originated during and prior to 2002 are evaluated using 1990 census data. The OCC determined that Small Bank CRA examinations conducted during 2004 may exclude loans made during 2003 to avoid multiple lending analyses, if bank management agrees it is appropriate and there are no significant changes to the bank's lending practices. There are no legal or financial impediments to GNB's ability to meet the credit needs of its assessment areas.

GNB's main office is located in Independence, Virginia. The bank also operates four full-service branch offices in Virginia and one in North Carolina. The bank opened a branch in North Carolina in 2000 and has not closed any branches since the last examination. GNB currently does not have any depository automated teller machines.

As of March 31, 2004, GNB's assets totaled \$265 million, of which net loans comprised 68%. The following table reflects the composition of GNB's loan portfolio based on the March 31, 2004 call report.

Loan Type	Dollar (000's)	Percent
Commercial & Industrial Including Commercial Real Estate	43,898	23.89
Residential Mortgage Loans	86,901	47.30
Individuals	13,092	7.13
Construction & Land Development	16,074	8.75
All Other	5,117	2.79
Farmland and Agriculture	18,649	10.14
Total	183,731	100.00

We determined the bank's primary loan type based on outstanding balances and discussions with management about loan originations. As indicated in the table above, the primary loan type based on outstanding balances is residential mortgage loans. Residential mortgage loans originated during 2000-2002 comprised 42.93% of gross loans. Management agreed with our selection of residential mortgages as the primary loan type.

DESCRIPTION OF ASSESSMENT AREAS

The bank has two assessment areas (AA):

- Grayson County, Carroll County, and City of Galax, VA
- Alleghany County, North Carolina

The first assessment area consists of the counties of Grayson and Carroll and the City of Galax. Carroll County and the City of Galax border Grayson County, which is located in the southwestern part of Virginia in the region known as the New River Valley. Carroll County is located on the crest of the Blue Ridge Mountains of Southwest Virginia. The City of Galax is adjacent to Carroll County and serves as the employment and commercial hub of Grayson and Carroll Counties. The economy of the area, particularly Grayson County, has transformed from a farming community to mixed industry and tourism as people are drawn by the natural beauty of the New River and surrounding mountains. Industrial companies include Vaughn-Basset, National Textiles, Webb Furniture Enterprises, and Nautilus. Unemployment for this assessment area is 2%, compared to the state average of 3.1%. Population for this assessment area is 49,542. The area's top three industries by distribution of employees are manufacturing, services, and retail. The bank has 94% of their deposits in this assessment area and 29.86% of the deposit market share. Competition in this assessment area consists of 22 branches of FDIC-insured institutions representing nine banks varying in asset size.

The second assessment area is Alleghany County, North Carolina. Alleghany County is located in northwest North Carolina's Blue Ridge Mountains and nestled between the New River and the Blue Ridge Parkway. Alleghany County is the state's fifth smallest county in land area

encompassing 233 square miles and sixth smallest in population with 9,500 residents. It is bordered by Grayson County, Virginia on the north, and Sparta is the only municipality. Unemployment for Alleghany County is 2%. The poverty rate is 23%, and the owner occupancy rate is 58%. The largest industries by distribution of employees are manufacturing, services, and farm. Major employers in Alleghany County, North Carolina are Alleghany Memorial Hospital, NAPCO, Sparta Industries, Pioneer Equip, and Magnolia Manufacturers. The bank has 6% of their deposits in the branch that serves this assessment area and 7.5% of the deposit market share. Competition in this assessment area consists of six branches of FDIC-insured institutions representing six banks of varying asset size.

Community Contact

We conducted one community contact during this examination with a representative of a housing assistance group serving Carroll County, Grayson County, and the City of Galax. The contact indicated that the major employers in the area are textile plants and furniture factories. Many of the textile plants have closed, and the furniture factories have cut back operations. General banking and credit needs of the community are being met, and about every six months a new branch is opening in the area. The contact would like to see the local banks attract more businesses to the area and expressed a need for department stores in Galax.

CONCLUSIONS ABOUT PERFORMANCE CRITERIA

Loan-to-Deposit Ratio

The loan to deposit ratio is excellent when compared to other similarly situated institutions. A review of bank data reveals that GNB is similarly situated to Mountain National Bank and The Bank of Floyd. Both institutions offer similar credit products and operate in at least one of the same assessment areas as GNB. The following table reflects the average quarterly loan to deposit ratio of GNB and the similarly situated banks.

Institution Name	Average Loan to Deposit Ratio
	Twenty-four quarters beginning June 30, 1998
Grayson National Bank	77.25%
Mountain National Bank	52.13%
The Bank of Floyd	63.88%

Lending in Assessment Area

To evaluate the bank’s performance in this area, we selected a sample of 57 residential real estate loans originated between January 1, 2000 and December 31, 2002. The bank originated a substantial majority of loans sampled within their assessment areas. The tables that follow summarize the results of our review.

Lending in Grayson County, Carroll County, and the City of Galax AA										
	Number of Loans					Dollars of Loans				
Loan Type	Inside		Outside		Total	Inside		Outside		Total
	#	%	#	%		\$ (000)	%	\$ (000)	%	
Home Purchases	25	89	3	11	28	1,331	80	341	20	1,672

Source: Sample of loans

Lending in Alleghany County, North Carolina AA										
	Number of Loans					Dollars of Loans				
Loan Type	Inside		Outside		Total	Inside		Outside		Total
	#	%	#	%		\$	%	\$	%	
Home Purchases	29	100	0	0	29	1,670	100	0	0	1,670

Source: Sample of loans

Lending to Borrowers of Different Incomes

The distribution of loans, given the demographics of the AAs, reflects more than reasonable penetration among borrowers of different income levels (including low- and moderate-income). The analysis of lending to borrowers of different income levels was completed using all files inside the AAs from the Lending in the Assessment Areas sample, excluding loans for which income information was not available. The following tables reflect the results from our sample.

Borrower Distribution of Residential Real Estate Loans in Grayson County, Carroll County, and the City of Galax AA								
Borrower Income Level	Low		Moderate		Middle		Upper	
Loan Type	% of AA Families	% of Number of Loans	% of AA Families	% of Number of Loans	% of AA Families	% of Number of Loans	% of AA Families	% of Number of Loans
Home Purchases	25	29	21	21	27	29	27	21

Source: Loan sample

The table above illustrates the distribution of home mortgage loans within the income levels compared to the percentage of families in each income level. The distribution of home mortgage loans to low-income borrowers is excellent in the Grayson County, Carroll County, and the City of Galax AA. The distribution of home mortgage loans to moderate-income borrowers is reflective of the percent of moderate-income families.

Borrower Distribution of Residential Real Estate Loans in Alleghany County, North Carolina AA								
Borrower Income Level	Low		Moderate		Middle		Upper	
Loan Type	% of AA Families	% of Number of Loans	% of AA Families	% of Number of Loans	% of AA Families	% of Number of Loans	% of AA Families	% of Number of Loans
Home Purchases	25	14	23	31	23	38	29	17

Source: Loan sample

The table above illustrates the distribution of home mortgage loans within the income levels compared to the percentage of families in each income level. The distribution of home mortgage loans to low-income borrowers is adequate in this AA. The distribution of home mortgage loans to moderate-income borrowers is excellent. The bank only has 6% of its total deposits in the branch that serves this assessment area, and competition in this market is strong.

Geographic Distribution of Loans

GNB's geographic distribution of loans reflects reasonable dispersion throughout their AAs. The analysis of the geographic distribution of loans was completed using all loans located in the AA from the loan sample previously described. There are no low-income or upper-income geographies in either AA. We focused our review on the moderate-income geographies in both AAs.

We evaluated the lending distribution in these AAs to determine if any unexplained conspicuous gaps existed. We used reports and maps to compare the geographies where loans were made to the geographies in the AAs. We considered loan distributions, branch locations, competition, market conditions, and demographic information. No unexplained conspicuous gaps were identified. The following tables reflect the results for the primary loan type.

Geographic Distribution of Residential Real Estate Loans in Grayson County, Carroll County, and the City of Galax AA								
Census Tract Income Level	Low		Moderate		Middle		Upper	
Loan type	% of AA Owner Occupied Housing	% of Number of Loans	% of AA Owner Occupied Housing	% of Number of Loans	% of AA Owner Occupied Housing	% of Number of Loans	% of AA Owner Occupied Housing	% of Number of Loans
Home Purchases	0	0	16	4	84	96	0	0

The table above illustrates the geographic distribution of home mortgage loans among geographies of different income levels compared to the percentage of owner occupied housing. The distribution of home mortgage loans in the moderate-income geographies is adequate taking into consideration that the bank does not have an office in the moderate-income geography. The closest office is located in the City of Galax, which is 15-20 miles away.

Geographic Distribution of Residential Real Estate Loans in Alleghany County, North Carolina AA								
Census Tract Income Level	Low		Moderate		Middle		Upper	
Loan type	% of AA Owner Occupied Housing	% of Number of Loans	% of AA Owner Occupied Housing	% of Number of Loans	% of AA Owner Occupied Housing	% of Number of Loans	% of AA Owner Occupied Housing	% of Number of Loans
Home Purchases	0	0	34	38	66	62	0	0

The table above illustrates the geographic distribution of home mortgage loans among geographies of different income levels compared to the percentage of owner occupied housing. The distribution of home mortgage loans in the moderate-income geography was excellent in this AA.

Responses to Complaints

GNB has not received any CRA-related complaints since the March 9, 1998 CRA examination.

Fair Lending or Other Illegal Credit Practices Review

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