



# INTERMEDIATE SMALL BANK

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Comptroller of the Currency  
Administrator of National Banks

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Washington, DC 20219

## PUBLIC DISCLOSURE

December 01, 2008

### COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

Hawaii National Bank  
Charter Number: 14911

45 North King Street  
Honolulu, HI 96817

Office of the Comptroller of the Currency

SAN FRANCISCO FIELD OFFICE  
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**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.**

**The Lending Test is rated: Satisfactory.**

**The Community Development Test is rated: Satisfactory.**

Hawaii National Bank (HNB) has an overall satisfactory record of meeting community credit needs. This is based on the following:

- The bank has a reasonable loan-to-deposit ratio and averaged 68% during the evaluation period.
- The bank's record of lending in its assessment area (AA) exceeds the standard for satisfactory performance. A substantial majority of the bank's loans originated within its defined AA.
- The distribution of loans reflects a reasonable penetration among individuals of different income levels and businesses of different sizes, given the bank's product offerings and local economic conditions. The bank's distribution of loans to businesses of different sizes is considered adequate.
- The bank's geographic distribution of loans reflects satisfactory dispersion throughout its AAs.
- The bank's community development performance demonstrates satisfactory responsiveness to the community development needs of its AA.
- There were no public complaints about the bank's CRA performance.

### **Scope of Examination**

This Performance Evaluation period covered April 14, 2005, through September 30, 2008, and was evaluated using 2000 Census demographic information. There has been no data integrity review conducted prior to this evaluation. We analyzed a random selection of business loans, including both commercial and commercial real estate loans, and all residential real estate loans for the lending test. We reviewed all of the bank's community development investments, loans, and services to ensure they met the definition for community development.

### **Description of Institution**

Hawaii National Bank (HNB) is a wholly owned subsidiary of Hawaii National Bancshares, Inc. The bank opened on September 19, 1960, and is headquartered in downtown Honolulu, Hawaii.

As of September 30, 2008, HNB had total assets of \$498 million and equity capital of \$47.2 million. The bank has not engaged in any merger activity during the assessment period. As of September 30, 2008, net loans represented 68.3% of total assets. HNB's commercial loans totaled \$114 million or 32.9% of total loans. One-to-four family

residential loans totaled \$64.5 million or 18.6% of total loans.

The bank's primary focus is on small business customers and, to a lesser extent, to individuals for home loans and consumer credit within the bank's AA. Most of the bank's customers are small family enterprises and closely-held businesses. HNB, one of the smaller commercial banks, was compared to Finance Factors Limited, the one institution that is of similar size. The bank has 1.73% market share of the deposits for its AA.

The mission of HNB is to be a strong and profitable financial institution, offering a broad range of products and services for commercial and retail accounts. The bank will continue to build its reputation as an independent community-oriented bank. It will enhance its efforts to provide knowledgeable, friendly, and well-trained staff, prompt and efficient service, and its special expertise in lending to closely-held and family-owned businesses.

HNB is affiliated through common ownership as defined in 12 U.S.C. § 371c with various business entities of the Luke family who own more than 90% of the holding company, Hawaii National Bancshares, Inc.

There are no legal or financial circumstances impeding the bank's ability to help meet the credit needs of the community. The bank's CRA performance was previously evaluated on April 13, 2005, and found to be satisfactory.

**Table 1**

<b>HAWAII NATIONAL BANK LOAN PORTFOLIO COMPOSITION</b>		
<b>Loan Type</b>	<b>\$ Volume (000)</b>	<b>% of Portfolio</b>
Commercial	253,334	73%
Residential Real Estate	82,829	24%
Consumer	6,926	2%
Farm & Other	5,326	1%
<b>Total Loans</b>	<b>348,415</b>	<b>100%</b>

*Call Report as of 9/30/08*

***Please refer to the bank's CRA public file for more information about the institution.***

## Description of Assessment Area(s)

Management and the Board have designated three AAs in Hawaii. The Oahu AA is comprised of part of the Honolulu Metropolitan Statistical Area (MSA). The other two AAs are selected census tracts on the islands of Maui and Hawaii. These two AAs are combined for purposes of this analysis since the two islands contain a smaller portion of the state’s population and neither is located in a MSA. We performed a full-scope review of the Oahu AA because it represents HNB’s major market, as well as a limited-scope review of the Maui-Hilo (Hawaii) AA. The AAs meet the requirements of the regulation and do not arbitrarily exclude any low- or moderate-income geographies.

In conjunction with this CRA examination, we conducted a community contact interview. Community contacts are interviewed to learn about credit opportunities within the community and how well financial institutions address the credit and service needs of the community. The contact was a representative of a local city and county agency that helps people qualify for the Section 8 homeownership program. The contact felt there is a need for local banks to provide more financial counseling and affordable loans for home purchases by low- and moderate-income people.

### Oahu AA

The Oahu AA consists of 140 census tracts in Honolulu County, which were determined by the 2000 U.S. Census. Honolulu County is located on the island of Oahu. The island of Oahu has the majority of the state’s population and is the site of state government. Oahu also generates most of the state’s tourism trade.

The following table highlights the demographic composition of the bank’s Oahu AA.

**Table 2**

<b>OAHU AA COMPOSITION</b>						
<b>INCOME CHARACTERISTICS OF CENSUS TRACTS, BUSINESSES AND FAMILIES</b>						
<b>Income of Census Tract</b>	<b># and % of Census Tracts</b>		<b># and % of Businesses</b>		<b># and % of Families</b>	
Low Income	6	4.29%	2,190	5.39%	2,979	2.45%
Moderate Income	46	32.86%	15,799	38.88%	38,543	31.74%
Middle Income	42	30.00%	14,444	35.55%	36,167	29.78%
Upper Income	44	31.43%	7,623	18.76%	43,762	36.03%
N/A	2	1.43%	577	1.42%	0	0.00%
<b>Total:</b>	<b>140</b>	<b>100.00%</b>	<b>40,633</b>	<b>100.00%</b>	<b>121,451</b>	<b>100.00%</b>

*Source: 2007 Dun & Bradstreet*

The total population of the AA is 507,675. The weighted average HUD updated MSA median family income is \$73,500, and the weighted average of median housing is \$276,114.

According to Moody’s Economy.com, dated August 2008, Honolulu’s (HON) economy has stalled and job losses have increased in recent months. The decline in tourism and the slump in the housing market have been the key causes of the downturn. Up until recently, the metro area’s economy held up relatively well compared with the national

economy. The turmoil at the national level has finally reached and impacted the HON economy. Very few industries are experiencing any notable growth; therefore, the unemployment rate has increased to 3.4% as of June. Even though it is well below the national average and lower than at any point during the last recession, it remains a concern. Major employers include Schofield Barracks, Pearl Harbor Naval Complex, Marine Corps Base Hawaii Kaneohe Bay, University of Hawaii, Hickam AFB and Marriott International.

The leisure/hospitality and retail industries are expected to contract in the near term as tourism from the U.S. mainland and abroad declines. Rising unemployment, tepid wage growth, and tight credit conditions will force consumers to curtail their discretionary spending, with vacations a likely casualty. The health of the metro area depends on tourism; with consumer-driven industries accounting for approximately one-quarter of payrolls in HON. The slowdown in travel from the mainland has been exacerbated by significantly higher air fares that resulted from record-high oil prices. However, most recently, the price of oil has experienced a significant drop, but the affects may not reverse the trend because other economic factors still weigh down the tourism industry. On the international front, the number of visitors from abroad will slow because of deteriorating global economic growth, coupled with the appreciation of the dollar against most major currencies.

Weak migration patterns will continue to hinder the metro area's economy as they weigh on population growth and, in turn, the consumer base. Net migration fell significantly in 2007, the second straight annual decline. The primary causes of the recent exodus are extremely high business and living costs. HON also had one of the highest inflation rates among U.S. cities over the past year because of surging housing and utility prices. The extremely high home prices have resulted in HON having one of the least affordable housing markets in the nation. A major determinant of migration is the movement of military personnel between bases. In the short term, HON's economy will contract through the end of the year as slowing tourism and the housing market downturn hamper growth. In the long term, the metro area will be hampered by high business and living costs. However, some of these costs will be offset as people are drawn to the relatively large and high-paying government and transportation industries and an attractive quality of life, while businesses are attracted to the metro area's highly educated workforce.

The five largest employment sectors in the Honolulu MSA employ 71.4% of all employees, both military and civilian: Government (21.2%), Leisure and Hospitality Services (14.1%), Professional and Business Services (13.3%), Education and Health Services (12.6%), and Retail trade (10.2%).

According to the 2007 Business Geodemographic Data, there are 40,633 businesses that operate within this AA. Of these, approximately 65% have reported annual revenues of \$1 million or less and 67% employ fewer than ten people.

Competition in the area is strong with 11 banks operating within the Honolulu MSA. HNB ranks 7<sup>th</sup> in deposit market share with 1.87%. The four largest banks hold 90.12% of the deposit market share. Other area banks include First Hawaiian Bank, Bank of

Hawaii, American Savings Bank FSB, and Central Pacific Bank.

***Please refer to the public file for additional information.***

## Conclusions with Respect to Performance Tests

Based on a full scope review, the bank's residential real estate and small business performance in the AA is overall satisfactory. Conclusions to support this rating are based on the following:

### LENDING TEST

#### Loan-to-Deposit Ratio

The bank's loan-to-deposit (LTD) ratio demonstrates a willingness to lend. The level of lending is reasonable given the bank's size, area credit needs, and the competitive banking market. We analyzed the bank's quarterly LTD ratio from January 1, 2004, through September 30, 2008. During this period, the LTD ranged from a low of 64% to a high of 76%, with a quarterly average of 68%. We compared the bank's average ratio to that of one peer bank that operated in the same AA. The peer group's quarterly LTD ratio, over the same time period, averaged 83%. While the bank's average ratio was lower than the peer bank average, it meets the standard for satisfactory performance.

#### Lending in Assessment Area

The bank's record of lending in the AA exceeds the standard for satisfactory performance.

**Table 3**

HAWAII NATIONAL BANK LENDING IN AA								
Loan Type	Number of Loans				Dollars of Loans			
	Inside		Outside		Inside		Outside	
	#	%	#	%	\$	%	\$	%
Business Loans (Sample)	20	100%	0	0%	12,745,000	100%	0	0%
Residential Real Estate (Actual)	141	93%	10	7%	48,607,000	91%	5,000,000	9%

*Source: Sample of 20 business loans originated from January 1, 2003 to June 30, 2008, and all HMDA reported loans from 2006, 2007 and YTD 2008*

A substantial majority of the bank's loans and other lending-related activities are made within the bank's designated AA. We sampled 20 business loans since the last CRA examination. Of the 20 sampled loans, the bank originated all loans, or 100% of the number of loans and dollar volume of the loans, to borrowers within their AA. We also

reviewed the banks Home Mortgage Disclosure Act reported information for the years of 2006, 2007, and YTD 2008. The bank originated 141 loans, or 93% of the number of loans to borrowers, within their AA. Based on the dollar volume of the loans, the inside ratio was 91%.

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

The distribution of loans reflects a reasonable penetration among individuals of different income levels and businesses of different sizes, given the bank's product offerings and local economic conditions.

### **Business Loans – Oahu AA**

The bank's distribution of loans to businesses of different sizes, given the demographics of the AAs, reflects reasonable penetration among businesses of different sizes.

**Table 4**

<b>OAHU AA</b>				
<b>INCOME DISTRIBUTION OF LOANS TO BUSINESSES</b>				
Business Revenues (or Sales)	≤\$1,000,000	>\$1,000,000	Unavailable/Unknown	Total
% of AA Businesses	65%	7%	28%	100%
% of Bank Loans in AA by #	50%	40%	10%	100%
% of Bank Loans in AA by \$	37%	53%	10%	100%

*Demographic Data Source: 2007 Business Geodemographic Data.*

The percentage of businesses with revenues of less than or equal to \$1,000,000 within the Oahu MSA AA is 65%. Based on our sample of 20 loans within the AA, the bank originated 50% of their loans by number and 37% by dollar volume to these businesses.

While these percentages indicate the bank's efforts to lend to businesses with revenues of less than or equal to \$1,000,000 are below the area demographics, the majority of all of the bank's business loans were for less than \$100,000, indicating responsiveness to the needs of the businesses in the area.

### **Residential Real Estate Loans – Oahu AA**

The distribution of home loans to low- and moderate-income borrowers is adequate. Table 5 shows that no home purchase and no home improvement loans were made to low-income borrowers. However, it shows that for home refinance loans, the bank made 13.92% to low-income borrowers, compared to the 20.55% of low-income families in the AA. The bank made 8.11% of their home purchase and 8.86% of their home refinance loans to moderate-income borrowers compared to 17.93% moderate-income families in the AA. The cost of housing in the Oahu AA continues to be one of the highest in the United States and the supply remains limited. The high cost of housing, coupled with the below average median incomes, makes home ownership and affordable home mortgages very difficult for low- and moderate-income borrowers. The following table shows the distribution of home loan products among borrowers of different income levels based on the 2000 US Census, as compared to the percent of

families in each income category.

**Table 5**

OAHU AA								
BORROWER DISTRIBUTION OF RESIDENTIAL REAL ESTATE LOANS								
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 Purchase	20.55	0.00	17.93	8.11	20.73	16.22	40.78	75.68
Home Improvement	20.55	0.00	17.93	0.00	20.73	100.00	40.78	0.00
Home Refinance	20.55	13.92	17.93	8.86	20.73	17.72	40.78	59.49

*Demographic Data Source: 2000 US Census*

The distribution of loans by percentage of number of loans originated in the low- and moderate- income geographies within the Maui-Hilo AA is consistent with the lending in the Oahu AA.

**Geographic Distribution of Loans**

The bank's geographic distribution of loans reflects satisfactory dispersion throughout the AAs. The bank was not able to penetrate all census tracts within their AAs. However, there were no conspicuous gaps in the bank's distribution of loans.

**Business Loans – Oahu AA**

As shown in the table below, the bank did not originate any business loans in low income geographies as compared to business located in low-income geographies. However, the bank's distribution of business loans by percentage of number of loans originated in the moderate-income geographies was 63%, exceeding area demographics of 39%.

**Table 6**

OAHU AA								
GEOGRAPHIC DISTRIBUTION OF LOANS TO BUSINESSES								
Census Tract Income Level	Low		Moderate		Middle		Upper	
Loan Type	% of AA Businesses	% of Number of Loans	% of AA Businesses	% of Number of Loans	% of AA Businesses	% of Number of Loans	% of AA Businesses	% of Number of Loans
Business Loans	5%	0%	39%	63%	36%	25%	19%	6%

*Demographic Data Source: 2007 Business Geodemographic Data*

The distribution of loans by percentage of number of loans originated in the low- and moderate-income geographies within the Maui-Hilo AA is consistent with the lending in the Oahu AA.

**Residential Real Estate Loans – Oahu AA**

As shown in the table below, the bank did not originate any home purchase loans in low-income geographies, as compared to 0.71% of owner occupied housing. However, the bank’s distribution of residential real estate loans by percentage of number of loans originated in the moderate-income geographies was 37.21%, exceeding the area demographics of 20.71%

Although the bank did not originate any home improvement loans in low- or moderate-income geographies, this could be explained by the fact that the bank only made a total of two home improvement loans during the entire review period.

For home refinance loans, the bank’s distribution by percentage of loans originated in the low-income geographies was 2.5%, exceeding the area demographics of 0.71%. The bank’s distribution of residential real estate loans by percentage of number of loans originated in the moderate-income geographies was 18.75%, which is just below the area demographics of 20.71%.

We placed more weight on the home refinance loans, which make up the majority of the residential real estate loans, and the percentage for these loans is in line with the area demographics.

**Table 7**

Oahu AA Geographic Distribution of Residential Real Estate Loans								
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 Purchase	0.71	0.00	20.71	37.21	32.24	30.23	46.35	32.56
Home Improvement	0.71	0.00	20.71	0.00	32.24	0.00	46.35	100.00
Home Refinance	0.71	2.50	20.71	18.75	32.24	35.00	46.35	43.75

*Demographic Data Source: 2000 US Census*

The distribution of loans by percentage of number of loans originated in the low- and moderate-income geographies within the Maui-Hilo AA is not consistent with the lending in the Oahu AA. However, the volume and number of loans is very low, and therefore it is difficult to draw a conclusion from the available data.

**Responses to Complaints**

There have been no consumer complaints relating to the bank’s Community Reinvestment Act performance during the evaluation period.

## COMMUNITY DEVELOPMENT TEST

The bank's overall performance under the Community Development Test is rated "Satisfactory." The community development needs and opportunities of the AA include affordable housing for low- and moderate-income individuals, community services targeted to low- and moderate-income individuals, activities that promote economic development by financing small businesses as defined by the regulation, and activities that revitalize or stabilize low- and moderate-income geographies. HNB has demonstrated responsiveness to the community development needs of its AA.

### Number and Amount of Community Development Loans

Qualifying community development (CD) loans are loans that meet the definition of community development, as defined in the CRA regulation. During the evaluation period, HNB originated 16 community development loans, totaling over \$24.6 million. Examples of loans for qualifying community development organizations are described below.

- **Hawaii Community Reinvestment Corporation (HCRC)**

The bank participated in various loan funds through HCRC. HCRC, chartered in July 1990, is a non-profit organization and its primary purpose is to provide financial and technical assistance to facilitate the development of affordable housing in the State of Hawaii. The membership of HCRC is comprised of federally insured depository institutions chartered under federal or state law, with business offices authorized to accept deposits in the State of Hawaii.

- **Daiichi-ya Love's Bakery**

The purpose of this CD loan was to provide financing to purchase equipment and provide a line of credit to Daiichi-ya Love's Bakery which is located in a moderate-income geography, and employs approximately 349 employees of which a majority are low-income individuals. Daiichi-ya Love's bakery was started in 1851, and was purchased by Wonder Bread and Hostess Cake in 1968. In 1981, the business was purchased by First Baking Co., Ltd. located in Japan. The business was going into bankruptcy prior to the \$5 million loan originated by the bank.

- **West Physicians Associates, LLC (WPA)**

The purpose of this CD loan was to provide financing to purchase commercial property located in a moderate-income geography. The complex houses approximately 40 small businesses and non-profits serving low- and moderate-income individuals. Although the property is not physically located within the bank's AA, it is within two miles, and many of the patients served are from within the AA. This loan for over \$4 million was originated by the bank.

### Number and Amount of Qualified Investments

The number and amount of qualified investments are satisfactory. During the

evaluation period, HNB had two Community Development Credit Union deposits totaling \$200M, two low-income housing tax credits (LIHTC) totaling over \$3 million, and one Small Business Investment Company investment totaling \$75M. HNB also had \$189M in qualifying donations during the period. The LIHTC investments and donations are described below.

- **Diamond Head Equity Fund**

In 2005, the bank made a \$1 million investment in the Diamond Head Equity Fund, which was invested in five affordable housing projects in Honolulu, Hawaii, and Maui counties. In 2006, the amount increased to \$1.115 million. This project consists of 248-units that are primarily for low- and moderate-income families.

- **Hawaii Housing Finance Equity Fund I, LLC**

In April 2008, the bank made a \$1 million investment into the Hawaii Housing Finance Equity Fund I, LLC, which was formed to invest in low-income residential rental properties located in the State of Hawaii, and to maintain such properties as low-income housing prior to, and to the extent possible, after disposition by the Fund of its interest in such properties. The Fund will construct a 70-unit affordable housing complex in Wahiawa primarily for low- and moderate-income families. In October 2008, the bank agreed to increase its investment to \$2 million.

- **Donations**

Cash donations of over \$189M were made to various organizations during this evaluation period, of which \$58.6M was to Aloha United Way. This organization targets low- and moderate-income people in Hawaii.

## **Extent to Which the Bank Provides Community Development Services**

HNB's record of providing community development (CD) services is satisfactory. HNB's performance in providing CD services in the AA is good. Bank employees have donated a good amount of service time, through their involvement in providing technical assistance in financial matters to various community organizations and programs within the AA. For example, one of the bank's officers serves as the Chairman for a committee that supports small businesses through loans and by providing technical assistance. Also, bank officers spent several hours attending meetings with representatives of the Department of Hawaii Home Land to develop and implement a mortgage program tailored to meet the needs of low- and moderate-income communities. In another instance, a bank officer served as a member of the Small Business Administration Advisory Counsel which promotes services to small businesses and minority businesses, minorities, and start-up businesses.

HNB is an intrastate bank and operates 14 branch offices on three islands. HNB offers a full range of products through its ten full-service branch offices located in the more populated areas of Honolulu, Pearl City, and Kailua on the island of Oahu. Two of these branches are located in low-income tracts and two are located in moderate-

income tracts. The bank operates two full-service branches on the island of Hawaii located in the communities of Hilo and Pauinako. One of these branches is located in a moderate-income tract. And the bank operates two full-service branches on the island of Maui in the communities of Kahului and Kihei. HNB closed the Moanalua Branch on June 28, 2008, in an effort to consolidate operations of two competing branches.

### **Responsiveness to Community Development Needs**

The bank's overall responsiveness through CD activities, CD lending, investment, and services needs, is good. This is supported by the CD services and investments originated during the period. These services and investments help stabilize and support local economies; and, help provide affordable housing to low- and moderate-income families within HNB's assessment area.

### **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.