FDIC State Profile

SPRING 2003

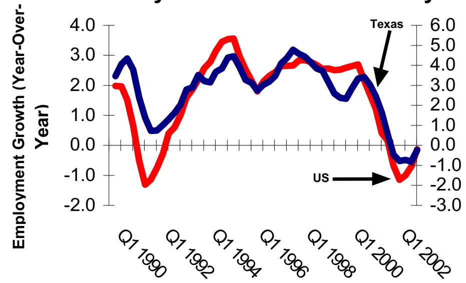
Texas

Employment growth in Texas has mirrored the tepid U.S. recovery, but a state budget deficit could stall the state's recovery.

- Texas employment growth remained negative on a year ago basis as of fourth quarter 2002 (see **Chart 1**). By year end 2002, the Texas unemployment rate had increased to 6.2 percent, slightly higher than the U.S. rate. The government and services sectors posted moderate growth. Employment in the government sector grew 2.17 percent; employment in the services sector grew .02 percent. Employment in other leading industries (manufacturing, transportation and mining) declined. Diversification away from energy and into high-tech benefited the Texas economy during the 1990s expansion. However, the recent downturn in the high-tech sector now represents a major factor in the state's sluggish performance.
- Sluggish employment growth, declines in the stock market, contractions in the manufacturing and high tech sectors, and soaring health care costs have undermined the Texas state budget. The 2003 budget deficit is estimated to be \$1.8 billion, or 5.8 percent of the general state budget, and is projected to double in 2004. In response, the governor has called for a 7 percent reduction in most government programs. Areas with a high share of employment in the local and state government sector will likely be the most affected by these cuts (see **Table 1**).
- Oil and natural gas prices have increased during the past year because of geopolitical tensions in the Middle East, a Venezuelan oil strike, and harsh winter weather across the country. Oil prices increased 67 percent over the 12 months ending January 2003 and exceeded \$35 a barrel in early February. Similarly, natural gas prices more than doubled during the same period (see **Chart 2**). Gasoline prices nationwide averaged \$1.61 in early February, up 50 cents from a year ago.

Despite the rapid rise in oil and natural gas prices, the state's total oil and gas rig count has increased only gradually during the past year because of concerns about the sustainability of higher prices. These concerns contributed to a 5 percent decline in employment in the Texas oil and gas extraction industry for the year ending fourth quarter 2002. Although prolonged uncertainty in the Middle East would be expected to contribute to continued high energy prices, the benefits of any increase in energy sector employment could be offset by higher energy prices for consumers and businesses.

Chart 1: Employment Trends In Texas Closely Track National Economy



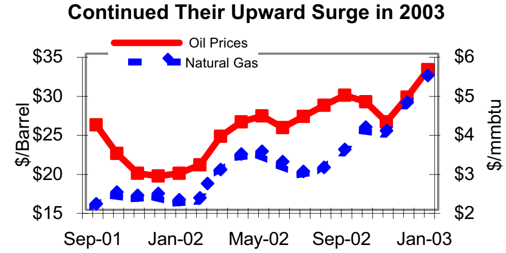
Source: Bureau of Labor Statistics (Haver Analytics)

Table 1: State And Local Government Employment Concentration Top Eight MSAs

MSA Name	Share Of Total Jobs
Bryan-College Station	39.65
Galveston-Texas City	28.67
McAllen-Edinburg-Mission	24.90
Bronwsville-Harlingen-San Benito	21.65
Laredo	21.12
Lubbock	20.97
Austin-San Marcos	20.77
El Paso	20.44

Source: Bureau of Labor Statistics (Haver Analytics)

Chart 2: Oil and Natural Gas Prices Continued Their Upward Surge in 2003



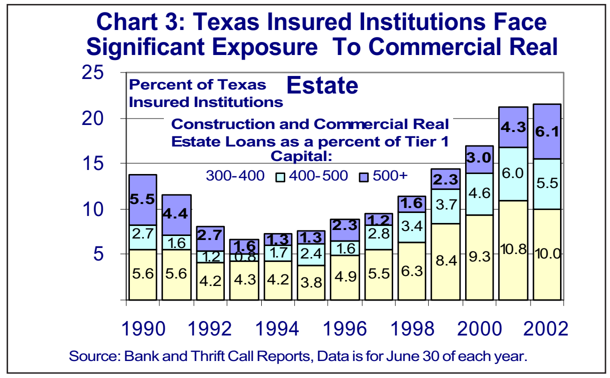
Note: Oil Prices are West Texas Intermediate, Cushing and Natural Gas Prices are Henry Hub, LA.
Source: The Wall Street Journal

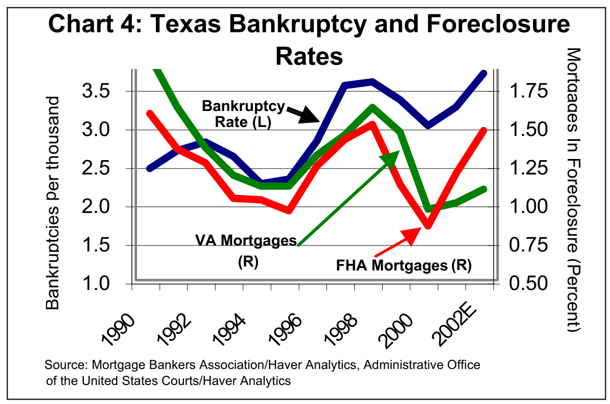
- Agricultural prices remain below the decade average for corn, soybeans and cotton. Prices increased in 2002 after four years of steady declines; however, this was the result of widespread drought conditions, not a reversal in supply and demand imbalances. Therefore, a year of normal production once again could pressure prices below break even levels.

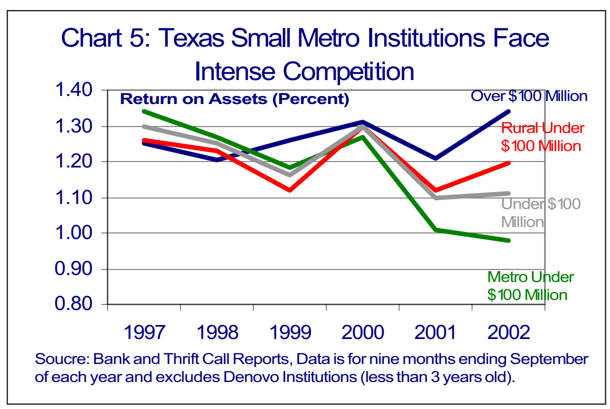
Historically high government subsidy levels are helping to mitigate the effects of low commodity prices and drought-related losses. Subsidies are also helping to bolster farm land values. However, increased dependence on subsidies could pose problems for producers and agricultural lenders if payment levels decline in the future at the same time commodity prices are low.

Insured institutions headquartered in Texas are reporting peak commercial real estate exposures during a time when the state's commercial real estate markets are showing signs of stress.

- Despite sluggishness in the state's economy, insured institutions based in Texas have performed well. The median return on assets for the nine months ending September 30, 2002, was 1.19 percent, up slightly from a year ago. Lower funding costs are contributing to this trend. The cost of earning assets was 1.94 percent, the lowest level in a decade. While past-due rates have increased slightly during the past several years, banks and thrifts report equity plus the allowance for loan and lease losses in excess of 10 percent of assets, a decade high.
- Texas-based insured institutions reported the highest level of commercial real estate loans (non-residential real estate plus construction and development) as of third quarter 2002 (see **Chart 3**). At the same time, the ***Dallas*** and ***Austin*** metro areas reported the highest office vacancy rates in the nation at 25.7 percent. Austin's high office vacancy rate, coinciding with the downturn in the high-tech and telecommunications sectors, surged 20.4 percentage points during the past three years.
- Residential foreclosures in Texas are at a 30-month high. (see **Chart 4**). The per capita bankruptcy rate is also at an all time high. However, insured institutions based in Texas reported an average residential mortgage past-due rate of 2.43 percent as of September 30, 2002, significantly less than industry averages. In addition, past-due rates on other consumer loans at 2.30 percent have increased modestly.
- Small metro banks (assets less than $100 million) headquartered in Texas face intense competition from larger financial institutions. The median ROA reported by small metro institutions as of September 30, 2002, was .98 percent, the lowest level in the past 10 years and lower than that for small rural banks (see **Chart 5**). Relatively higher levels of non interest expense is a contributing factor to the lower levels of profitability reported by small metro banks.
- Weakness in the Texas agricultural industry has continued for several years; however, agricultural banks continue to report strong performance, in large part due to significant levels of government payments. The median return on assets ratio for Texas-based agricultural banks was 1.30 percent for the nine months ending September 30, 2002, in line with performance during the past several years. Past-due and charge-off rates have increased slightly, but remain within the range of the past decade.







Texas at a Glance

General Information	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
Institutions (#)	718	741	774	810	860
Total Assets (in thousands)	211,895,214	192,422,748	225,750,004	232,943,947	227,758,701
New Institutions (# < 3 years)	18	21	30	36	30
New Institutions (# < 9 years)	54	52	48	47	41

Capital	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
Tier 1 Leverage (median)	9.16	9.03	9.29	9.18	9.19

Asset Quality	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
Past-Due and Nonaccrual (median %)	2.16%	2.07%	1.81%	1.95%	2.15%
Past-Due and Nonaccrual ≥ 5%	103	102	83	101	141
ALLL/Total Loans (median %)	1.24%	1.19%	1.20%	1.19%	1.25%
ALLL/Noncurrent Loans (median multiple)	1.54	1.75	2.11	1.82	1.79
Net Loan Losses/Loans (aggregate)	0.39%	0.38%	0.31%	0.41%	0.43%

Earnings	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
Unprofitable Institutions (#)	43	46	36	42	48
Percent Unprofitable	5.99%	6.21%	4.65%	5.19%	5.58%
Return on Assets (median %)	1.19	1.13	1.29	1.18	1.22
25th Percentile	0.74	0.77	0.93	0.80	0.86
Net Interest Margin (median %)	4.52%	4.46%	4.79%	4.50%	4.65%
Yield on Earning Assets (median)	6.43%	7.81%	8.23%	7.65%	8.01%
Cost of Funding Earning Assets (median)	1.96%	3.37%	3.43%	3.13%	3.33%
Provisions to Avg. Assets (median)	0.18%	0.14%	0.14%	0.12%	0.11%
Noninterest Income to Avg. Assets (median)	0.88%	0.87%	0.89%	0.88%	0.86%
Overhead to Avg. Assets (median)	3.36%	3.37%	3.42%	3.35%	3.33%

Liquidity/Sensitivity	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
Loans to Deposits (median %)	63.61%	62.96%	62.12%	58.90%	57.07%
Loans to Assets (median %)	54.90%	54.93%	54.32%	51.57%	49.97%
Brokered Deposits (# of institutions)	59	51	42	41	38
Bro. Deps./Assets (median for above inst.)	3.85%	1.96%	2.51%	2.67%	1.89%
Noncore Funding to Assets (median)	16.47%	16.58%	15.90%	14.81%	13.84%
Core Funding to Assets (median)	71.95%	71.82%	73.02%	74.04%	74.71%

Bank Class	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
State Nonmember	297	303	319	338	361
National	333	346	361	382	404
State Member	42	43	44	39	43
S&L	11	12	10	12	16
Savings Bank	12	13	15	15	17
Mutually Insured	23	24	25	24	19

MSA Distribution	# of Inst.	Assets	% Inst.	% Assets
No MSA	375	33,138,104	52.23%	15.64%
Dallas TX PMSA	79	46,684,958	11.00%	22.03%
Houston TX PMSA	51	28,441,011	7.10%	13.42%
Ft Worth-Arlington TX PMSA	39	7,531,471	5.43%	3.55%
Austin-San Marcos TX	20	2,102,184	2.79%	0.99%
San Antonio TX	18	46,922,966	2.51%	22.14%
Killeen-Temple TX	12	2,349,268	1.67%	1.11%
Longview-Marshall TX	12	1,558,357	1.67%	0.74%
McAllen-Edinburg-Mission TX	11	6,784,121	1.53%	3.20%
Waco TX	11	1,570,849	1.53%	0.74%
Lubbock TX	10	5,330,231	1.39%	2.52%
Corpus Christi TX	8	1,067,392	1.11%	0.50%
Brazoria TX PMSA	7	753,606	0.97%	0.36%
Sherman-Denison TX	7	1,080,816	0.97%	0.51%