FDIC State Profile

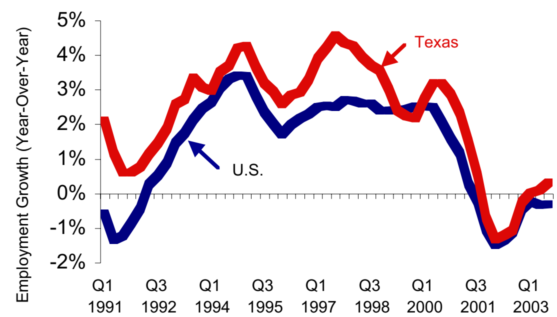
WINTER 2003

Texas

The Texas economy began to emerge from the recession in early 2003, and is now showing signs of strengthening as the national economy gathers momentum.

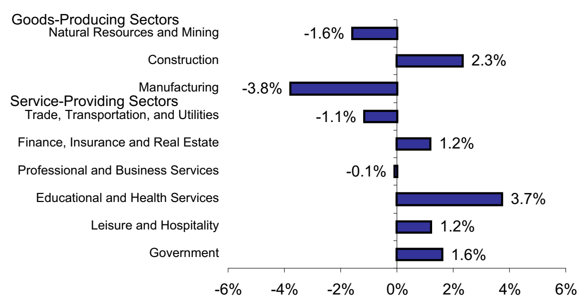
- After mirroring U.S. employment trends in 2002, Texas job growth turned positive in early 2003, resuming its traditional role of outpacing U.S. employment growth rates (see Chart 1).
- However, job losses continued to occur in manufacturing, accelerating in each of the past two quarters, with the most significant losses occurring in industrial machinery, computers, communications equipment, semiconductors, and apparel.
- Manufacturing should begin to stabilize and add jobs sometime in late 2004, because of increased business investment spending and the weaker dollar, which will stimulate Texas exports.

Chart 1: Texas Employment Growth Rate Gradually Accelerating



Source: Bureau of Labor Statistics (Haver Analytics)

Chart 2: Texas Job Growth Concentrated in Service-Providing Sectors



Employment Growth (Third Quarter 2003, Year-Over-Year Percent Change)
Source: Bureau of Labor Statistics (Haver Analytics)

Nonmanufacturing employment should see broad-based gains going forward.

- Federal defense spending will bolster job growth in transportation equipment manufacturing, especially in the ***Fort Worth*** and ***San Antonio*** areas.
- Job losses in the natural resources and mining sector are abating, a result of high energy prices and increased drilling activity. Even so, rig counts are below the level some industry economists associate with current oil prices.
- Educational and health services continued to be the strongest job growth sector in the Texas economy, reflecting largely demographic trends (see Chart 2). However, reductions in state and local government spending and higher college and university tuition rates will somewhat dampen employment gains in education.
- The construction sector recorded the second fastest job growth rate, reaching employment levels not seen since two years ago; residential housing and infrastructure spending were the two major contributors to industry job growth. However, gradually rising mortgage rates, state budget woes, and continuing high commercial vacancy rates are likely to result in only modest gains in construction employment in 2004.

Growth in government, high-technology/telecommunications and tourism should buoy the state economy in 2004.

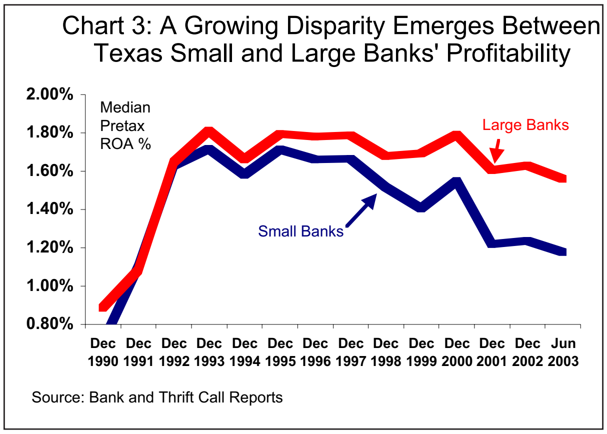
- Growth in government employment continued to expand, but at a gradually declining rate. Spending cutbacks needed to balance the state budget could limit growth in this sector; however, $700 million of new federal money, made available in second quarter 2003, should help offset some of the effects of the state's revenue shortfalls.
- Texas Instruments' announcement that it will build a new $3 billion chip plant in ***Dallas,*** and Motorola's and Samsung's plans to upgrade their chip plants in ***Austin*** bode well for the long-term health of the state's high-tech, telecom, computer and semiconductor industries.

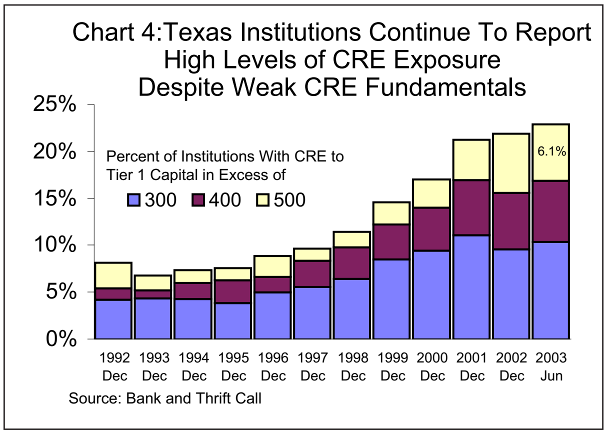
Larger institutions benefit from other noninterest income sources, while small insured institutions face falling profits.

- A sluggish state recovery resulted in **mixed results** for the 708 insured institutions headquartered in Texas. While the median pretax return on assets ratio[1] was 1.38 percent at June 30, 2003, a disparity is growing between small banks (less than $100 million in assets) and larger banks (more than $100 million in assets), especially in metro areas (see Chart 3). Larger metro banks have been more successful in developing other sources of noninterest income and have also recognized more securities gains than small metro banks.

Despite weakness in CRE markets, lenders have not experienced significant deterioration in their portfolios.

- The Dallas metro continued to report the **highest office vacancy rate in the nation** at 27.8 percent as of September 30, 2003. Austin ranked second at 24.8 percent. Houston office vacancy rates were slightly above the national average of 16.9 percent, while Fort Worth office vacancy rates declined 50 basis points to 16.7 percent from one-year ago. Industrial, multifamily, and hotel property types have shown similar signs of weakness.
- Despite continued weakness in **commercial real estate** (CRE) markets, Texas insured institutions reported the highest **concentration of** CRE loans[2] as a percent of Tier 1 capital in a decade (see Chart 4). Notwithstanding this heightened exposure, CRE past-due and charge-off rates remained within five-year averages. The CRE portfolios of banks and thrifts have been insulated from the effects of deteriorating market fundamentals by: 1) low interest rates; 2) the tremendous growth in public, non-governmental mortgage securitization; and 3) greater regulatory oversight and stringent CRE lending standards.[3] While most banks and thrifts headquartered in Texas are not lenders to the largest CRE projects, rising vacancies and increasing unemployment may have negative implications for community bank loan portfolios.





Residential lending continues to exhibit some weakness.

- Texas per capita **bankruptcy rates** continued to hover near record levels, albeit below national averages. Moreover, continued slow employment growth does not suggest a quick recovery. However, consumer loans held by Texas insured institutions continued to report stable past-due and charge-off rates.
- After a constitutional amendment was passed in the September 2003 election, **home equity loans** can now be structured with lines of credit (HELOC). A March 2003 report from the Texas Comptroller of Public Account office estimated Texas consumers would exchange $12.7 billion in existing loans for HELOCs and Texas homeowners could save $741 million in interest charges and federal income taxes annually.

[1] Pretax ROA is used to allow better comparability between regular banking corporations and institutions electing Subchapter S status. Thirty-seven percent of Texas' insured institutions have elected Subchapter S status, which eliminates income tax at the bank level.

[2] Commercial real estate is defined as non-residential real estate, multifamily, and construction and development loans.

[3] Murray, Thomas, "How Long Can Bank Portfolios Withstand Problems in Commercial Real Estate?" *FDIC FYI*, June 23, 2003.

Texas at a Glance

General Information	Jun-03	Jun-02	Jun-01	Jun-00	Jun-99
Institutions (#)	708	723	742	786	821
Total Assets (in thousands)	219,099,564	204,628,477	188,726,153	246,643,848	229,887,863
New Institutions (# < 3 years)	20	17	22	30	36
New Institutions (# < 9 years)	54	53	51	48	46

Capital	Jun-03	Jun-02	Jun-01	Jun-00	Jun-99
Tier 1 Leverage (median)	9.17	9.11	9.09	9.15	8.93

Asset Quality	Jun-03	Jun-02	Jun-01	Jun-00	Jun-99
Past-Due and Nonaccrual (median %)	2.11%	2.00%	2.05%	1.76%	1.99%
Past-Due and Nonaccrual > = 5%	103	93	83	75	109
ALLL/Total Loans (median %)	1.26%	1.25%	1.19%	1.18%	1.22%
ALLL/Noncurrent Loans (median multiple)	1.77	1.81	1.98	2.05	1.93
Net Loan Losses/Loans (aggregate)	0.41%	0.39%	0.36%	0.33%	0.40%

Earnings	Jun-03	Jun-02	Jun-01	Jun-00	Jun-99
Unprofitable Institutions (#)	42	47	36	34	45
Percent Unprofitable	5.93%	6.50%	4.85%	4.33%	5.48%
Return on Assets (median %)	1.06	1.17	1.16	1.28	1.14
25th Percentile	0.68	0.71	0.82	0.92	0.76
Net Interest Margin (median %)	4.25%	4.48%	4.48%	4.79%	4.47%
Yield on Earning Assets (median)	5.74%	6.49%	7.99%	8.15%	7.58%
Cost of Funding Earning Assets (median)	1.47%	2.03%	3.52%	3.34%	3.12%
Provisions to Avg. Assets (median)	0.14%	0.16%	0.13%	0.13%	0.11%
Noninterest Income to Avg. Assets (median)	0.93%	0.87%	0.89%	0.87%	0.87%
Overhead to Avg. Assets (median)	3.33%	3.36%	3.37%	3.43%	3.34%

Liquidity/Sensitivity	Jun-03	Jun-02	Jun-01	Jun-00	Jun-99
Loans to Deposits (median %)	63.69%	63.39%	62.53%	62.14%	56.84%
Loans to Assets (median %)	54.17%	54.86%	54.98%	54.15%	50.39%
Brokered Deposits (# of Institutions)	65	54	49	41	41
Bro. Deps./Assets (median for above inst.)	2.98%	3.28%	1.77%	2.73%	1.95%
Noncore Funding to Assets (median)	16.61%	16.58%	16.78%	15.64%	14.44%
Core Funding to Assets (median)	72.15%	72.23%	72.17%	73.39%	74.44%

Bank Class	Jun-03	Jun-02	Jun-01	Jun-00	Jun-99
State Nonmember	294	298	305	325	343
National	326	335	347	367	392
State Member	42	42	41	43	36
S&L	11	11	12	10	12
Savings Bank	12	13	13	15	15
Mutually Insured	23	24	24	26	23

MSA Distribution	# of Inst.	Assets	% Inst.	% Assets
No MSA	373	34,817,258	52.68%	15.89%
Dallas TX PMSA	76	41,384,781	10.73%	18.89%
Houston TX PMSA	50	29,943,536	7.06%	13.67%
Ft Worth-Arlington TX PMSA	41	8,256,605	5.79%	3.77%
Austin-San Marcos TX	20	3,131,291	2.82%	1.43%
San Antonio TX	17	50,700,804	2.40%	23.14%
Longview-Marshall TX	12	1,594,714	1.69%	0.73%
Killeen-Temple TX	11	2,539,490	1.55%	1.16%
Waco TX	11	1,635,172	1.55%	0.75%
McAllen-Edinburg-Mission TX	10	8,001,131	1.41%	3.65%
Lubbock TX	10	6,549,504	1.41%	2.99%
Corpus Christi TX	8	1,835,033	1.13%	0.84%
Sherman-Denison TX	7	1,161,188	0.99%	0.53%
Tyler TX	7	2,462,844	0.99%	1.12%