Condition of the Texas State Banking System

A Report to the Finance Commission of Texas

March 31, 2009

Prepared by:

Texas Department of Banking
Texas Department of Savings and Mortgage Lending

Financial Data as of December 31, 2008

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Key for Symbols Used Throughout this Report:	**Abbreviations Used Throughout this Report**:
⇧ Improving or strong conditions ⇩ Deteriorating or weak conditions ⇳ Mixed conditions ❖ Interest item	FDIC - Federal Deposit Insurance Corporation OCC - Office of the Comptroller of the Currency FRB - Federal Reserve Board OTS - Office of Thrift Supervision

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ECONOMIC REVIEW AND OUTLOOK
STATE BANKING SYSTEM OF TEXAS

BANKING SYSTEM OVERVIEW

The Texas economy is fortunate in that it is not suffering the same severity or degree of economic stresses that other parts of the country are facing. While no longer robust, the Texas economy continues to show signs of underlying strength and resiliency, and these same characteristics are evident in a majority of our state-chartered banks. Texas banks continue to be better capitalized than U.S. banks as a whole, and have been able to better absorb the impact of the financial market disruptions. The housing market in Texas has softened from a position of strength as short as two years ago, and banks with heavy concentrations in residential construction and land development loans are more vulnerable to declines in this market's activity.

Aided by a resilient state economy, more conservative lending standards and lessons learned from the savings and loan crisis two decades ago, Texas banks continue to hold up comparatively well in the face of tight credit markets and recession. Sheshunoff and Co. Investment Banking, a bank advisory firm, recently released a report that states Texas banks carry fewer problem loans and have more capital than banks elsewhere in the nation. As a result, the national bank bail-out has had a limited impact on Texas so far.

Overall profitability of Texas banks was down during 2008, but still well above national levels. Texas asset quality was strong. The median ratio of bad assets as a portion of a bank's total assets was less than half that for banks nationally. Core capital levels of Texas banks are about 150 basis points higher than the national average.

State-chartered banks in Texas reported net income of $1.1 billion for year end 2008, a decline of $.7 billion from the $1.8 billion the industry earned in 2007. Rising loan-loss provisions and a decreasing net interest margin contributed to this reduction as some banks continue to repair their balance sheets. The number of state-chartered banks declined slightly to 327 from 330 one year earlier. However, assets rose to $164.7 billion from $154.3 billion a year earlier, a 6.7% increase. Loans increased $3.4 billion or 3.3%, while deposits grew slightly by $1.8 billion or 1.6%. Although the volume of nonaccrual loans and other real estate continue to show large increases over 2007 numbers, asset quality remains generally satisfactory overall.

State-chartered thrifts reported $8 million in net income at year end 2008, compared to $76 million the prior year; however, after a CALL report adjustment of $21 million to year-end 2007, net income was adjusted to $55 million, declining by 85% or $46.1 million. Reduced earnings were primarily affected with increased overhead expenses and increased provisions for loan and lease losses, and to a lesser extent, market losses on available for sale securities. While net interest income has improved primarily through improved loan income, compression of the net interest margin continues through falling yields on a greater volume of earning assets. State thrifts reduced total assets by $6 billion or 60% due to a conversion of a thrift to a federal charter in Plano, and the failure of another thrift in Houston, but the number of charters increased by two to twenty-eight. Excluding the two largest thrifts in 2007, total assets increased $978 million or 32%, with 48% of the increase attributed to *de novo*'s or charter conversions. Net loans comprised 63% of the asset growth with investment securities comprising 23 percent. Deposits increased by 30% or $726 million. Nonperforming, nonaccrual loans and other real estate foreclosed total $81 million or 2.0% of total assets, increasing by $30 million or 35 basis points over 2007 numbers, and continue to be monitored by regulators.

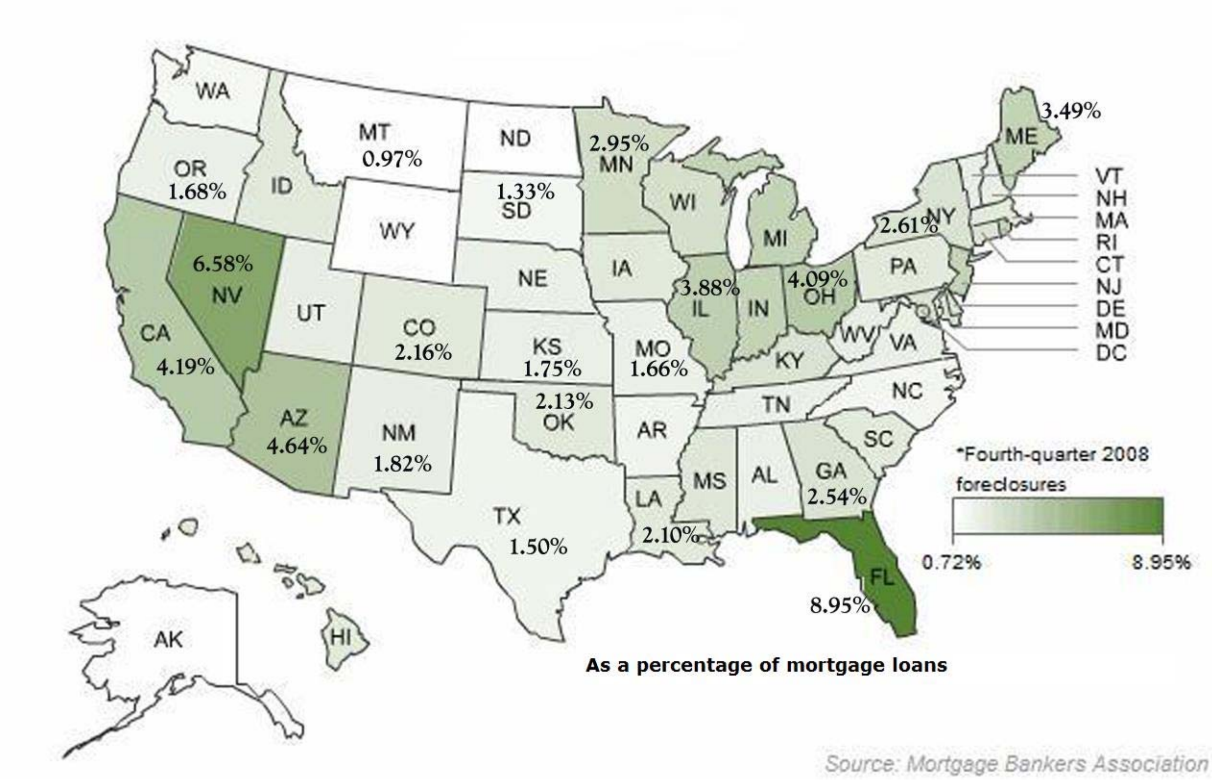
TEXAS ECONOMIC PROFILE

Despite economic conditions nationally, Texas fared better than the U.S. in 2008, as its gross product expanded at a rate twice that of the nation. However, Texas is beginning to feel the effects of the worldwide recession. Although the Texas economy is not as affected by the worldwide recession as other states, the state's economy is showing signs of the effects with an increase in the unemployment rate. Consumer confidence across the nation is at an all time low, with the index standing at 25.0. Texas and surrounding states have experienced similar declines in consumer confidence, and as of February 2009, the regional index fell to 50.0, a decline of 53% for the year.

From December 2007 to December 2008, Texas accounted for 80 percent of all job gains in the nine states that reported increased employment. Over the last year, jobs were added in all industries except information and manufacturing. The state's unemployment rate has been below or at the national rate for over 24 months, rising more slowly than the U.S. average during the year. In January 2009, Texas' unemployment rate was 6.4 percent, compared to the U.S. rate of 8.1 percent. In the 12 month period ending January 2009, Texas gained 19,900 jobs.

Decreases in oil prices are adversely affecting job creation in the Texas oil and natural gas industries. Oil services and machinery contacts reported that drilling activity has declined in response to lower energy prices, with the rig count sharply decreasing from the 2008 levels. Additionally, energy producers are pointing to the national credit crunch as a reason for the declining number of rigs in East Texas.

The national real estate crunch did not affect Texas to the same degree as the rest of the nation since property values did not inflate to the same extent as in other states. However, sales and construction activity are slowing and the state's housing conditions remain weak. Existing home sales fell by 27 percent in the last year. The median home price also declined; however, it was not in the double digits as experienced in other states. The number of mortgage foreclosures continued to fall between December 2007 and December 2008, while the U.S. count rose. According to a recent release from the Mortgage Bankers Association, Texas' foreclosure rate in the fourth quarter is minimal compared to Florida, Arizona, Nevada, and California. As of February 2009, the Texas foreclosure rate was one in every 896 mortgages. Comparable rates in other states include Nevada's one in 70, California's one in 165 and Arizona's one in 147.



Retailers, including discount stores, and auto dealers reported across the board declines. While weaknesses are reported in almost every aspect of the Texas economy, a slight increase in the sales of used vehicles and repair services is noted. The financial services sector reports maintaining tight credit standards, and most show generally stable deposits with the slowdown in loan demand being broad-based.

STATE CHARTERED BANKING PROFILE

During the last half of 2008, the number of Texas state-chartered banks declined by two, to 327. Two charters were merged into other state-chartered banks, while one new bank opened -- Liberty Capital Bank, Addison, Texas. The conversions of The Bank of Crowley, Crowley, Texas and First Bank of Snook, Snook, into state savings banks were offset by the conversions to state banks of Fidelity Bank, N.A., Plano (as Fidelity Bank) and Snyder National Bank, Snyder (as Community Bank of Snyder). The second loss was the result of the failure of Sanderson State Bank, Sanderson, Texas. Its deposits were acquired by The Pecos County State Bank, Fort Stockton, Texas. For the near future, the number of Texas state banks is expected to remain relatively stable, with at least two new banks -- First Bandera State Bank, Bandera, Texas, and R Bank, Round Rock, Texas -- opening in the first half of 2009.

Texas state bank assets for the last half of 2008 increased by $10.8 billion, or 14% (annualized). While a significant part of this increase can be attributed to the acquisition of the failed Franklin Bank, S.S.B., Houston, Texas, by Prosperity Bank, El Campo, Texas, the size of the increase (disregarding Prosperity, the increase was still over 11%), as well as the fact that a disproportionate amount occurred in the last quarter of 2008, seems to indicate that Texas state banks were perceived as relatively "safe harbors" amidst the swirling negative publicity about the large national financial institutions and the unprecedented federal efforts to stabilize them, and the general downturn in the stock market and real estate market.

SELECT FEDERAL ASSISTANCE PROGRAMS

In an effort to stabilize and strengthen the financial services sectors, the federal government instituted the Troubled Asset Relief Program (TARP) designed to purchase assets and equity from financial institutions. From TARP emerged a number of assistance programs from the various federal agencies to steady the country's financial system.

The Capital Purchase Program (CPP) was announced by the U.S. Treasury Department on October 14, 2008. The program's primary purpose is to inject capital into the U.S. banking system. In the months following the Treasury announcement, a series of three capital investment facilities were developed for banks with different organizational structures beginning with publicly held institutions. Terms for capital injections applicable to non-publicly traded institutions were announced next, and lastly terms for Subchapter S corporations were released on January 14, 2009. The Treasury and the other federal regulators have been reviewing and approving bank applications for these funds beginning with the larger publicly traded financial institutions. As of March 31, 2009, only 17 Texas based financial institutions are shown to have received TARP-CPP funds in the amount of $2.8 billion.

The FDIC implemented the Temporary Liquidity Guarantee Program to strengthen confidence and encourage liquidity in the U.S. banking system. There are two components of the program: 1) the Temporary Debt Guarantee Program guarantees all newly issued senior unsecured debt of banks, thrifts, and certain holding companies; and, 2) the Transaction Account Guarantee Component which provides for full coverage of non-interest (or low interest) bearing deposit transaction accounts, regardless of dollar amount. This program is in addition to the temporary and automatic increase in the level of FDIC deposit insurance available per depositor up to $250,000 through the end of 2009.

Temporary Debt Guarantee

Type	*Opted Out
State-Chartered	172
National	124
State Savings Banks	12
Federal Savings Banks	6
Holding Companies	180

*Source: FDIC website as of February 12, 2009

Transaction Account Guarantee
While most FDIC insured entities are participating in this program, over 1000 have opted out, including 81 Texas chartered financial institutions - 29 national banks and 41 state-chartered banks. The coverage will last through December 31, 2009, for banks not opting out. (Source: FDIC as of February 12, 2009)

SUPERVISORY CONCERNS

The nation's economic and financial conditions were under distress in 2008. Mortgage giants Fannie Mae and Freddie Mac were seized by the government, Merrill Lynch was sold in distress, and the 158-year-old investment bank Lehman Brothers failed. In October 2008, the Dow fell 18 percent - its worst week in history – and at that point, $8 trillion in equity value had been lost. Despite these events, the Texas banking system is considered sound. Most Texas banks did not participate in the high risk lending practices that fueled the crisis; however, Texas banks are beginning to feel the effects of the national recession.

Competition for quality consumers will require Texas bankers to exercise higher levels of diligence in all banking activities to ensure prudent decisions are made and sound practices followed. The national recession is affecting some borrowers who are beginning to experience difficulties in repaying debt obligations, which in turn is resulting in higher past due and default rates. The Texas housing market did not fluctuate at the same levels as other states; however, trends show that the market is experiencing declining home sales and pricing.

Supervisory concerns not only involve the current economic and financial crisis but include corporate governance; bank holding company strength; Bank Secrecy Act and USA Patriot Act compliance; fraud; liquidity management and home equity lending. The Texas Department of Banking and the Texas Savings and Mortgage Lending Department are diligently monitoring each of these areas to ensure that any changes or disruptions receive prompt corrective action.

During a weak economic climate, liquidity is critical to the solvency of a distressed financial institution and system. If a financial institution maintains strong asset quality, earnings, and capital but is unable to satisfy its liquidity needs, it runs the risk of failure. Other crucial elements of strong liquidity management are a strong analysis of funding requirements under alternative scenarios, diversification of funding sources, and contingency planning.

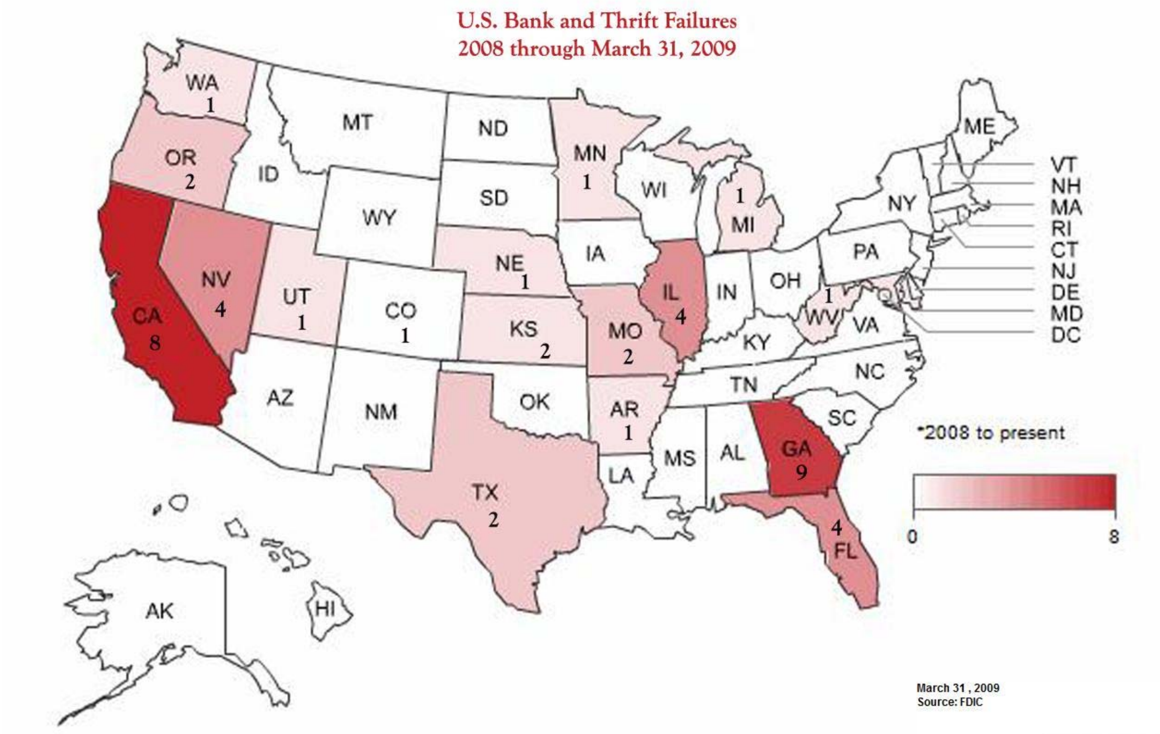
Declining commercial real estate markets can place additional pressure on already strained financial institutions and markets. Overcoming problems in the financial sector is central to achieving economic recovery. The Department is prescribing a path of prudence and caution in situations regarding concentration risk. Those institutions that engage heavily in real estate construction and development financing are being encouraged to counter their risk with additional capital support in case economic stresses accelerate in Texas. The Department of Banking is participating with the FDIC in targeted horizontal examinations of financial institutions with high levels of commercial real estate. Thus far, these examinations are proving helpful to regulators by providing a mechanism to react promptly to any erosion in asset quality. Increased bank failures could result if problem loans are not identified in a timely manner, or funding sources are not properly managed.

How bank management identifies, monitors and controls these various risk elements significantly influences how the Department responds to these supervisory concerns. Supervisors will remain alert to emerging trends, as bank performance typically lags behind unfavorable conditions. Consequently, bank and thrift supervisors must continue to look ahead for potentially damaging factors that may weaken borrowers' repayment ability and subsequently erode the asset quality of financial institutions. Financial institutions that recognize these factors early and are quick to respond, can dramatically improve their chances to minimize their loss exposure.

SUPERVISORY MEASURES BEING TAKEN BY THE DEPARTMENT OF BANKING

The Department continues to be extremely sensitive to the state of the economy. The supervisory practices of the agency are designed to identify trends in the industry as a whole, and practices of individual banks that could threaten the safety and soundness of an institution or the industry. The Department continues to closely monitor and identify concerns surrounding the stability of our financial institutions and is sensitive to identifying individual banks that demonstrate difficulty. Examiners will review institutional exposure to the changing economic conditions and take action to limit risk, when necessary.

Although the majority of institutions are meeting the current economic challenges, the number of problem financial institutions will likely increase over the next six to twelve months, as regulators know that financial problems in institutions often lag behind economic instability. The number of financial institution failures has increased throughout the nation, however, only two financial institutions failed in Texas between January 2008 and March 2009. Problem status can sometimes be prevented, or a quick turnaround implemented, by timely regulatory identification and positive management response.



The Department's staff is performing the following:

- ❖ Frequent conference calls with other state and federal regulators;
- ❖ Monthly calls to state banks to obtain industry input on prevailing economic conditions;
- ❖ Conducting horizontal (targeted) reviews of high risk area, such as commercial real estate and exposure to the devaluation of private-label collateralized mortgage obligations;
- ❖ Expanded off-site monitoring to include areas of greatest concerns;
- ❖ Revising bank examination review procedures with a greater focus on risk assessment;
- ❖ Monitoring and evaluating asset concentrations, liquidity, and funding sources;
- ❖ Increasing scrutiny of bank contingency plans that may be implemented during a catastrophic event, like the hurricanes along the Gulf of Mexico;
- ❖ Frequent communication with state legislators and congressional representatives;
- ❖ Internal monitoring of state, national, and world political and economic events impacting the industry such as federal bailouts designed to stabilize the financial market;
- ❖ Increasing internal communication for examiner awareness of issues.

SUPERVISORY MEASURES BEING TAKEN BY THE DEPARTMENT OF SAVINGS AND MORTGAGE LENDING

State-chartered thrift assets under the Department's jurisdiction totaled $3.99 billion as of December 31, 2008, and decreased by 59.9% or $5.15 billion from June 30, 2008's balance of $9.14 billion. The total number of state chartered savings banks at December 31, 2008 is twenty-eight, increasing by one new charter since June 30, 2008. Charter changes that have occurred during the six month period include: (1) the conversion of The Bank of Crowley, Crowley, to Texas Exchange Bank, SSB, effective September 15, 2008; (2) the conversion of First Bank of Snook, Snook, Texas, to Spirit of Texas Bank SSB, College Station, effective November 17, 2008; and, (3) the closure of Franklin Bank, SSB, Houston, with the Federal Deposit Insurance Corporation's appointment as receiver effective November 7, 2008.

Major application activities included one *de novo* application, from One Earth Bank, SSB, Austin, Texas filed September 16, 2008. This application was subsequently withdrawn March 27, 2009. The total industry is projected to remain at the current level in number and in total assets; however, several state savings banks could have the potential for asset contraction.

The Departments' supervisory monitoring and enforcement staff will take the following actions:

- ❖ Regular conference calls and close coordination with other state and federal regulators;

- Quarterly analysis of Call Report financial data including telephone inquiries of thrift management for explanation of unusual items and variation in quarterly operating results;
- Off-site monitoring of each institution's activity (i.e., regulatory correspondence and approvals, independent audit reports, reports of examination, and institution responses to examination comments, criticisms and recommendations);
- Joint review by the FDIC and the Department of savings bank's contingency / disaster recovery plans;
- Regular assessments of each institution's activities, strengths and weaknesses, and revising the Department's plan of examination and monitoring for the institution, including the downgrading of institutions if deemed necessary by the Department and the FDIC;
- Monitoring increased foreclosure activity and changes in the housing market;
- Working with various community groups on foreclosure prevention / education;
- Reviewing concentrations in commercial real estate and monitor with Commercial Real Estate Lending Joint Guidance, issued December 12, 2006;
- Internal monitoring of local, state, national and world political and economic events impacting the industry, including recent events bailouts and major financial market changes; and,
- Monitoring of any state savings banks' participation in the U.S. Treasury's Troubled Asset Relief Program and Capital Purchase Program, and the Federal Deposit Insurance Corporation's (FDIC's) Temporary Liquidity Guarantee Program (TLGP), and other effects of the Emergency Economic Stabilization Act of 2008 (EESA), and proposals for increased FDIC assessments.

PERFORMANCE SUMMARY AND PROFILE
TEXAS BANKING SYSTEM

In 2008, banking industry indicators deteriorated for both Texas and the nation. However, it is noted that Texas banks carry fewer problem loans and have more capital than banks in other states.

State-chartered banks saw an increase in assets over $10 billion or 6.7% from year end 2007 and a reported net income of $1.1 billion for year end 2008. The economic stresses added to the erosion of the return on assets (ROA) for state-chartered banks, declining from 0.90% in June 2008 to 0.70% at year-end. While this performance ratio is not as good, it remains acceptable considering the nation's ROA of 0.21% as of December 31, 2008. There has been a significant increase in the percentage of unprofitable institutions to 15.90% from 9.70% the same time last year, but eleven new institutions opened in 2008 and historically they take 24 to 36 months to become profitable. In 2008 state thrifts observed $8 million in net income, but a 60% or $6 billion decrease in assets due to a thrift failure and a charter conversion. ROA for thrifts increased to 0.23% at year-end 2008, up from the negative 2.87% in June 2008 that was also primarily affected by a thrift's failure. Eliminating such factors, December 2008 thrift ROA compared to June 30, 2008's would have declined 21 basis points and net interest income to average assets would have declined by 10 basis points, impacted by declining yields on earning assets that declined 31 basis points. The level of unprofitable savings banks would have also increased from 34.6% at June 2008 to 42.9% at year-end 2008. Nearly 29% of savings bank's are newer chartered, reorganized or converted which further influences the profitability ratio. Provisions for loan and lease losses to average assets would have been the same 0.45% of average assets with a decline of only 3 basis points to 1.07% to total loans between June 30, 2008 and December 31, 2008. Non-interest income and non-interest expenses to average assets would have also declined by 15 and 11 basis points, respectively. Losses on securities would have increased by 13 basis points.

Texas banks are better able to absorb losses under difficult conditions as is illustrated by the regulatory capital levels of Texas banks, which are higher than the national average. For December 31, 2008, state-chartered banks show a leverage (core) capital ratio of 8.91%. Although the capital protection decreased slightly in 2008, it continues to exceed the highest regulatory capital standards. State thrifts experienced a 289 basis point increase in their regulatory capital levels between June and December 2008 to 10.65% from 7.76% six months earlier. However, adjusting for the failed thrift, core capital would have been 11.08% for June 2008, and 11.77% for December 2007, excluding the two largest thrifts for 2007, resulting in a decline of 43 and 112 basis points, respectively, for June 2008 and December 2008. The decline in thrift capital ratio is due to the continued asset expansion of activity of *de novo* savings banks. Thrifts also continue to exceed the national capital ratios for all savings institutions, that was 8.09% for year-end 2008, 9.77% for June 30, 2008, and 9.97 for December 31, 2007.

Net interests margins have remained stable for state-chartered banks, declining only 3 basis points from the June 2008 level of 3.66%. State thrifts posted a 139 basis point increase from 2.39% in June 2008 to 3.78% at year end, however, after adjusting for the variance of the failed thrift, the net interest margin would have been 3.86% for June 2008, declining by 8 basis points compared to year-end. Year to date provisions to the allowance for loan losses increased for state banks but declined for thrifts. State banks increased their provisions $545 million over six months to end 2008 with $978 million. Thrifts provisions were $16 million, down from the $73 million reflected in June 2008; however, after adjusting as previously stated, provisions would have increased by nearly $9 million. The thrift allowances for loan and lease losses to non-current loans and leases, presently at 46.86%, continues to be less than the national ratio of 53.09% and the state federally chartered thrifts ratio of 67.36%. Some of the increase in the provision for state banks is attributed to one financial institution with branches in other markets outside of Texas that is taking additional precautions.

Although the volume of nonaccrual loans and other real estate continues to show increases over 2007 numbers, overall asset quality remains satisfactory. Banks' noncurrent assets plus other real estate owned to total assets increased 63 basis points over year end 2007 to 1.28%. Thrifts decreased 136 basis points to a total of 2.04% at December 2008 in noncurrent loans plus other real estate owned to total assets. Adjusting for the reasons stated previously, the June 2008 ratio would have been 1.74%. Further excluding the two largest thrifts at year-end 2007 would have resulted in a 1.69% ratio, indicating a 30 basis point increase between June and December 2008 and a 35 basis point increase since December 2007.

Noncurrent loans—those 90 days or more past due, plus those no longer accruing interest—continued to increase. The trend exhibited by state-chartered banks in 2008 reinforces that asset quality is weakening. In December 2008, banks' noncurrent loans to loans were 1.63%, an increase from 1.30% in June 2008. Thrifts experienced a decrease from 7.63% in June 2008 to 2.36% at year end. The variance between the period is due to the circumstances previously described. Adjusting for the failed thrift results in a non-current assets to loan ratio of 1.98% and 1.99% for June 30, 2008 period and 2007 year-end, respectively.

Given the current economic conditions, the overall charge-off levels for both banks and thrifts are not unreasonable. Net loan charge-offs increased significantly from June 2008 for state-chartered banks to $639 million, with 45% of the net charge-offs being related to construction and land development. One reason for the increase is due to one financial institution with branches in other markets outside of Texas that have been affected by the global financial crisis. Net charge-offs decreased significantly for thrifts, declining from $60 million in June 2008, to $8 million at year end. As with banks, a considerable portion of the net charge-offs (57%), are related to construction and land development loans. Given the unprecedented economic situation, loss reserves appear to be adequate for both banks and thrifts. Reserves now represent 1.31% of loans for banks and 1.10% for savings institutions. This is a slight increase for state banks of 7 basis points and a 32 basis point decrease for savings institutions since June 2008.

Number of Institutions and Total Assets

	12-31-2008 No. of Institutions	12-31-2008 Assets	12-31-2007 No. of Institutions	12-31-2007 Assets	Difference No. of Institutions	Difference Assets
Texas State-Chartered Banks	327	$164.7	330	$154.3	-3	+$10.4
Texas State-Chartered Thrifts	28	$4.0	26	$10.0	+2	-$6.0
	355	$168.7	356	$164.3	-1	+$4.4
Other states' state-chartered:						
Banks operating in Texas*	23	$28.1	18	$15.2	+5	+$12.9
Thrifts operating in Texas*	0	0	0	0	0	0
	23	$28.1	18	$15.2	+5	+$12.9
Total State Chartered Activity	378	$196.8	374	$179.5	+4	+$17.3
National Banks Chartered in Texas	267	$108.8	282	$107.3	-15	+$1.5
Federal Thrifts Chartered in Texas	22	$87.6	21	$74.3	+1	+$13.3
	289	$196.4	303	$181.6	-14	+$14.8
Other states' federally-chartered:						
Banks operating in Texas*	21	$181.7	22	$165.1	-1	+$16.6
Thrifts operating in Texas*	11	$73.6	12	$75.0	-1	-$1.4
	32	$255.3	34	$240.1	-2	+$15.2
Total Federally-Chartered Activity	321	$451.7	337	$421.7	-16	+$30.0
Total Banking/Thrift Activity	699	$648.5	711	$601.2	-12	+$47.3

Assets in Billions

**Indicates estimates based on available FDIC information.*

Ratio Analysis

As of December 31, 2008

	State-Chartered Banks	Texas National Banks	All Texas Banks	State-Chartered Thrifts	Texas Federal Thrifts	All Texas Thrifts
Number of Banks-------------------------→	*327*	*267*	*594*	*28*	*22*	*50*
% of Unprofitable Institutions	15.90%	11.99%	14.14%	42.86%	31.82%	38.00%
% of Institutions with Earnings Gains	40.37%	45.69%	42.76%	35.71%	40.91%	38.00%
Yield on Earning Assets	5.70%	6.08%	5.85%	6.49%	3.87%	3.97%
Net Interest Margin	3.63%	4.12%	3.82%	3.78%	2.22%	2.28%
Return on Assets	0.70%	1.00%	0.82%	0.23%	-0.16%	-0.15%
Return on Equity	7.04%	8.96%	7.86%	2.05%	-2.11%	-1.86%
Net Charge-offs to Loans	0.61%	0.33%	0.50%	0.35%	1.01%	0.98%
Earnings Coverage of Net Loan C/Os	3.75	8.58	5.00	3.55	1.82	1.84
Loss Allowance to Loans	1.31%	1.30%	1.31%	1.10%	1.97%	1.93%
Loss Allowance to Noncurrent Loans	80.58%	115.99%	91.62%	46.86%	67.36%	66.56%
Noncurrent Assets+OREO to Assets	1.28%	0.94%	1.14%	2.04%	1.87%	1.87%
Net Loans and Leases to Core Deps	118.02%	103.04%	111.58%	107.65%	120.12%	119.45%
Equity Capital to Assets	9.77%	11.36%	10.40%	10.90%	7.52%	7.67%
Core Capital (Leverage) Ratio	8.91%	8.98%	8.94%	10.65%	7.96%	8.07%

Data for other state chartered institutions doing business in Texas is not available and therefore excluded.

Comparison Report

Select Balance Sheet and Income/Expense Information

As of December 31, 2008

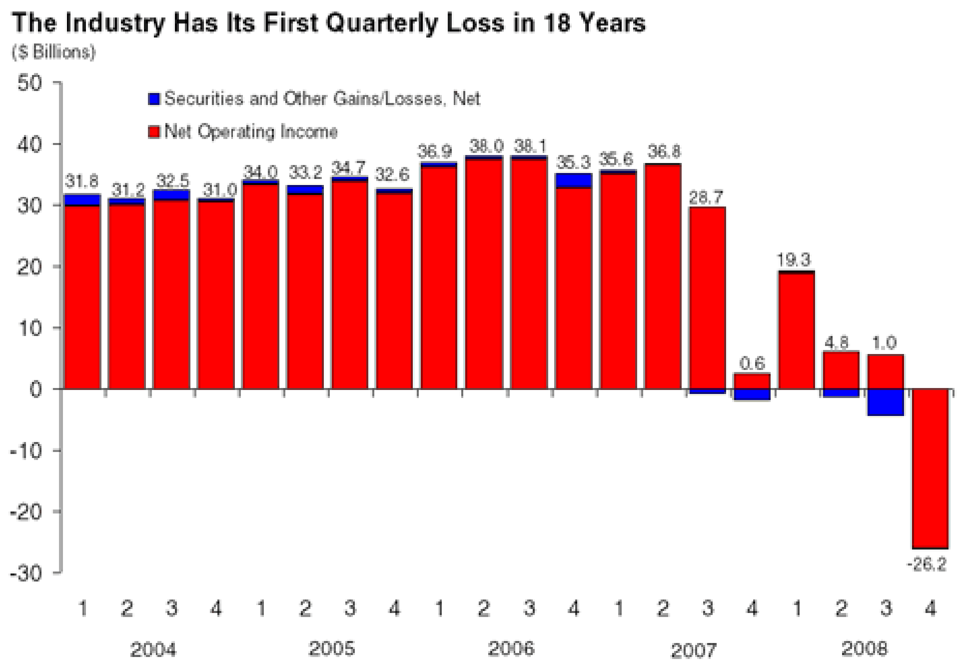
	State Banks*		State Thrifts	
	End of Period	% of Total Assets	End of Period	% of Total Assets
Number of Institutions	327		28	
Number of Employees (full-time equivalent)	35,834		974	
(In millions)				
Total Assets	$164,676		$3,988	
Net Loans and Leases	$107,320	65.17%	$2,526	63.32%
Loan Loss Allowance	$1,429	0.87%	$28	0.71%
Other Real Estate Owned	$329	0.20%	$22	0.57%
Goodwill and Other Intangibles	$2,170	1.32%	$20	0.51%
Total Deposits	$118,490	71.95%	$3,120	78.22%
Federal Funds Purchased and Repurchase Agreements	$4,795	2.91%	$12	0.30%
Other Borrowed Funds	$20,413	12.40%	$398	9.98%
Equity Capital	$16,083	9.77%	$435	10.90%
Memoranda:				
Noncurrent Loans and Leases	$1,773	1.08%	$60	1.51%
Earning Assets	$149,047	90.51%	$3,648	91.47%
Long-term Assets (5+ years)	$32,401	19.68%	$1,131	28.35%
	Year-to Date	% of Avg. Assets	Year-to Date	% of Avg. Assets
Total Interest Income	$7,963	5.15%	$215	5.99%
Total Interest Expense	$2,900	1.88%	$90	2.50%
Net Interest Income	$5,063	3.27%	$125	3.48%
Provision for Loan and Lease Losses	$978	0.63%	$16	0.45%
Total Noninterest Income	$1,929	1.25%	$18	0.51%
Total Noninterest Expense	$4,595	2.97%	$114	3.17%
Securities Gains	-$24	-0.02%	-$3	-0.09%
Net Income	$1,086	0.70%	$8	0.23%
Memoranda:				
Net Loan Charge-offs	$639	0.41%	$8	0.22%
Cash Dividends	$667	0.43%	$8	0.23%

* *Excludes branches of state-chartered banks of other states doing business in Texas. As of 12-31-08 an estimate is twenty three institutions with $28.1 billion in assets. No branches of state-chartered thrifts of other states conducted business in Texas as of 12-31-08.*

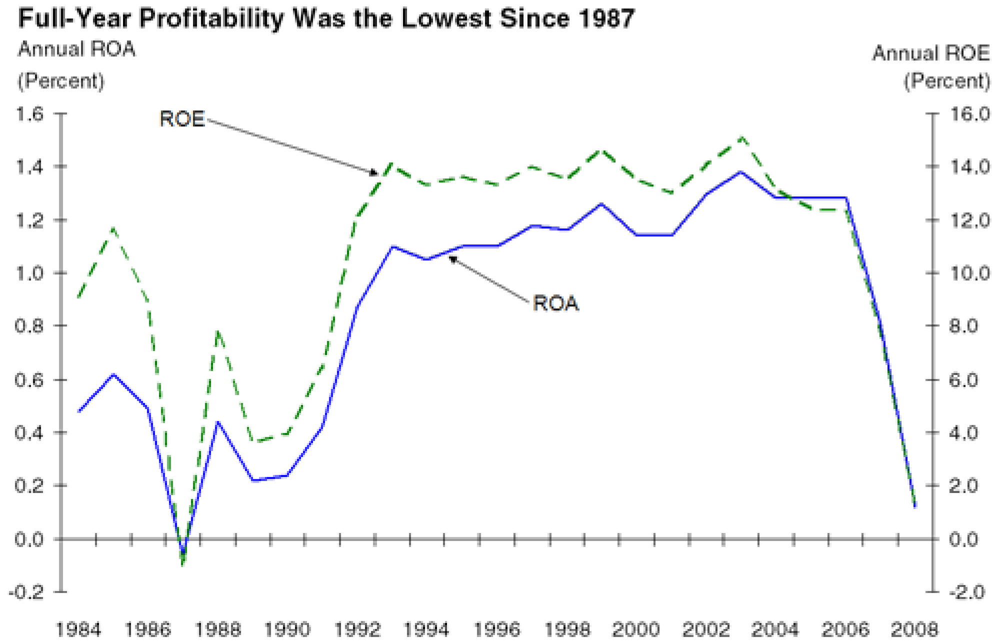
PERFORMANCE SUMMARY
UNITED STATES BANKING SYSTEM

Quarterly Banking Profile – National Level
Fourth Quarter 2008
Federal Deposit Insurance Corporation

⇩ **Earnings Performance** – Expenses associated with rising loan losses and declining asset values overwhelmed revenues in the fourth quarter of 2008, producing a net loss of $26.2 billion at insured commercial banks and savings institutions. This is the first time since the fourth quarter of 1990 that the industry has posted an aggregate net loss for a quarter. The -0.77 percent quarterly return on assets (ROA) is the worst since the -1.10 percent in the second quarter of 1987. A year ago, the industry reported $575 million in profits and an ROA of 0.02 percent. High expenses for loan-loss provisions, sizable losses in trading accounts, and large writedowns of goodwill and other assets all contributed to the industry's net loss. A few very large losses were reported during the quarter - four institutions accounted for half of the total industry loss- but earnings problems were widespread. Almost one out of every three institutions (32 percent) reported a net loss in the fourth quarter. Only 36 percent of institutions reported year-over-year increases in quarterly earnings, and only 34 percent reported higher quarterly ROAs.

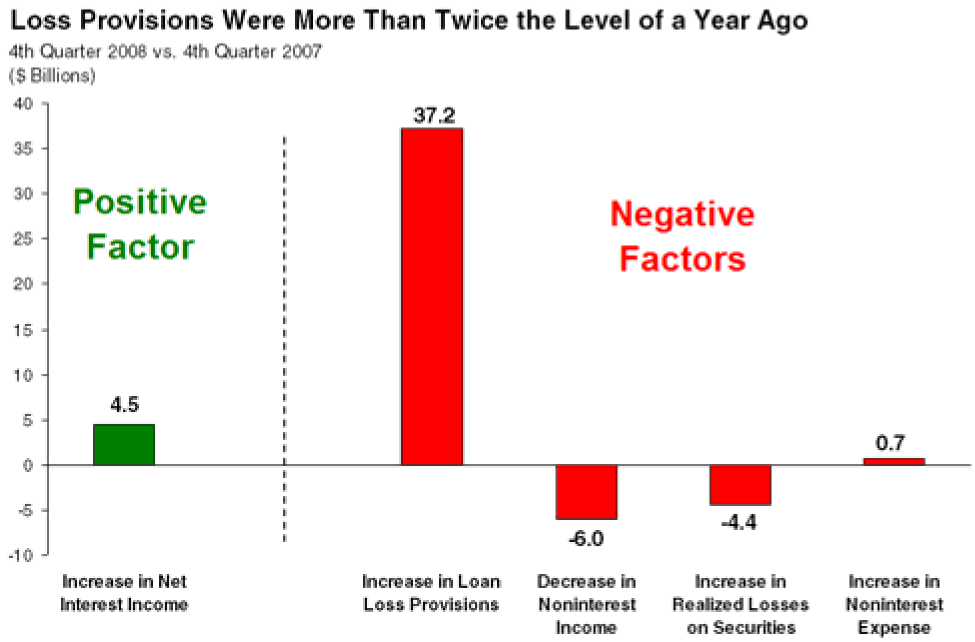


⇩ **Earnings Fall to Lowest Level in 18 Years** - Net income for all of 2008 was $16.1 billion, a decline of $83.9 billion (83.9 percent) from the $100 billion the industry earned in 2007. This is the lowest annual earnings total since 1990, when the industry earned $11.3 billion. The ROA for the year was 0.12 percent, the lowest since 1987, when the industry reported a net loss. Almost one in four institutions (23.4 percent) was unprofitable in 2008, and almost two out of every three institutions (62.5 percent) reported lower full-year earnings than in 2007. Loss provisions totaled $174.3 billion in 2008, an increase of $105.1 billion (151.9 percent) compared to 2007. Total noninterest income was $25.5 billion (10.9 percent) lower as a result of the industry's first-ever full-year trading loss ($1.8 billion), a $5.8-billion (27.4 percent) decline in securitization income, and a $6.8-billion negative swing in proceeds from sales of loans, foreclosed properties and other assets. As low as the full-year earnings total was, it could easily have been worse. If the effect of failures and purchase accounting for mergers that occurred during the year is excluded from reported results, the industry would have posted a net loss in 2008. The magnitude of many year-over-year income and expense comparisons is muted by the impact of these structural changes and their accounting treatments.



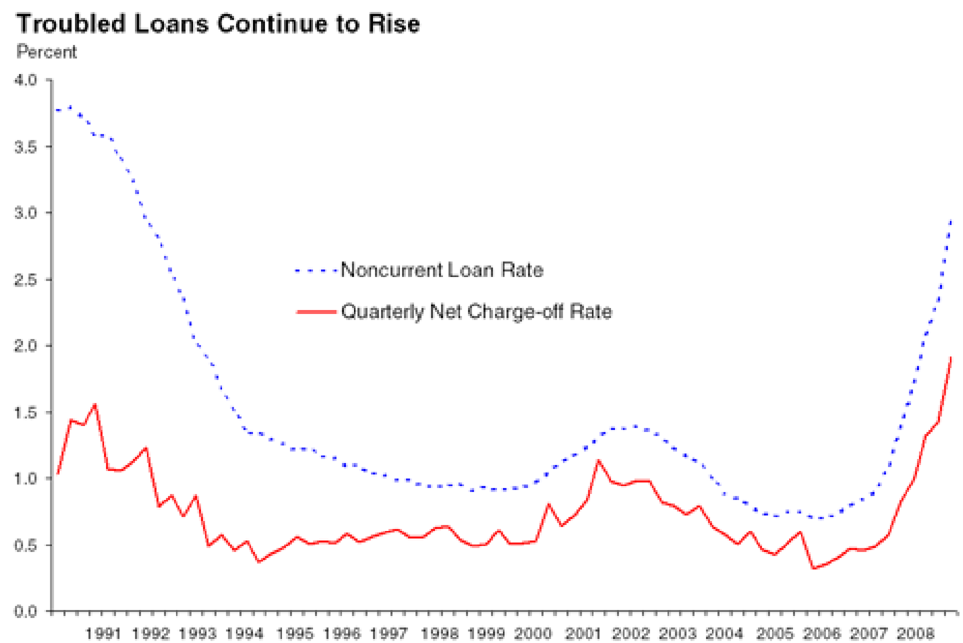
⇳ **<u>Net Interest Margins</u>** - Net interest income totaled $97.0 billion in the fourth quarter, an increase of $4.5 billion (4.9 percent) from the fourth quarter of 2007. The average net interest margin (NIM) was 3.34 percent in the quarter, up slightly from 3.32 percent a year earlier but lower than the 3.37 percent average in the third quarter. The year-over-year margin improvement was confined mostly to larger institutions. More than half of all institutions (56 percent) reported lower NIMs. At institutions with less than $1 billion in assets, the average margin was 3.66 percent, compared to 3.85 percent a year earlier and 3.78 percent in the third quarter. This is the lowest quarterly NIM for this size group of institutions since the second quarter of 1988. At larger institutions, the average NIM improved from 3.24 percent a year earlier to 3.30 percent, slightly below the 3.32 percent average of the third quarter. When short-term interest rates are low and declining, it is more difficult for banks to reduce the rates they pay for deposits without causing deposit outflows. The cost of short-term nondeposit liabilities, in contrast, tends to follow movements in short-term interest rates more closely. Community banks fund more than two-thirds of their assets with domestic interest-bearing deposits, whereas larger institutions fund less than half of their assets with these deposits. As rates fell in the fourth quarter, average funding costs declined at larger institutions but remained unchanged at community banks.

⇩ **Provisions for Loan Losses** –Insured banks and thrifts set aside $69.3 billion in provisions for loan and lease losses during the fourth quarter, more than twice the $32.1 billion that they set aside in the fourth quarter of 2007. Loss provisions represented 50.2 percent of the industry's net operating revenue (net interest income plus total noninterest income), the highest proportion since the second quarter of 1987 when provisions absorbed 53.2 percent of net operating revenue.



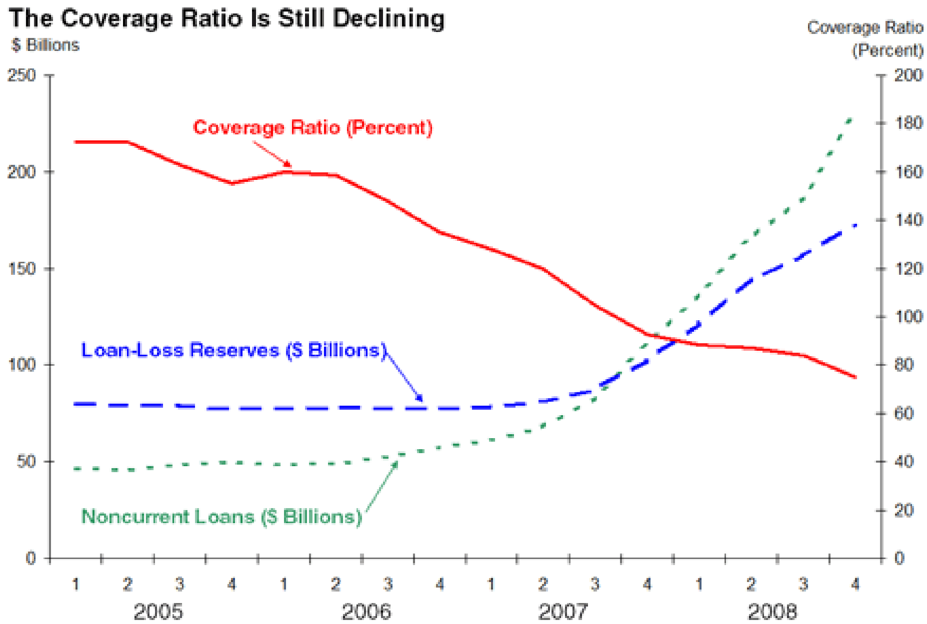
⇩ **Net Charge-Offs** - Net loan and lease charge-offs totaled $37.9 billion in the fourth quarter, an increase of $21.6 billion (132.2 percent) from the fourth quarter of 2007. The annualized quarterly net charge-off rate was 1.91 percent, equaling the highest level in the 25 years that institutions have reported quarterly net charge-offs (the only other time the charge-off rate reached this level was in the fourth quarter of 1989). The year-over-year increase in quarterly net charge-offs was led by real estate construction and development loans (up $6.1 billion, or 448.1 percent), closed-end 1-4 family residential mortgage loans (up $4.6 billion, or 206.1 percent), commercial and industrial (C&I) loans (up $3.0 billion, or 97.3 percent), and credit cards (up $2.5 billion, or 60.1 percent). Charge-offs in all major loan categories increased from a year ago. Real estate loans accounted for almost two-thirds of the total increase in charge-offs (64.7 percent).

⇩ **Noncurrent Loans** - The amount of loans and leases that were noncurrent rose sharply in the fourth quarter, increasing by $44.1 billion (23.7 percent). Noncurrent loans totaled $230.7 billion at year-end, up from $186.6 billion at the end of the third quarter. More than two-thirds of the increase during the quarter (69.3 percent) came from loans secured by real estate. Noncurrent closed-end 1-4 family residential mortgages increased by $18.5 billion (24.1 percent) during the quarter, while noncurrent C&I loans rose by $7.6 billion (43.0 percent). Noncurrent home equity loans increased by $3.0 billion (39.0 percent), and noncurrent loans secured by nonfarm nonresidential real estate increased by $2.9 billion (20.2 percent). In the 12 months ended December 31, total noncurrent loans at insured institutions increased by $118.8 billion (107.2 percent). At the end of the year, the percentage of loans and leases that were noncurrent stood at 2.93 percent, the highest level since the end of 1992. Real estate construction loans had the highest noncurrent rate of any major loan category at year-end, at 8.51 percent, up from 7.30 percent at the end of the third quarter.



⇩ **Trust Activities** - In a difficult year for financial markets, it was not surprising that trust activities at insured institutions diminished. Total managed fiduciary assets declined in 2008 by $1.1 trillion (25.1 percent), while non-managed assets fell by $3.5 trillion (20.1 percent), and assets in custodial and safekeeping accounts fell by $12.1 trillion (20.8 percent). Net fiduciary income was $1.1 billion (8.2 percent) less in 2008 than in 2007.

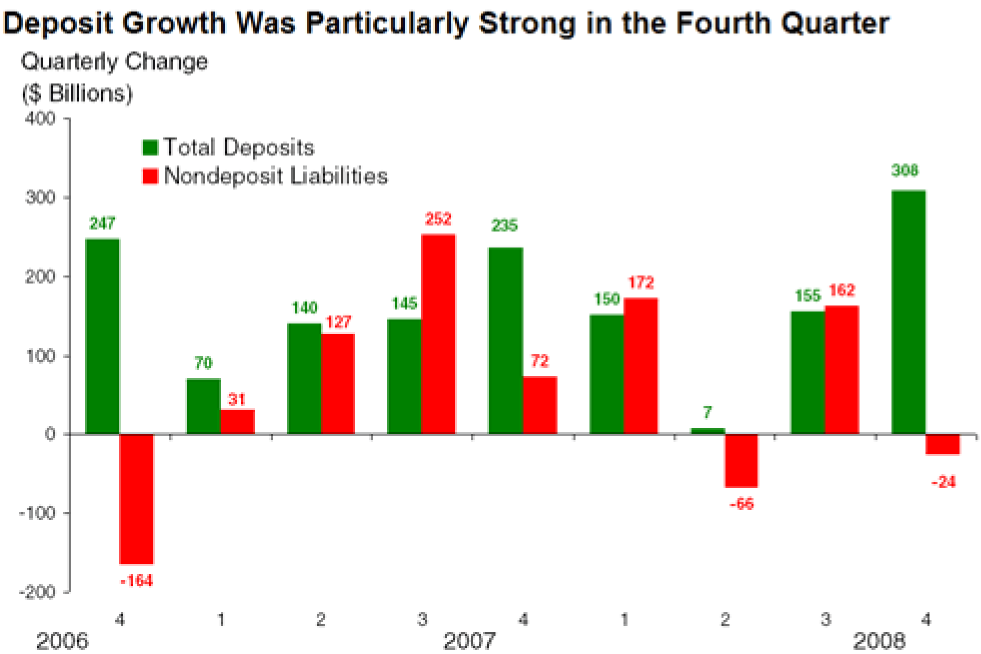
⇩ **Reserve Coverage Ratio** - Total reserves increased by $16.5 billion (10.5 percent) in the fourth quarter. Insured institutions added $31.5 billion more in loss provisions to reserves than they took out in charge-offs, but the impact of purchase accounting from a few large mergers in the quarter limited the overall growth in industry reserves. The growth in reserves, coupled with a decline in industry loan balances, caused the industry's ratio of reserves to total loans to increase during the quarter from 1.96 percent to 2.20 percent, a 14-year high. However, the increase in reserves did not keep pace with the sharp rise in noncurrent loans, and the industry's ratio of reserves to noncurrent loans fell from 83.9 percent to 75.0 percent. This is the lowest level for the "coverage ratio" since the third quarter of 1992.



⇩ **Equity Capital** - Total equity capital declined for a third consecutive quarter, falling by $3.7 billion (0.3 percent) in the fourth quarter. A $39.4 billion (11.0-percent) decline in goodwill and a $16.1 billion reduction in other comprehensive income were the main reasons for the decline. In contrast, regulatory capital, which does not include goodwill and is not affected by unrealized losses on securities (which are included in other comprehensive income), increased during the quarter. Tier 1 leverage capital increased by $22.2 billion (2.3 percent), to $1 trillion at year-end. Total regulatory capital increased by $27.8 billion (2.2 percent) during the quarter, to $1.28 trillion. For the full year, equity capital fell by $44.8 billion. Other comprehensive income, which includes unrealized gains and losses on securities held for sale, declined by $60.6 billion, and goodwill fell by $35 billion. Even though the industry's dividends fell by more than half in 2008 compared to 2007, the $50.9 billion paid out in 2008 exceeded the year's net income by almost $35 billion. Of the 5,621 insured institutions that paid dividends in 2007, more than half (54 percent) reduced their dividends in 2008, including 505 institutions (9 percent) that eliminated their dividends. At the end of 2008, 97.6 percent of all insured institutions, representing 98.7 percent of industry assets, met or exceeded the highest regulatory capital standards.

⇧ **Balances at Federal Reserve Banks** - Total assets of insured institutions increased by $250.7 billion (1.8 percent) in the fourth quarter. The growth was driven by a $341.7 billion (194.3-percent) increase in balances with Federal Reserve banks. While 1,069 banks reported increases in reserve balances during the quarter, five banks accounted for more than half of the entire industry increase. Net loans and leases fell by $130.6 billion (1.7 percent), as several large institutions restructured their loan portfolios. Three large banks accounted for all of the decline in the industry's loans during the fourth quarter; most institutions grew their loan balances in the quarter. Almost two-thirds of all institutions (64.2 percent) reported increases in their loans and leases, while only about half as many institutions (2,894 institutions, or 34.8 percent of all reporters) had declines in their loan portfolios.

⇧ **Deposit Share** - Total deposits increased by $307.9 billion (3.5 percent) in the fourth quarter, the largest percentage increase in a quarter in ten years. Deposits in domestic offices grew by $274.1 billion (3.8 percent), with interest-bearing domestic deposits rising by $242.9 billion (4.2 percent). Brokered deposits increased by $101.4 billion (15.3 percent). Deposits in foreign offices increased by $33.8 billion (2.2 percent) during the quarter. Deposit growth outpaced growth in total assets, and at the end of 2008, deposits funded 65.2 percent of industry assets, the highest proportion since mid-year 2007. Nondeposit liabilities fell by $24.0 billion (0.7 percent), as Federal Home Loan Bank (FHLB) advances declined by $124.0 billion 13.6 percent), and Federal funds purchased declined by $54.6 billion (5.8 percent).



⇩ **Failures and Assistance Transactions** - The number of FDIC-insured commercial banks and savings institutions reporting financial results fell to 8,305 at the end of 2008, down from 8,384 at the end of the third quarter. The net decline of 79 institutions was the largest since the first quarter of 2002. Fifteen new institutions were chartered in the fourth quarter, the smallest number in any quarter since the third quarter of 1994. Seventy-eight insured institutions were absorbed into other institutions through mergers, and 12 institutions failed during the quarter (five other institutions received FDIC assistance in the quarter). For all of 2008, there were 98 new charters, 292 mergers, 25 failures and 5 assistance transactions. This is the largest number of failed and assisted institutions in a year since 1993, when there were 50. At year-end, 252 insured institutions with combined assets of $159 billion were on the FDIC's "Problem List." These totals are up from 171 institutions with $116 billion in assets at the end of the third quarter, and 76 institutions with $22 billion in assets at the end of 2007.

Bank and Thrift Closures Nationwide
Federal Deposit Insurance Corporation

Failures since the last report to March 31, 2009	Charter	Date Closed	Total Assets
Omni National Bank, Atlanta, GA	National	03-27-09	$979.6 Million
TeamBank, National Association, Paola, KS	National	03-20-09	$669.8 Million
Colorado National Bank, Colorado Springs, CO	National	03-20-09	$123.5 Million
FirstCity Bank, Stockbridge, GA	State	03-20-09	$297.0 Million
Freedom Bank of Georgia, Commerce, GA	State	03-06-09	$173.0 Million
Security Savings Bank, Henderson, NV	State	02-27-09	$238.3 Million
Heritage Community Bank, Glenwood, IL	State	02-27-09	$232.9 Million
Silver Falls Bank, Silverton, OR	State	02-20-09	$131.4 Million
Pinnacle Bank of Oregon, Beaverton, OR	State	02-13-09	$73.0 Million
Corn Belt Bank and Trust Company, Pittsfield, IL	State	02-13-09	$271.8 Million
Riverside Bank of the Gulf Coast, Cape Coral, FL	State	02-13-09	$539.0 Million
Sherman County Bank, Loup City, NE	State	02-13-09	$129.8 Million
County Bank, Merced, CA	State	02-06-09	$1.7 Billion
Alliance Bank, Culver City, CA	State	02-06-09	$1.1 Billion
FirstBank Financial Services, McDonough, GA	State	02-06-09	$337.0 Million
Ocala National Bank, Ocala, FL	National	01-30-09	$223.5 Million
Suburban Federal Savings Bank, Crofton, MD	National	01-30-09	$360.0 Million
MagnetBank, Salt Lake City, UT	State	01-30-09	$282.8 Million
1st Centennial Bank, Redlands, CA	State	01-23-09	$803.3 Million
Bank of Clark County, Vancouver, WA	State	01-16-09	$446.5 Million
National Bank of Commerce, Berkeley, IL	National	01-16-09	$430.9 Million
Sanderson State Bank, Sanderson, TX	State	12-12-08	$38.2 Million
Haven Trust Bank, Duluth, GA	State	12-12-08	$572.0 Million
First Georgia Community Bank, Jackson, GA	State	12-05-08	$237.5 Million
PFF Bank and Trust, Pomona, CA	National	11-21-08	$3.7 Billion
Downey Savings and Loan, Newport Beach, CA	National	11-21-08	$12.8 Billion
The Community Bank, Loganville, GA	State	11-21-08	$611.4 Million
Security Pacific Bank, Los Angeles, CA	State	11-07-08	$561.1 Million
Franklin Bank, SSB, Houston, TX	State	11-07-08	$5.1 Billion
Freedom Bank, Bradenton, FL	State	10-31-08	$287.0 Million
Alpha Bank & Trust, Alpharetta, GA	State	10-24-08	$354.1 Million
Meridian Bank, Eldred, IL	State	10-10-08	$39.2 Million
Main Street Bank, Northville, MI	State	10-10-08	$98.0 Million
Washington Mutual Bank, Henderson, NV	National	09-25-08	$307.0 Billion
Washington Mutual Bank FSB, Park City, UT	National	09-25-08	$46.0 Million
Ameribank, Northfork, WV	State	09-19-08	$115.0 Million
Silver State Bank, Henderson, NV	State	09-05-08	$2.0 Billion

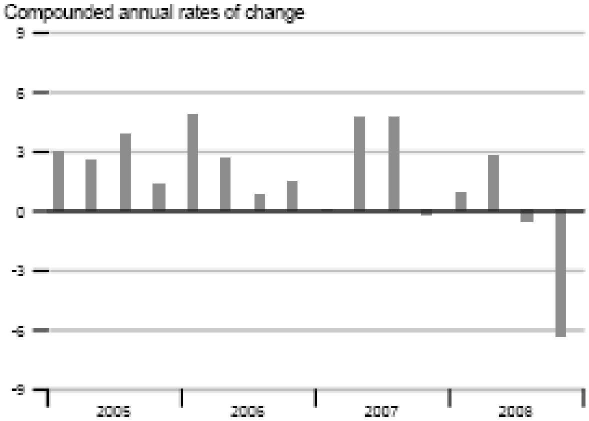
Stock Performance
Southwest Regional Banks

Name	Last Trade		52 Wk Range		PE	EPS	Mkt Cap	Div/Shr	Div Yld
Bancfirst Corporation	03/05	**23.24**	17.11	26.00	N/A	N/A	N/A	N/A	N/A
Banco Bilbao Vizcaya Argentaria	03/05	**5.98**	6.32	23.95	N/A	N/A	22.33B	0.93	13.00%
Bok Financial Corporation	03/05	**23.98**	25.32	61.41	10.57	2.27	1.62B	0.90	3.00%
Cass Information Sys Inc	03/05	**25.50**	23.20	39.15	12.56	2.03	233.78M	0.52	2.00%
Cobiz Incorporated	03/05	**4.20**	4.14	15.20	80.77	0.05	98.17M	0.28	5.90%
Comerica Inc.	03/05	**12.36**	11.83	42.00	9.52	1.30	1.87B	0.20	1.30%
Community Shores Bank Corp	03/02	**1.60**	1.45	7.04	N/A	-0.70	2.35M	N/A	N/A
Cullen Frost Bkrs Incorporated	11/07	**42.10**	28.50	45.34	N/A	N/A	N/A	N/A	N/A
Enterprise Fin Serv Corp	03/05	**8.44**	8.61	25.50	24.11	0.35	108.03M	0.21	2.30%
First Comnty Corp S C	03/05	**5.55**	5.05	15.48	N/A	-2.14	17.89M	0.32	5.40%
First Federal Bankshares Inc	03/05	**1.20**	1.00	15.35	N/A	-6.71	3.96M	N/A	N/A
First Financial Bankshares	03/05	**37.78**	37.06	67.00	14.81	2.55	785.86M	1.36	3.20%
First ST Bancorporation	03/05	**0.90**	0.81	14.93	N/A	-6.17	18.27M	0.36	36.00%
Firstcity Finl Corp	03/05	**1.15**	1.00	8.33	N/A	-1.26	11.31M	N/A	N/A
Franklin Bank Corporation	03/05	**0.01**	N/A	N/A	N/A	-1.86	0.00	N/A	N/A
Great Southn Bancorp Inc	03/05	**10.44**	7.03	18.48	N/A	-0.35	139.69M	0.72	6.20%
Guaranty Fed Bancshares Inc	03/05	**3.85**	3.29	26.64	N/A	-1.33	10.11M	0.72	15.20%
Heartland Financial USA Inc	03/05	**8.87**	9.85	27.14	13.06	0.68	144.35M	0.40	3.50%
International Bancs Cor	03/05	**8.43**	9.26	35.80	4.39	1.92	578.12M	0.66	6.60%
Landmark Bancorp Inc	03/04	**14.51**	12.80	24.75	7.68	1.89	34.42M	0.76	5.20%
Liberty Bancorp Inc	03/05	**6.70**	4.50	10.64	12.96	0.52	25.12M	0.10	1.40%
Mackinac Finl Corp	03/05	**3.24**	2.45	9.24	5.92	0.55	11.08M	N/A	N/A
Metrocorp Bancshares Inc	03/05	**2.92**	2.29	13.49	7.39	0.40	31.78M	0.16	5.50%
Midwestone Finl Group Inc	03/08	**10.55**	10.21	14.31	N/A	N/A	N/A	N/A	N/A
Osage Bancshares Inc	03/05	**7.25**	6.80	10.38	N/A	-0.73	20.51M	0.34	4.50%
Prosperity Bancs Inc	03/05	**21.49**	22.88	46.48	11.57	1.86	990.26M	0.55	2.20%
QCR Holdings Inc	03/05	**7.75**	7.60	16.20	7.30	1.06	34.94M	0.08	0.90%
Sterling Bancshares Inc	03/05	**4.73**	4.30	14.01	9.10	0.52	346.52M	0.22	4.00%
Team Financial Inc	03/04	**0.15**	0.10	13.49	N/A	-6.35	0.00	N/A	N/A
Tex Capital Bancs Inc	03/05	**7.20**	7.20	22.00	8.32	0.87	223.06M	N/A	N/A
Tierone Corporation	03/05	**1.54**	1.13	13.96	N/A	-5.33	27.77M	0.16	8.50%
UMB Financial Corporation	03/05	**34.33**	35.21	69.60	14.42	2.38	1.41B	0.70	1.80%
West Bancorp Incorporated	03/05	**4.50**	4.70	16.21	10.23	0.44	78.31M	0.32	5.20%
Zions Bancorp	03/05	**6.77**	7.49	54.90	N/A	-2.67	780.88M	0.16	1.70%

Source: Yahoo Finance (March 2009)
NA – Indicates information was not available.

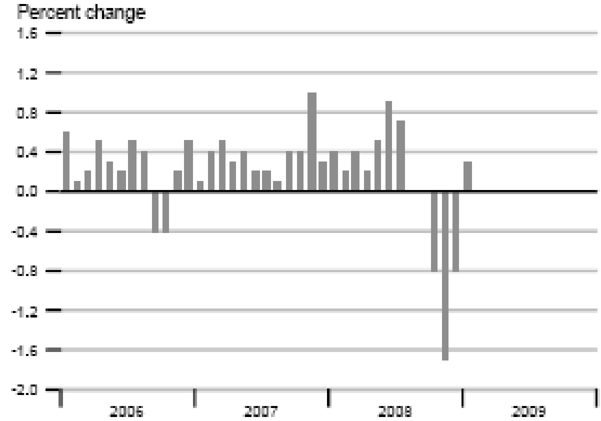
Real GDP Growth

Compounded annual rates of change



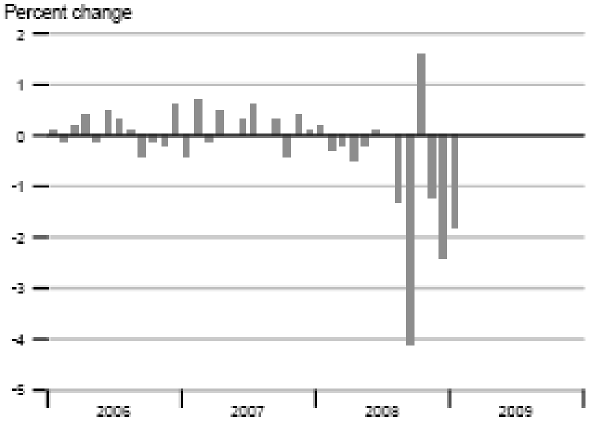
Consumer Price Index

Percent change



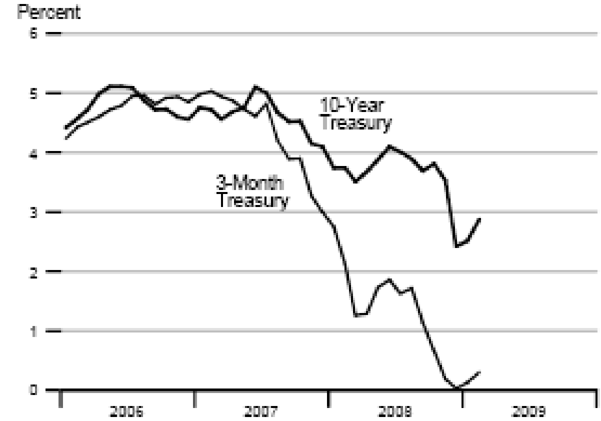
Industrial Production

Percent change



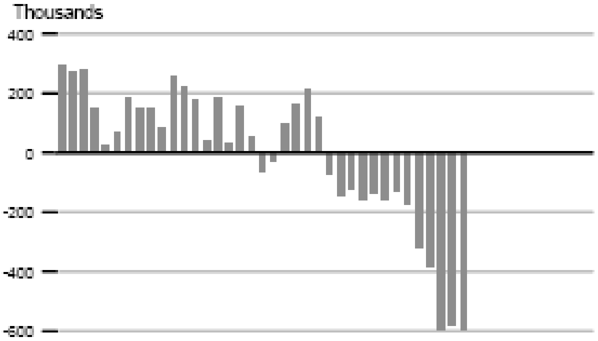
Interest Rates

Percent



Change in Nonfarm Payrolls

Thousands

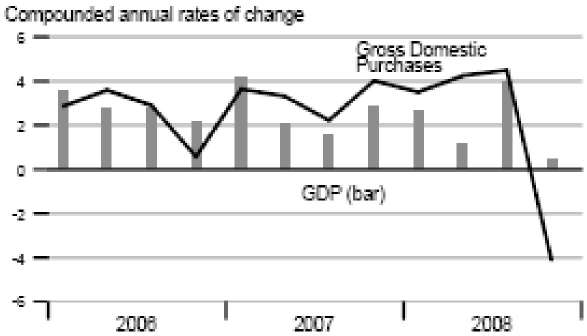


Unemployment Rate

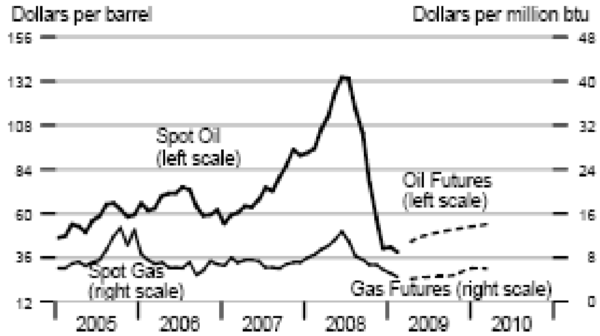
Percent of labor force

Provided by the Federal Reserve Bank of St. Louis, National Economic Trends. Updated March 2, 2009.

NIPA Chain Price Indexes

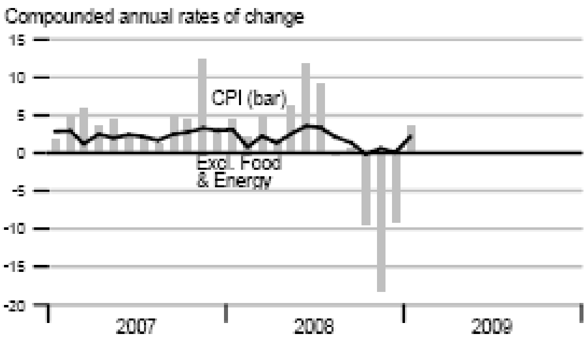


Oil & Natural Gas Prices: Spot & Futures

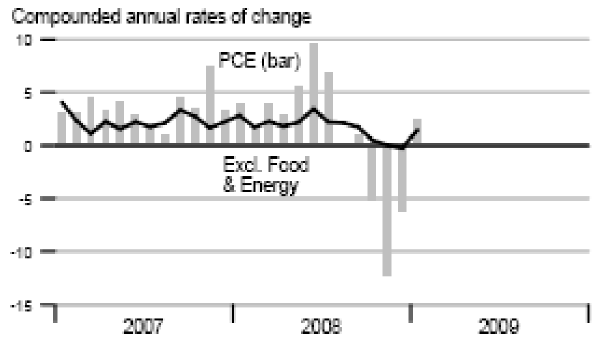


Note: Futures prices as of 2/27/2009.

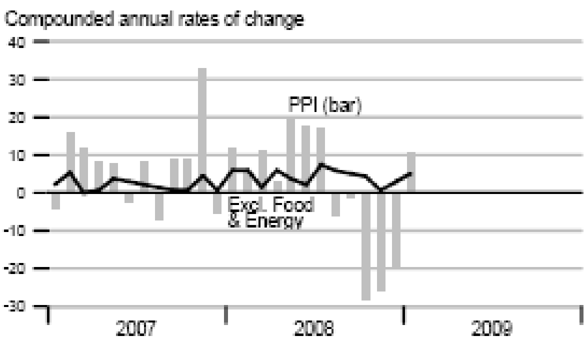
Consumer Price Index



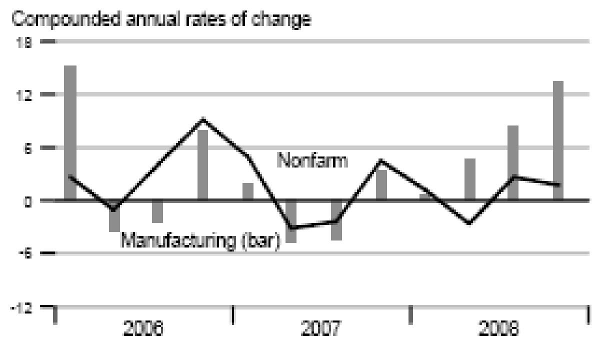
Consumption Chain Price Index



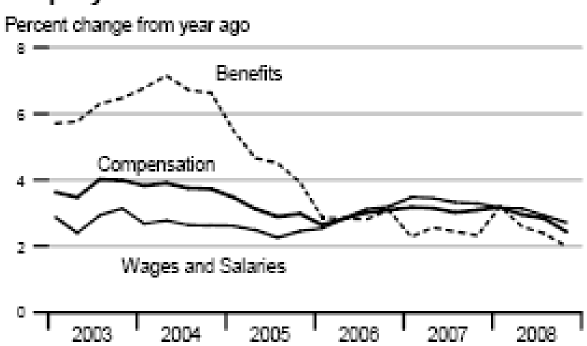
Producer Price Index, Finished Goods



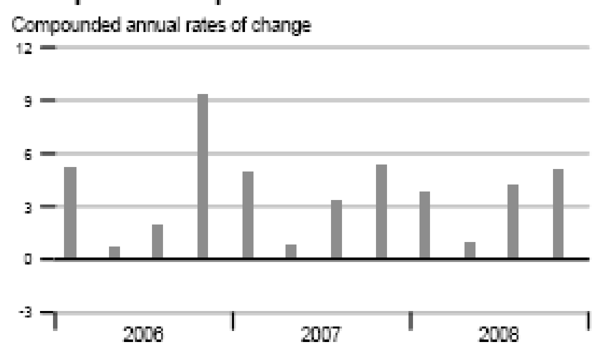
Unit Labor Cost



Employment Cost Index



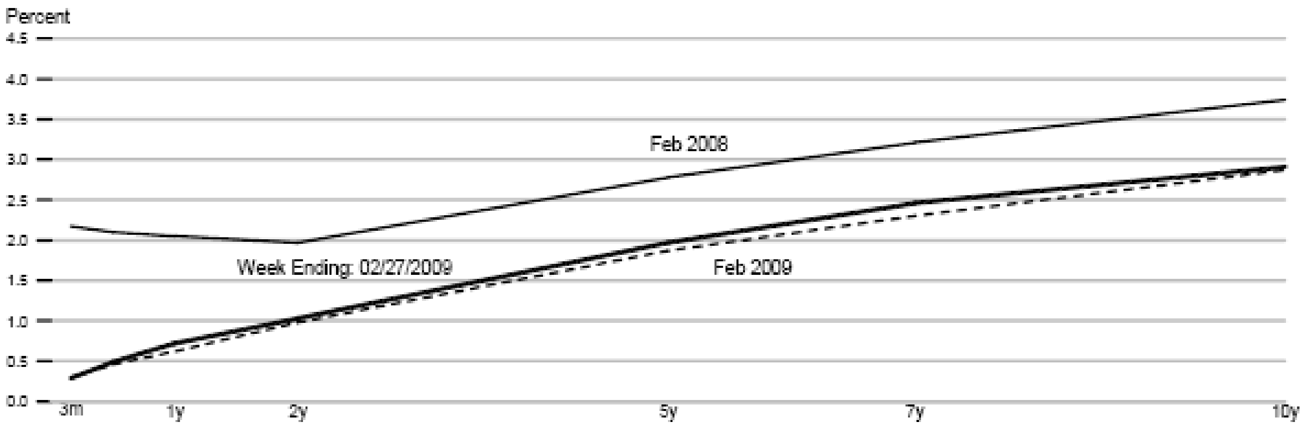
Compensation per Hour



Provided by the Federal Reserve Bank of St. Louis, National Economic Trends. Updated March 2, 2009.

Interest Rates

Treasury Yield Curve



Standard and Poor's 500 Index with Reinvested Dividends

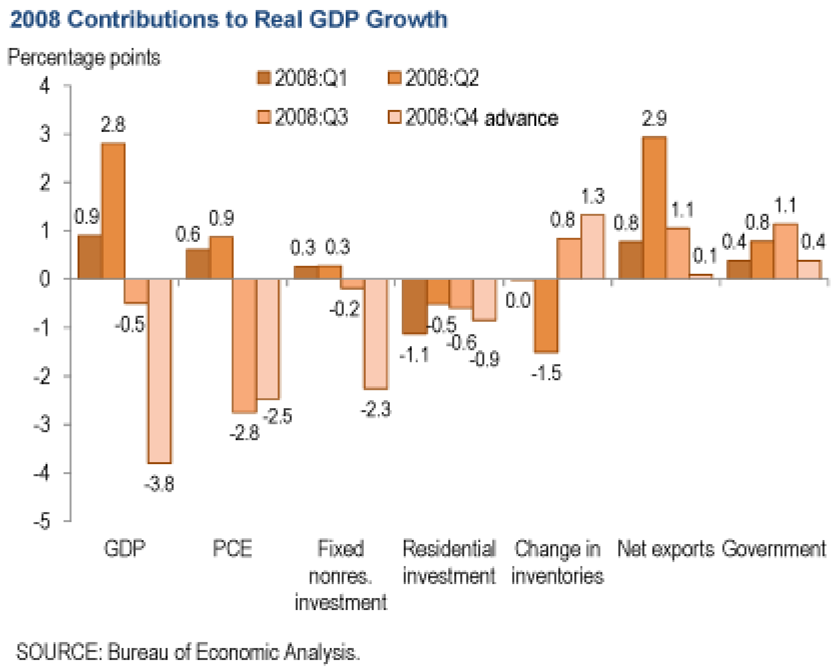
Provided by the Federal Reserve Bank of St. Louis, National Economic Trends. Updated March 2, 2009.

ECONOMIC REPORTS AND FORECASTS
UNITED STATES

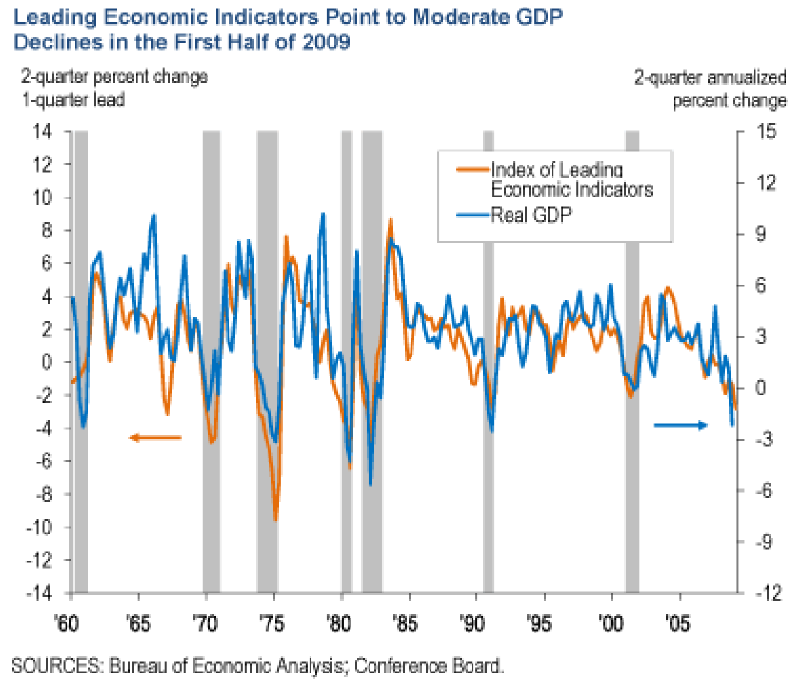
National Update – February 2009
Federal Reserve Bank of Dallas

⇩ **Overall Economy** - Recently released data indicates that economic contraction has intensified at a pace associated with severe recessions. Two consecutive quarters of negative real growth, striking job losses and deep declines in both manufacturing and services output defined year-end 2008. While the economic outlook remains bleak for the first half of 2009, a few indicators suggest that the pace of contraction may slow in coming months.

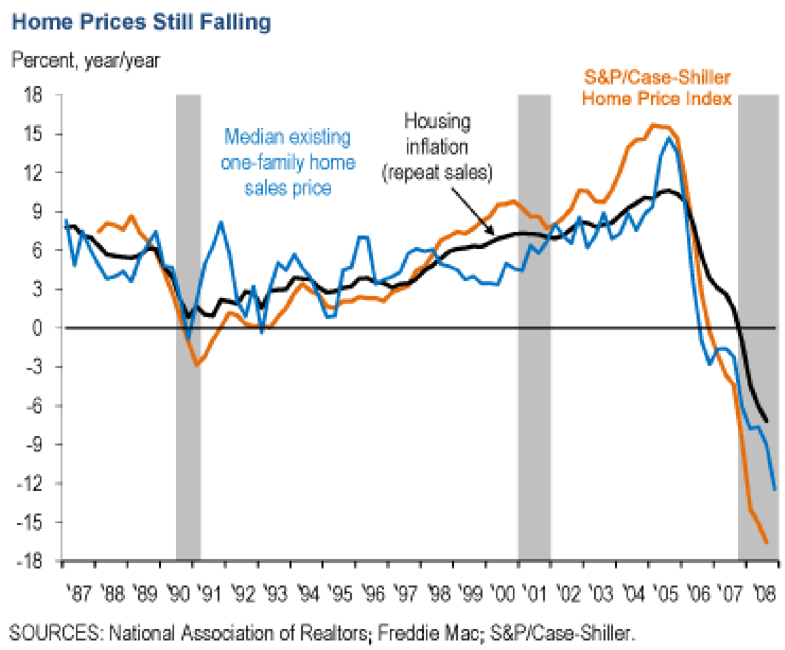
⇩ **Gross Domestic Product** - Real gross domestic product (GDP) fell at a 3.8 percent annualized rate in fourth quarter 2008, less steep than market expectations. Accounting for the notable drop in GDP, consumer spending, business investment and residential investment all declined substantially in the fourth quarter. In particular, spending on durable consumer goods plunged 22 percent at an annualized rate, the sharpest decline since 1987. Spending on nondurable goods fell an annualized 7 percent for the second straight quarter, its worst performance since 1967. Real personal consumption expenditures dropped 0.5 percent in December as low consumer confidence spurred consumers to increase the savings rate by 0.8 percentage point to 3.6 percent.



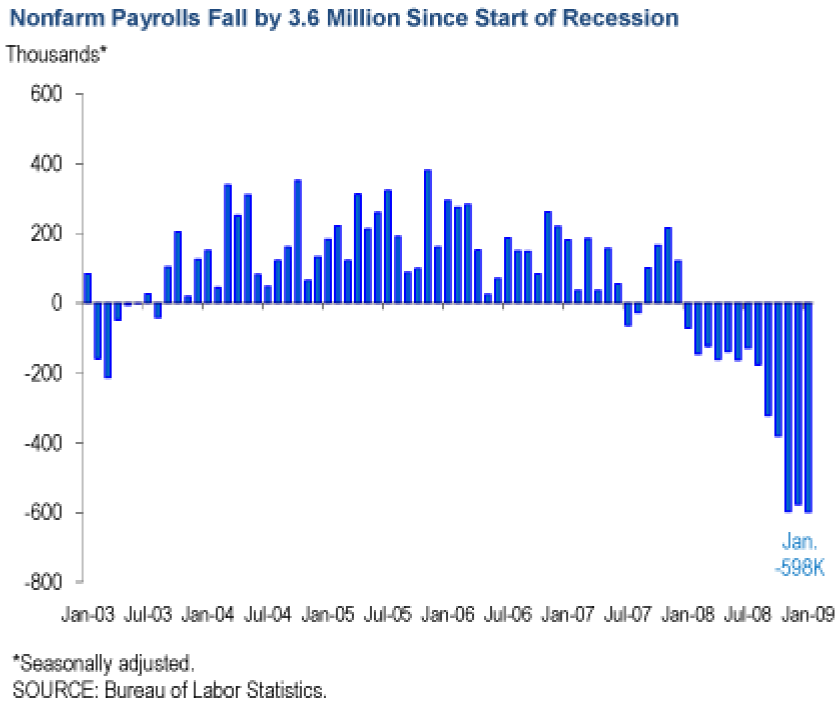
New orders for manufactured durable goods fell 3 percent in December, the fifth consecutive month of decline. Notable drops in core capital goods orders suggest substantial weakening in equipment and software investment in the coming months. Industrial production continued its downward trend in January, falling 1.8 percent following December's 2.4 percent retreat. On a positive note, retail sales increased 1.1 percent in January following six straight months of declines. The small uptick in the Institute for Supply Management's indexes of manufacturing and service-sector growth, which hit historic lows in December, ended a streak of steep declines that began in August 2008. While both indexes reflect significant pullbacks in output, January's uptick may signal a possible stabilization in the rate of economic contraction. The Index of Leading Economic Indicators, which tracks more normal cyclical movements, points to a moderate decline in overall GDP growth in the first half of 2009. (Chart on next page.)



⇩ **Housing** – Construction indicators declined further in December, with overall construction spending falling 1.4 percent. Housing permits and starts plummeted 11.1 percent and 14.5 percent in December, respectively, having dropped 50.8 percent and 44 percent over 2008. In January, permits fell another 4.8 percent and starts plunged 16.8 percent to only 466,000 units, a new post–World War II low. Both permits and starts are now nearing 80 percent declines from their peaks of three years ago. New-home sales slid another 14.7 percent in December, far worse than expected. However, December existing-home sales surprised the market with a 6.5 percent gain, although the median existing-home sales price increase was 9.7 percent lower than a year ago. Falling home prices have yet to show signs of nearing bottom.

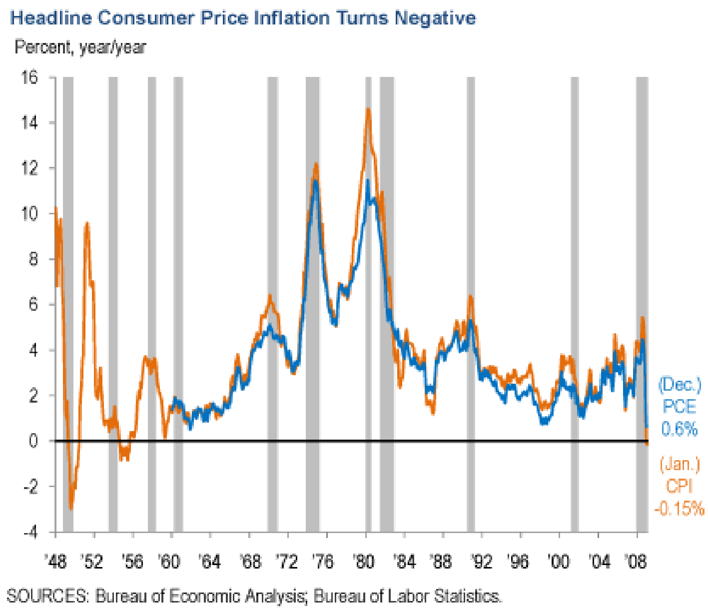


⇩ **Employment** - Labor market conditions worsened significantly in January. Nonfarm payroll employment fell by 598,000—more than 19,000 jobs per day and the largest one-month drop since 1974. Job losses in November and December were also revised upward to 597,000 and 577,000, respectively. These last three employment reports revealed a net loss of nearly 1.8 million jobs, the largest three-month loss in the post–World War II period. With all major sectors posting substantial declines, payroll employment has fallen by nearly 3.6 million since the start of the recession in December 2007.



The unemployment rate in January rose 0.4 percentage point to 7.6 percent. The increase experienced by males ages 25–54 was twice that for females of the same age group, putting prime-age males 1.3 percentage points higher on the unemployment scale than their female counterparts. Given the recent spike in initial claims for unemployment to around 630,000—a level last seen in October 1982—further job losses and increases in unemployment are likely in February. While the employment outlook is rather ominous, average hourly earnings are up 3.9 percent from a year ago, and productivity increased at an annualized rate of 3.2 percent in the fourth quarter, suggesting firms are retaining their most productive workers.

⇩ **Inflation** - Amid growing slack, there has been rapid disinflation in recent months. As of December, prices for nearly half of all goods and services have declined. Consumer prices fell in December and January, largely owing to plunging energy prices. Even less-volatile, year-over-year figures show producer prices falling and consumer price inflation in negative territory—a pattern not seen since August 1955. Headline PCE inflation was up by only 0.6 percent from a year ago. Year-over-year core CPI and PCE inflation rates have also slowed to about a 1.7 percent pace. Although the recession has deepened in recent months, efforts to repair the financial system, coupled with fiscal and monetary stimulus, should spur an eventual economic recovery. (Chart on next page.)



⇳ **Some Financial Market Improvement** - Financial markets have one major signal that firms are facing difficulties in obtaining financing is that the benchmark yield spread between Baa- and Aaa-rated corporate bonds jumped in December to levels not seen since 1933. This spread has only narrowed from 350 at its December peak to around 280 basis points in recent days, a level near the peak during the 1981–82 recession. On a brighter note, investment-grade corporate bond issuance increased notably in January, signaling a reopening of the corporate bond market to highly rated firms.

Interest rate spreads in the interbank and commercial paper markets have edged down further following large improvements in late December and early January. Likewise, mortgage rates have come down from their October highs, though they have crept up some in recent weeks. According to senior loan officers surveyed by the Federal Reserve Board in January, the rate of decline in their willingness to make consumer loans has slowed substantially from three months earlier. Credit standards at banks reportedly also tightened at a slower rate through the fourth quarter.

U.S. Economy at a Glance
U. S. Bureau of Labor Statistics

Data Series	Sept 2008	Oct 2008	Nov 2008	Dec 2008	Jan 2009	Feb 2009
Unemployment Rate (1)	6.2	6.6	6.8	7.2	7.6	8.1
Change in Payroll Employment (2)	-321	-380	-597	-681	-655(P)	-651(P)
Average Hourly Earnings (3)	18.21	18.28	18.34	18.40	18.44(P)	18.47(P)
Consumer Price Index (4)	0.0	-0.8	-1.7	-0.8	0.3	
Producer Price Index (5)	-0.1	-2.7(P)	-2.5(P)	-1.9(P)	0.8(P)	
U.S. Import Price Index (6)	-3.6	-6.0(R)	-7.3(R)	-5.0(R)	-1.1(R)	

Footnotes:

(1) In percent, seasonally adjusted. Annual averages are available for not seasonally adjusted data.
(2) Number of jobs, in thousands, seasonally adjusted.
(3) For production and nonsupervisory workers on private nonfarm payrolls, seasonally adjusted.
(4) All items, U.S. city average, all urban consumers, 1982-84=100, 1-month percent change, seasonally adjusted.
(5) Finished goods, 1982=100, 1-month percent change, seasonally adjusted.
(6) All imports, 1-month percent change, not seasonally adjusted.
(R) Revised
(P) Preliminary

Data Series	4th Qtr 2007	1st Qtr 2008	2nd Qtr 2008	3rd Qtr 2008	4th Qtr 2008
Employment Cost Index (1)	0.8	0.7	0.7	0.7	0.5
Productivity (2)	-0.5	2.6	4.7	2.2	-0.4

Footnotes:

(1) Compensation, all civilian workers, quarterly data, 3-month percent change, seasonally adjusted.
(2) Output per hour, nonfarm business, quarterly data, percent change from previous quarter at annual rate, seasonally adjusted.

Data extracted on: March 11, 2009

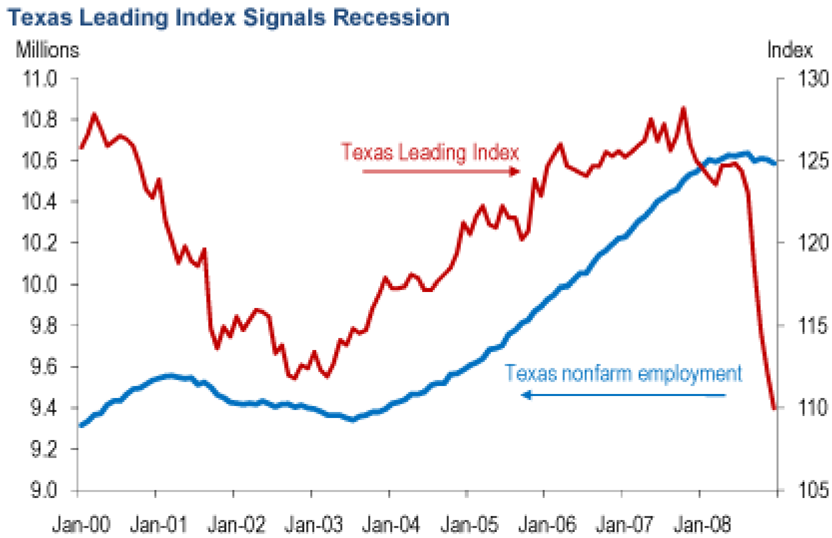
⇩ **Economy** – Reports from the twelve Federal Reserve Districts suggest that national economic conditions deteriorated further during the reporting period of January through late February. Ten of the twelve reports indicated weaker conditions or declines in economic activity; the exceptions were Philadelphia and Chicago, which reported that their regional economies "remained weak." The deterioration was broad based, with only a few sectors such as basic food production and pharmaceuticals appearing to be exceptions. Looking ahead, contacts from various Districts rate the prospects for near-term improvement in economic conditions as poor, with a significant pickup not expected before late 2009 or early 2010.

Consumer spending remained sluggish on net, although many Districts noted some improvement in January and February compared with a dismal holiday spending season. Travel and tourist activity fell noticeably in key destinations, as did activity for a wide range of nonfinancial services, with substantial job cuts noted in many instances. Reports on manufacturing activity suggested steep declines in activity in some sectors and pronounced declines overall. Conditions weakened somewhat for agricultural producers and substantially for extractors of natural resources, with reduced global demand cited as an underlying determinant in both cases. Markets for residential real estate remained largely stagnant, with only minimal and scattered signs of stabilization emerging in some areas, while demand for commercial real estate weakened significantly. Reports from banks and other financial institutions indicated further drops in business loan demand, a slight deterioration in credit quality for businesses and households, and continued tight credit availability.

Upward price pressures continued to ease across a broad spectrum of final goods and services. This was largely associated with lower prices for energy and assorted raw materials compared with earlier periods, but also with weak final demand more generally, which spurred price discounting for items other than energy and food. With rising layoffs and hiring freezes, unemployment has risen in all areas, reducing or eliminating upward wage pressures. A number of reports pointed to outright reductions in hourly compensation costs, through wage reductions and reduction or elimination of some employment benefits.

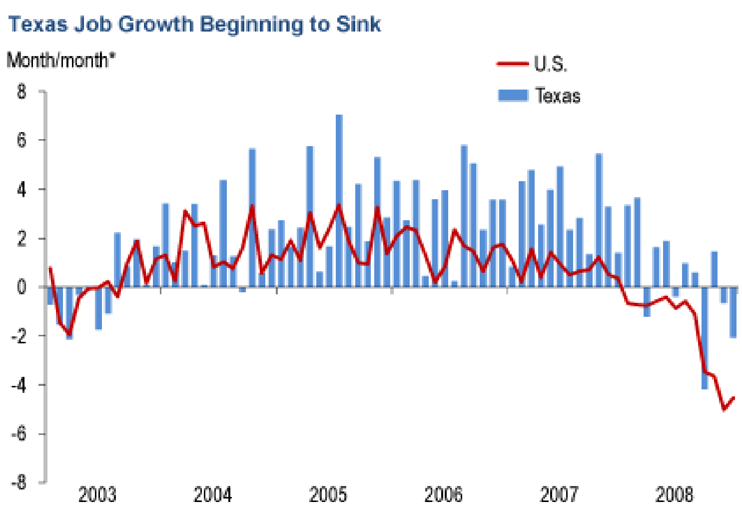
Regional Economic Update – February 2009
Federal Reserve Bank, Dallas

⇩ **Overall Economy** - Over the three months ending in December, the Texas Leading Index experienced its sharpest decline since its inception in January 1981. All eight of the indicators gave negative signals, with the steepest drops coming from the increase in the Texas export-weighted value of the dollar and declines in the stock index of Texas-based companies. In addition, the Texas Business-Cycle Index was revised downward, indicating Texas likely entered a recession sometime in the second half of 2008.



SOURCES: Bureau of Labor Statistics, Texas Workforce Commission, Dallas Fed.

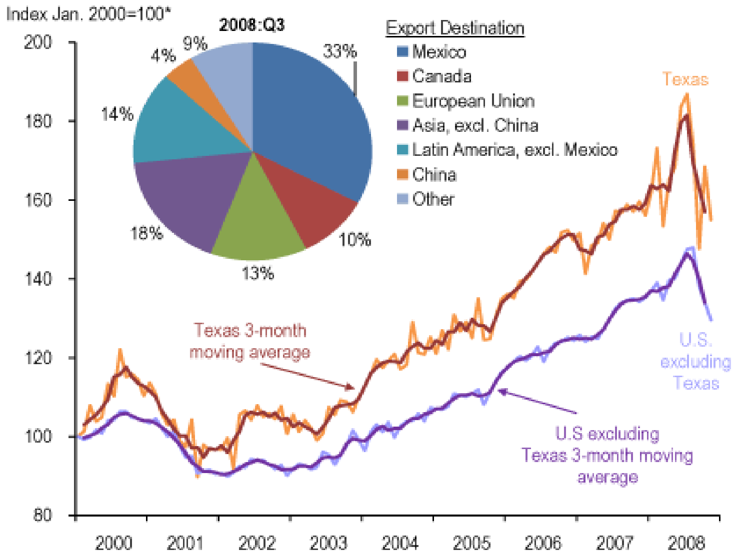
⇩ **Employment –** Texas employment growth was revised downward, showing a sharply negative turn in September, and then proceeded to fall further in both November and December. In December the unemployment rate reached 6 percent, up 1.9 percentage points from its bottom in April 2008. Given the sharp fall in the Texas Leading Index and the negative outlook of Beige Book respondents, further increases in the unemployment rate are expected.



*Seasonally adjusted, annualized rate.
SOURCES: Bureau of Labor Statistics, Texas Workforce Commission.

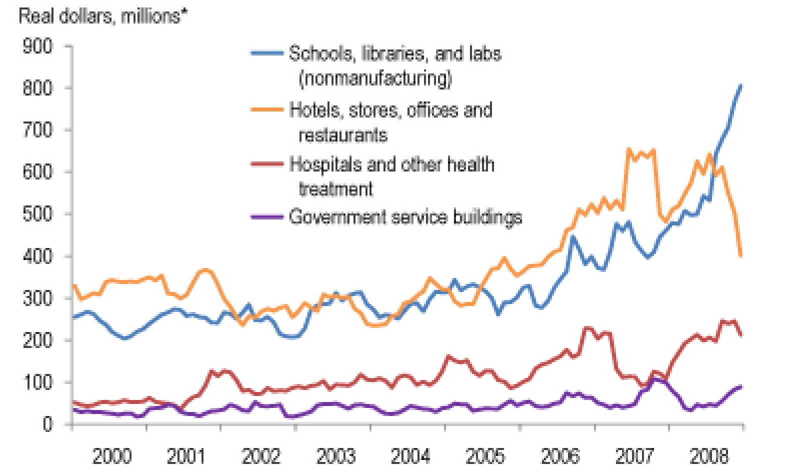
⇩ **Texas Exports** - In December, Beige Book contacts across a wide range of industries reported further weakening in economic activity. The majority of respondents now expect a recession through midyear, with some contacts not expecting a recovery until early 2010. Texas exports have dropped over 17 percent from the high reached in July 2008. Contributing to the decline was a sharp slowing of the world economy and an appreciation of the dollar against the currencies of primary trade partners. For example, the dollar appreciated significantly against the Mexican peso, which has a powerful impact on Texas exports, as Mexico is Texas' largest export destination.

Texas Exports Drop Sharply



*Seasonally adjusted.
SOURCES: Bureau of Labor Statistics, Census Bureau.

⇩ **Real Estate Activity** –The Texas housing market continues to weaken, although home inventories and rates of mortgage delinquencies and foreclosures suggest that markets are in better shape than the national average. According to industry contacts, a growing concern in Texas is that commercial construction will drop sharply due to restrictive financing for the industry. While residential construction values have been in decline for some time now, nonresidential construction values are yet to show a significant drop off. This is due in part to the expansion of the Port Arthur refinery, which began in 2008. The public sector continued to add space, while private construction of hotels, stores, offices and restaurants began to decline in the closing months of 2008. (Chart on next page.)



*Five-month moving average, seasonally adjusted.
SOURCES: F.W. Dodge, calculations by the Dallas Fed.

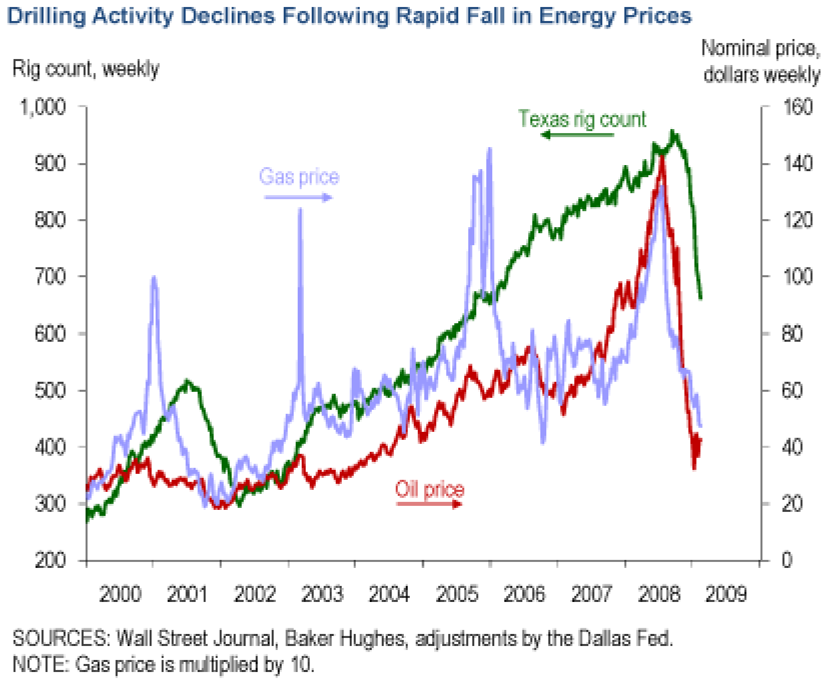
⇳ **Texas Major MSA Exposure to Current Recession** – One way to analyze the different metros' exposure to the national downturn is by computing their job-share location quotients. The location quotient quantifies the relative concentration of a specific industry as compared with the concentration of that industry nationwide. A location quotient value greater than one represents a higher concentration in that industry than the nation as a whole, and values less than one imply a lower concentration. As shown, Dallas and Austin are more heavily concentrated in cyclically sensitive industries like information services and simultaneously less represented in the more cyclically stable industries like education and health services. Houston is heavily weighted in the energy sector, and much of its fate this year likely rests with energy prices.

Texas Major MSA Exposure to Current Recession

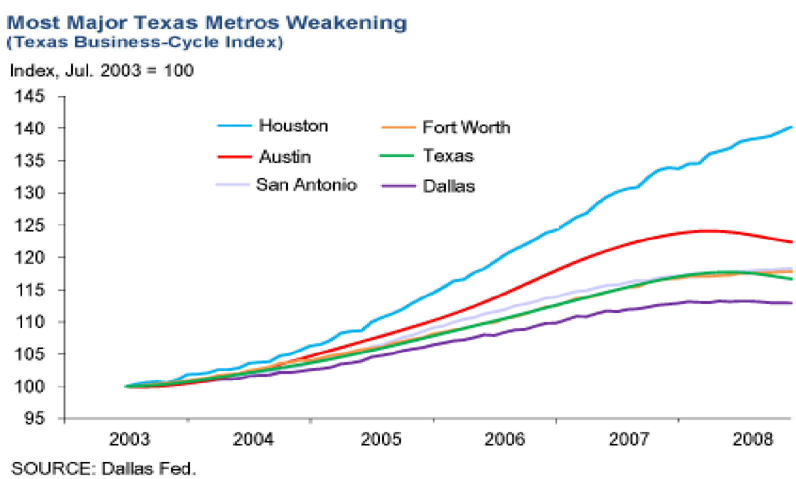
	Austin	Dallas	Fort Worth	Houston	San Antonio	El Paso	Texas
Natural Resources and Mining	0.4	0.4	1.1	2.6	0.5	0.3	1.9
Construction	1.2	1.0	1.1	1.4	1.1	1.0	1.2
Manufacturing	0.8	1.0	1.1	0.9	0.6	0.8	0.9
Trade, Transportation and Utilities	0.9	1.0	1.2	1.0	0.9	1.1	1.0
Wholesale Trade	1.2	1.4	1.1	1.2	0.8	0.9	1.1
Retail Trade	0.9	0.9	1.1	0.9	1.0	1.2	1.0
Information	1.3	1.6	0.8	0.7	1.2	0.9	0.9
Financial Activities	1.0	1.5	0.9	0.9	1.3	0.7	1.0
Finance and Insurance	0.9	1.6	0.9	0.8	1.3	0.6	1.0
Real Estate and Rental and Leasing	1.1	1.4	1.0	1.3	1.2	1.0	1.1
Professional and Business Services	1.1	1.3	0.9	1.1	1.0	0.9	1.0
Non-Cyclical Industries							
Education and Health Services	1.0	0.8	0.9	0.9	1.1	1.2	1.0
Leisure and Hospitality	1.0	0.9	1.0	0.9	1.2	1.0	1.0
Public Administration	1.3	0.5	0.6	0.5	0.8	1.1	0.7

SOURCE: TWC 2007 ES202 employment

⇳ **Energy and Business Services** - Energy prices have stabilized at levels far below those seen in 2008, with oil prices fluctuating around $40 for the past month. The rig count has responded sharply—228 rigs have been removed from service since the end of November. Most of the decline has come from land-based natural gas rigs. Employment cutbacks are expected to hit the industry in 2009 as energy prices languish.



Of Texas' major metros, Austin and Dallas have been hit the hardest in recent months, while Houston has fared the best. However, the decline in energy prices makes it likely that all major Texas metros will experience a recession in 2009. (Chart on next page.)

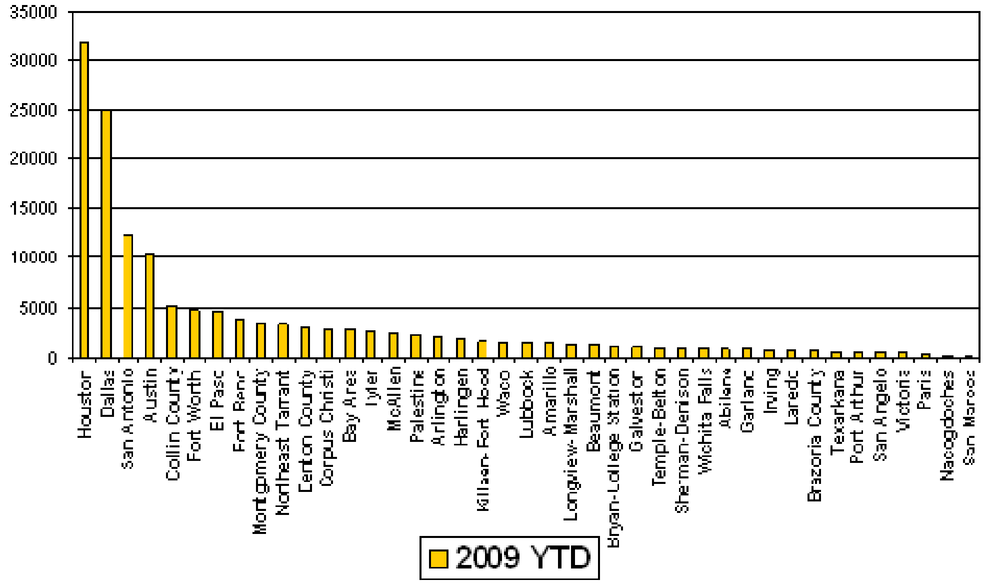


Data Series	Aug 2008	Sept 2008	Oct 2008	Nov 2008	Dec 2008	Jan 2009
Civilian Labor Force [1]	[5] **11,734.7**	[5] **11,761.9**	[5] **11,791.8**	[5] **11,823.4**	[5] **11,856.7**	[P] **11,816.9**
Unemployment Rate [2]	[5] **5.0**	[5] **5.1**	[5] **5.3**	[5] **5.4**	[5] **5.6**	[P] **6.4**
Total Nonfarm [3]	**10,640.4**	**10,601.1**	**10,655.1**	**10,647.5**	**10,631.3**	[P] **10,580.7**
Mining and Logging [3]	**234.1**	**235.4**	**238.4**	**239.6**	**240.2**	[P] **235.5**
Construction [3]	**674.0**	**670.3**	**675.6**	**664.6**	**655.8**	[P] **650.6**
Manufacturing [3]	**922.7**	**919.1**	**913.3**	**913.0**	**909.6**	[P] **896.6**
Trade, Transportation, and Utilities [3]	**2,152.1**	**2,144.6**	**2,155.4**	**2,152.5**	**2,143.5**	[P] **2,116.9**
Information [3]	**216.1**	**214.6**	**212.8**	**213.8**	**214.6**	[P] **209.6**
Financial Activities [3]	**647.7**	**646.5**	**648.6**	**651.3**	**651.6**	[P] **650.3**
Professional & Business Services [3]	**1,341.8**	**1,333.1**	**1,350.7**	**1,343.2**	**1,339.2**	[P] **1,337.0**
Educational & Health Services [3]	**1,300.2**	**1,229.1**	**1,314.0**	**1,316.5**	**1,317.4**	[P] **1,320.6**
Leisure & Hospitality [3]	**1,006.3**	**1,000.5**	**1,006.8**	**1,009.8**	**1,014.1**	[P] **1,015.8**
Other Services [3]	**363.3**	**360.1**	**359.4**	**359.0**	**359.4**	[P] **358.3**
Government [3]	**1,782.1**	**1,777.8**	**1,780.1**	**1,784.2**	**1,785.9**	[P] **1,789.5**
Layoff events, all industries [4]	**40**	**97**	**86**	**64**	**95**	**136**

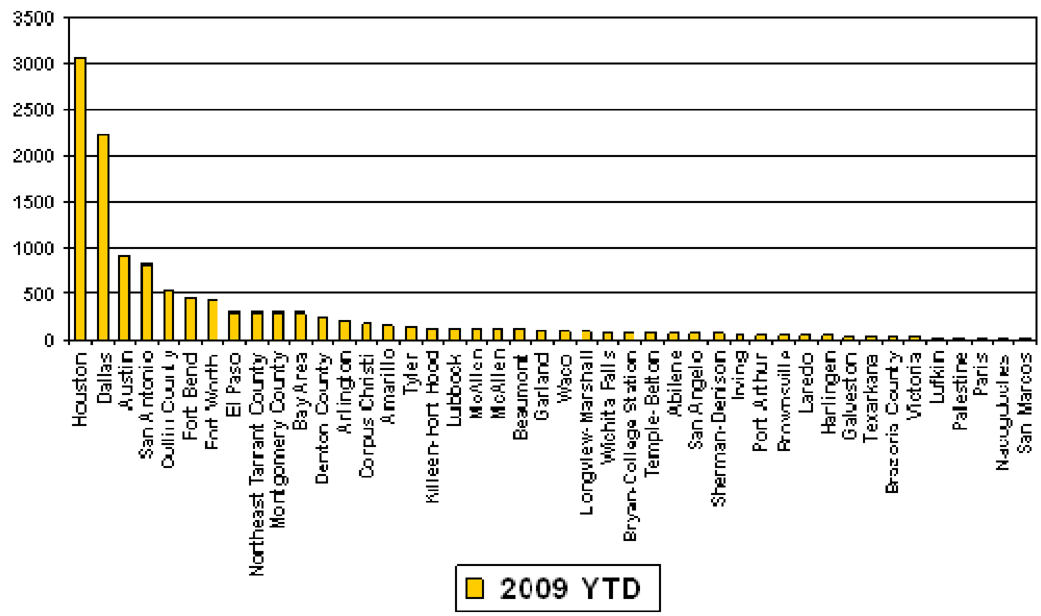
Footnotes:
[1] Number of persons, in thousands, seasonally adjusted.
[2] Percent, seasonally adjusted
[3] Number of jobs, in thousands, seasonally adjusted.
[4] See About the data.
[5] Reflects revised population controls, model reestimation, and new seasonal factors
[P] Preliminary

Data extracted on: March 13, 2009
Source: U. S. Bureau of Labor Statistics

Texas Residential MLS Activity
Number of Houses for Sale



Texas Residential MLS Activity
Number of Homes Sold



- **Survey of Banking and the Economy** – The Banker and Business Economic Survey is conducted monthly by the Texas Department of Banking and reflects the opinions of executives of state-chartered banks throughout Texas. The banker selection varies but is intended to provide a good cross-section of state-chartered banks in Texas, both in size and location. Bankers who are asked to participate in the survey are selected from rural and metropolitan markets alike, and each state-chartered bank is sent a survey once each year. The fourth quarter 2008 survey includes responses from 65 bankers.

  - **Local Economy** – National economic events that transpired in the fourth quarter were reflected in the most recent banker economic survey: 37% of the bankers reported a decrease in general business activity, compared to only 14% in the third quarter. Bankers reporting that economic activity stayed about the same also slipped to 52% of respondents in the fourth quarter. Comments provided by bankers indicate that many are focused on controlling credit risk and closely monitoring adverse economic trends versus taking advantage of business expansion and growth opportunities. However, some banks pointed out that consolidation in the industry among some of the larger banks and a general movement toward more restrictive lending standards has opened up opportunities on the lending side that did not exist before. Bankers in the High Plains / Coast region expressed the most optimism, while bankers in the Upper East / Southeast, Alamo / Capital / Central, Metro / Gulf Coast, and large banks were the most pessimistic. Survey responses continue to reflect concern for a softening of the residential real estate markets. For the first time since collection began of the banker economic survey information, more than half of the bankers (61%) reported a decrease in residential property sales activity. A reduced 34% reported sales at about the same level, and only 3% reported an increase. Respondents report equally pessimistic commercial real estate sales activity: 56% report decreasing sales activity; 40% report sales activity at about the same level; and only 3% report increasing sales activity. Area wide employment was also downgraded. Though the vast majority (75%) believes that employment stayed relatively constant from the third quarter to the fourth quarter, a greater percentage (17%) believed that employment had decreased.

  - **Economic Indicator Forecasts –** As a reflection of economic circumstances during the period of the survey, 62% of the respondents believed that rates would decrease over the next six months. In addition, 68% of the bankers surveyed thought that the equity markets, as reflected in the Dow Jones Industrial Average, would deteriorate further in the next six months. Unlike previous surveys, more bankers predicted that fuel prices would decrease (45%) over the next six months versus increase (24%). Less concern was indicated in the narrative responses from bankers about net interest margins. Respondents who believed that inflation would decrease (32%) in the next six months slightly outnumbered those that believed that inflation would increase (25%). The largest percentage, however, (40%) believed that inflation would remain relatively constant. Many bankers expressed concern about the national economy, increasing unemployment, and the fall of crude oil prices.

  - **Competition –** Bankers indicate that competition remains strong.

Rated Area	*Significantly Increasing*	*Increasing*	*About the Same or Decreasing*
Consumer Loans	2%	22%	73%
Commercial Loans	2%	23%	75%
Deposits	9%	49%	40%

  - **Bank Growth Characteristics from the 4Q 2008 as compared to 3Q 2008 –** Bankers report very good asset growth trends in the fourth quarter compared to the third: 51% increasing; 37% about the same; and 12% decreasing. Loan growth continues to be healthy with 3% reporting significant increases; 44% reporting increases; and 53% reporting about the same or decreasing.

  - **Earnings –** Over half of the bankers expected to post a return on average assets of greater than 1% for the fourth quarter. However, a larger percent of bankers (36%) expected a reduced ROA than expected an improved ROA (22%), and 40% expected their ROA to be about the same as reported in the third quarter. Fewer bankers, on a percentage basis, reported an increasing margin (17%) versus those reporting a decreasing margin (37%), and 46% reported a stable margin from the previous quarter.

- **Asset Quality Indicators -** Asset quality weaknesses expressed by bankers in the second and third quarters continued into the fourth quarter. Across all categories surveyed, slightly more bankers reported that past dues, nonaccruals, foreclosures, repossessions, and customer bankruptcies had increased than those reporting that they had decreased. One significant trend that we continue to monitor is that 36% of reporting bankers experienced an increase in internal watch list loans in the fourth quarter. Bankers reporting increases in watch list loans in the second and third quarters were 23% and 29%, respectively. Concerns about credit quality continue to affect loan underwriting standards as more than half (57%) of the respondents indicate they are tightening loan underwriting standards, and none reported any loosening of standards.

- **Summary –** Though the majority of the respondents indicated that the general business activity and area wide employment were either stable or improving, concerns about residential and commercial sales activity, as well as deteriorating asset quality influences, were noted from the previous quarter. The Department will be diligent to monitor these factors to determine the effect, if any, on industry performance.

- **<u>Senior Loan Officer Opinion Survey</u>** - The Federal Reserve's January 2009 survey of lending practices addresses changes in the supply of, and demand for, bank loans to businesses and households over the past three months. The survey is based on responses from 53 domestic banks and 23 U.S. branches and agencies of foreign banks

  - **Commercial and Industrial Lending** – About 65 percent of domestic banks reported having tightened lending standards on commercial and industrial (C&I) loans to large and middle-market firms over the past three months. This percentage was down from the reported tightening in the October survey but still above the previous peaks reported in 1990 and 2001. At about 70 percent, the fraction of domestic respondents that tightened standards on C&I loans to small firms was only slightly lower than that found in the October survey. Significant majorities of domestic respondents indicated that they had further tightened price terms on C&I loans to firms of all sizes over the past three months. Around 90 percent of domestic banks indicated that they had increased spreads of loan rates over their cost of funds for C&I loans to large and middle-market firms and to small firms--fractions slightly lower than those in the October survey. Likewise, very large fractions of banks reported having charged higher premiums on riskier loans and having increased the costs of credit lines to firms of all sizes over the survey period.

    On net, the fractions of banks that reported having tightened nonprice terms on C&I loans to large and middle-market firms over the past three months stayed at an elevated level but declined relative to the October survey. Large fractions of banks again noted that they had reduced both maximum size and the maximum maturity of loans or credit lines to firms of all sizes. In addition, about 70 percent of all domestic respondents reported having tightened covenants on C&I loans to large and middle-market firms and about 60 percent reported having done so on such loans to small firms. U.S. branches and agencies of foreign banks also tightened their business lending stance further over the past three months. About 65 percent of foreign institutions, a slightly smaller percentage than in October, indicated in the January survey that they had firmed their lending standards on C&I loans. Large fractions of foreign respondents had tightened price and nonprice terms on C&I loans over the survey period, including increasing the premiums charged on riskier loans, raising the cost of credit lines, and reducing the maximum size of credit lines. The majority of foreign banks also reported that they had imposed more-restrictive covenants and collateralization requirements on C&I loans.

    All domestic and foreign respondents pointed to a less favorable or more uncertain economic outlook as a reason for tightening their lending standards and terms on C&I loans over the past three months. Most respondents indicated that a worsening of industry-specific problems and their bank's reduced tolerance for risk were also important factors in their decision to tighten C&I lending policies. In contrast, only about 25 percent of the domestic respondents that had tightened standards or terms noted that a deterioration in their bank's current or expected capital position had contributed to the change, in comparison with approximately 40 percent in the October survey. High net percentages of foreign respondents were given as reasons for tightening standards and terms on C&I loans decreased liquidity in the secondary market for C&I loans (75 percent) and an increase in defaults by borrowers in public debt markets (70 percent).

    On balance, domestic and foreign respondents reported a further weakening of demand for C&I loans over the past three months. On net, about 60 percent of domestic respondents reported a reduction in demand for such loans from firms of all sizes, compared with about 15 percent of respondents that, on net, had reported a decrease in C&I loan demand in the October survey. About 25 percent, on net, of U.S. branches and agencies of foreign banks saw a decrease in demand for C&I loans over the past three months, compared with the 5 percent of respondents, on net, in the October survey.

    Substantial majorities of the domestic institutions that had experienced weaker demand for C&I loans over the past three months pointed to decreases in their customers' needs to finance investment in plant and equipment, to finance mergers and acquisitions, to finance inventories, and to finance customer accounts receivable as reasons for the weaker demand. Among the few domestic respondents that saw an increase in loan demand over the past three months, all indicated that business borrowing had shifted to their bank from other bank or nonbank sources because the other sources had become less attractive. In addition, over 30 percent of domestic and foreign institutions, on net, reported that inquiries from potential business borrowers had decreased during the survey period.

  - **Commercial Real Estate** – On balance, about 80 percent of domestic banks reported that they had tightened their lending standards on commercial real estate (CRE) loans over the past three months, slightly less than the roughly 85 percent that reported doing so in the October survey. Fifty percent of foreign respondents also indicated that they had tightened their lending standards on CRE loans. On net, about 55 percent of domestic and foreign respondents reported weaker demand for CRE loans over the survey period. In response to special questions on CRE lending, significant net fractions of banks reported having tightened many lending policies on CRE loans. Over 2008 as a whole, about 95 percent of domestic banks increased their loan-rate spreads, and about 80 percent tightened their loan-to-value ratios. About 75 percent of foreign respondents, on net, reported wider loan-rate spreads, and about 65 percent, on net, had reduced their loan-to-value ratios. About 30 percent of the domestic respondents indicated that the shutdown of the CMBS securitization market had led to an increase in CRE lending at their bank over the second half of 2008, whereas about 15 percent indicated that the shutdown of the CMBS securitization market had reduced the volume of their CRE lending.

- ❑ **Existing Credit Lines** – The January survey included a special question that queried banks on how they had changed the sizes of credit lines for existing customers for a number of account types over the past three months. On net, domestic banks reported that they had reduced the size of existing credit lines for all major types of business and household accounts. Regarding existing accounts for businesses, roughly 60 percent, on balance, reported a decrease in the limits on commercial construction lines of credit, about 50 percent indicated a decrease in the limits on credit lines extended to financial firms, about 30 percent indicated a decrease in credit limits on business credit card accounts, and roughly 25 percent noted a decrease in the size of C&I credit lines. On net, large fractions of foreign banks also decreased limits on commercial construction lines of credit, credit lines extended to financial firms, and C&I credit lines. Regarding accounts for households, about 40 percent of domestic banks reported having reduced the sizes of existing home equity lines of credit, on net, and approximately 35 percent reported having trimmed existing consumer credit card account limits.
- ❑ **Residential Real Estate Lending** – Smaller, though still substantial, fractions of domestic respondents reported having tightened lending standards on prime and nontraditional residential mortgages in the January survey. About 45 percent of domestic respondents indicated that they had tightened their lending standards on prime mortgages over the past three months, and almost 50 percent of the 25 banks that originated nontraditional residential mortgage loans over the survey period reported having tightened their lending standards on such loans. About 10 percent of domestic respondents saw weaker demand, on net, for prime residential mortgage loans over the past three months, a significantly lower fraction than the roughly 50 percent that so reported in the October survey. About 65 percent of respondents--a slightly lower percentage than in the October survey--reportedly experienced weaker demand for nontraditional mortgage loans over the same period. Only four banks reported making subprime mortgage loans over the past three month. On net, about 60 percent of domestic respondents, down from 75 percent in the October survey, noted that they had tightened their lending standards for approving applications for revolving home equity lines of credit (HELOCs) over the past three months. Twenty percent of domestic banks, on net, reported weaker demand for HELOCs over the past three months, slightly less than the percentage that had reported weaker demand in the October survey.
- ❑ **Consumer Lending** – Large fractions of domestic banks continued to report a tightening of policies on both credit card and other consumer loans over the past three months. Nearly 60 percent of respondents indicated that they had tightened lending standards on credit card and other consumer loans, about the same fractions as in the October survey. Close to 55 percent of respondents reported having reduced the extent to which both credit card accounts and other consumer loans were granted to customers who did not meet credit-scoring thresholds. Roughly 45 percent of the respondents also reported having raised minimum required credit scores on credit card accounts and other consumer loans, a proportion slightly lower than posted in the October survey. About 45 percent of banks reported having lowered credit limits for either new or existing credit card customers, down from the 60 percent that reported doing so in the October survey. On net, about 15 percent of domestic banks indicated that they had become either somewhat or much less willing to make consumer installment loans over the past three months, a notable change from the roughly 45 percent that so indicated in the October survey. About 45 percent of respondents, on net, reported that they had experienced weaker demand for consumer loans of all types, similar to the fraction in the October survey.
- ❑ **Use of Interest Rate Floors** – The January survey also included special questions regarding the use of interest rate floors in floating-rate loan agreements during 2008. Eighty percent of domestic banks cited an increase in their use of interest rate floors in such agreements with businesses last year, while about 45 percent of domestic banks cited an increase in the use of such rate floors on loans to households over the same period. No domestic bank reported a reduction in the use of interest rate floors on loans to businesses or households last year. Large fractions of domestic banks, however, noted that less than 5 percent of their outstanding loans--to both households and businesses--currently had interest rate floors that were binding, and only a small number of respondents indicated that the majority of their outstanding loans to households or businesses had binding rate floors.

National Events

National

❖ **<u>March 4, 2009</u>** –The Obama Administration announced new U.S. Department of the Treasury guidelines to enable servicers to begin modifications of eligible mortgages under the Administration's Homeowner Affordability and Stability Plan. The release of detailed requirements for the "Making Home Affordable" program facilitates implementation of the critical provisions that will help bring relief to responsible homeowners struggling to make their mortgage payments, while preventing neighborhoods and communities from suffering the negative spillover effects of foreclosure such as lower housing prices, increased crime and higher taxes.

Program details:

1. Home Affordable Refinance Program for Responsible Homeowners Suffering From Falling Home Prices
2. A Comprehensive $75 Billion Home Affordable Modification Program
3. Support Low Mortgage Rates by Strengthening Confidence in Fannie Mae and Freddie Mac.

(*U.S. Department of the Treasury)*

❖ **<u>February 17, 2009</u>** –The American Recovery and Reinvestment Act of 2009 (Recovery Act) was signed into law by President Obama on February 17th, 2009. It is an unprecedented effort to jumpstart our economy, create or save millions of jobs, and put a down payment on addressing long-neglected challenges so our country can thrive in the 21st century. The Act is an extraordinary response to a crisis unlike any since the Great Depression, and includes measures to modernize our nation's infrastructure, enhance energy independence, expand educational opportunities, preserve and improve affordable health care, provide tax relief, and protect those in greatest need. *(U.S. Department of Housing and Urban Development)*

Acknowledgements

Information used throughout this report originated from the following sources:

- The Consumer Confidence Board, New York, NY
- Federal Deposit Insurance Corporation, Washington, D.C.
- Federal Reserve Bank of Dallas, Dallas, TX
- Federal Reserve Bank of St. Louis, St. Louis, MO
- Federal Reserve Board, Washington D.C.
- Mortgage Bankers Association, Washington D.C.
- Real Estate Center, Texas A&M University, College Station, TX
- RealtyTrac, Inc., Irvine, CA
- SNL Financial
- Texas Comptroller of Public Accounts, Austin, TX
- Texas Department of Banking, Austin, TX
- Texas Department of Savings and Mortgage Lending, Austin, TX
- Texas Workforce Commission, Austin, TX
- The White House, Washington D.C.
- U.S. Bureau of Labor Statistics, Washington, D.C.
- U.S. Department of Housing and Urban Development, Washington, D.C.
- U.S. Department of the Treasury
- Yahoo Finance