

PUBLIC DISCLOSURE

August 9, 1999

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

**The First National Bank of Hughes Springs
Charter Number 6922**

**418 East First Street
Hughes Springs, Texas 75656**

**Office of the Comptroller of the Currency
Longview Field Office
1800 West Loop 281
Suite 306
Longview, Texas 75604**

NOTE: This evaluation is not, nor should it be construed as, an assessment of the financial condition of this institution. The rating assigned to this institution does not represent an analysis, conclusion or opinion of the federal financial supervisory agency concerning the safety and soundness of this financial institution.

GENERAL INFORMATION

The Community Reinvestment Act (CRA) requires each federal financial supervisory agency to use its authority when examining financial institutions subject to its supervision, to assess the institution's record of meeting the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound operation of the institution. Upon conclusion of such examination, the agency must prepare a written evaluation of the institution's record of meeting the credit needs of its community.

*This document is an evaluation of the Community Reinvestment Act (CRA) performance of **The First National Bank of Hughes Springs** prepared by the **Office of the Comptroller of the Currency**, the institution's supervisory agency, as of **August 9, 1999**. The agency rates the CRA performance of an institution consistent with the provisions set forth in Appendix A to 12 CFR Part 25.*

INSTITUTION'S CRA RATING: This institution is rated Satisfactory.

The First National Bank of Hughes Springs has a Satisfactory record of meeting community credit needs. This rating is based on the following:

- < The bank's loan-to-deposit ratio is more than reasonable when compared to other area banks.
- < A majority of the bank's loans are extended within its assessment area.
- < Credit activity is reasonably distributed to borrowers of different income levels.

DESCRIPTION OF INSTITUTION:

The First National Bank of Hughes Springs (FNB) is a \$107 million financial institution with six full-service locations and one stand alone drive-in facility. The bank's main office is located at 418 E. First Street, Hughes Springs, Texas. Branches are located in nearby Omaha, Liberty City, Daingerfield, Atlanta, and a drive-in facility in Queen City. In addition, FNB acquired The First National Bank of Jefferson on August 9, 1999. The institution is retail oriented and offers a wide range of deposit and loan products. The loan portfolio consists of the following: 52% commercial and commercial real estate; 23% residential real estate; 20% consumer related; and 5% agricultural. As of June 30, 1999, loans totaled \$66 million and represented 62% of the bank's total assets. The bank is a wholly owned subsidiary of Chalybeate Springs Corporation, a one bank holding company and Hughes Springs Corporation, an intermediate holding company based in Delaware. Each holding company is \$107 million in assets. Bank management elected to become a Subchapter "S" Corporation effective January 1, 1997. There are no legal or other impediments which limit the bank's ability to help meet the community's credit needs. The bank was rated Satisfactory during the prior CRA Examination dated April 30, 1996.

DESCRIPTION OF ASSESSMENT AREAS:

Based on the location of the branch offices, the Board of Directors has designated two separate assessment areas for CRA purposes. As the acquisition of the Jefferson branch was consummated on August 9, 1999, the Board of Directors had not yet determined the parameters of this new assessment area as of the CRA Examination date. A review of the bank's performance within the Jefferson branch assessment area will be conducted during the next scheduled CRA Examination.

Morris/Cass County Assessment Area:

Morris and Cass Counties have been designated as one assessment area serviced by the Hughes Springs, Omaha, Daingerfield, Atlanta, and Queen City offices. This assessment area includes eight of the ten identified Block Numbering Areas (BNAs) for these two contiguous counties and is not a part of a Metropolitan Statistical Area (MSA). BNA 9505 (Bivins-McLeod Division) and 9506 (Linden Division) were excluded from Cass County due to the location of other financial institutions in these areas. Management does not feel the bank can reasonably service these two areas. The eight BNAs included in the assessment area are all designated as middle income geographies. There are no low or moderate income BNAs in either county. The assessment area meets the requirements of the Community Reinvestment Act and does not arbitrarily exclude low and moderate income geographies. The population of this assessment area totals 35,738. The percentage of families within each income category is as follows:

low income - 22%; moderate income - 17%; middle income - 21%; and upper income - 40%. According to 1998 Department of Housing and Urban Development (HUD) information, the median family income for this area is \$33,900 with 22.32% of the households below poverty level. Housing units within the assessment area include 66% owner occupied units with a median housing value of \$37,476. Major employers include Lone Star Steel, Texas Pipe Coupling, Daingerfield-Lone Star Independent School District, Hughes Springs Independent School District, Atlas Roofing, Scot Industries, and A & E Machine Shop. Competition within the assessment area includes five banks and one credit union. The local economy is considered stagnant with an unemployment rate for Cass County of 8.6% and for Morris County 14.9% as of November 1998. Based on recent contacts with a quasi-government official, the most pressing need within the community is affordable housing. This contact indicated that financial institutions in the area are working with the community (i.e., Project Hughes Springs) to meet this identified need through residential lending and other programs.

Liberty City Assessment Area:

The second assessment area consists of Census Tract 104 in the Longview-Marshall Metropolitan Statistical Area (MSA) and is serviced by the Liberty City branch. Contiguous census tracts have been excluded due to the intense competition of other financial institutions in these areas. Census Tract 104 is designated as a middle income geography. The assessment area meets the requirements of the Community Reinvestment Act and does not arbitrarily exclude low and moderate income geographies. The population of this assessment area totals 6,487. The percentage of families within each income category is as follows: low income - 19%; moderate income - 15%; middle income - 25%; and upper income - 41%. According to 1998 Department of Housing and Urban Development (HUD) information, the median family income for this area is \$39,900 with 16.67% of the households below poverty level. Housing units within the assessment area include 77% owner occupied units with a median housing value of \$53,100. A majority of the residents of Liberty City commute to surrounding cities such as Longview and Kilgore to work. Liberty City is primarily a residential community with very limited industry and commercial business. The area is very stable with an unemployment rate of 2.79%. As part of our evaluation, we contacted a local community group leader. This contact indicated both new and affordable housing as the primary needs within the community. There currently is intense competition in regard to residential lending products offered through the approximately forty financial institutions located in the MSA.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA:

LOAN TO DEPOSIT RATIO:

The loan-to-deposit ratio of The First National Bank of Hughes Springs is more than reasonable given the bank's size, financial condition, and assessment area credit needs and meets the standards for satisfactory performance. The bank's average quarterly loan-to-deposit ratio was 69.40% since the prior CRA examination as of April 30, 1996. The average loan-to-deposit ratio of other local community banks within the assessment area for the same time period was 62.23%. The quarterly loan-to-deposit ratio of these banks ranged from a low of 42.54% to a high of 75.95%.

LENDING IN ASSESSMENT AREA:

The bank's lending activity within both assessment areas meets the standards for satisfactory performance. A majority of the bank's lending activity is located within both assessment areas.

Morris/Cass County Assessment Area:

Concerning the Morris/Cass County Assessment Area, we reviewed a sample of 332 residential real estate loans, 20 consumer loans, and 20 commercial loans originated since April 1996. This sample reflected approximately 79.30% of the number of loans and 75.93% of the dollar amount of loans were extended within the bank's assessment area. The breakdown by loan category in the Morris/Cass County Assessment Area is illustrated in the following tables:

Consumer Loans	Number	Percent	\$ (000's)	Percent
Inside Assessment Area	17	85.00%	34	85.00%
Outside Assessment Area	3	15.00%	6	15.00%

Residential Real Estate Loans	Number	Percent	\$ (000's)	Percent
Inside Assessment Area	264	79.52%	5,730	74.19%
Outside Assessment Area	68	20.48%	1,993	25.81%

Business Loans	Number	Percent	\$ (000's)	Percent
Inside Assessment Area	14	70.00%	768	91.43%
Outside Assessment Area	6	30.00%	72	8.57%

Liberty City Assessment Area:

Concerning the Liberty City Assessment Area, we reviewed a sample of 31 residential real estate loans, 20 consumer loans, and 49 commercial loans originated since April 1996. This sample reflected approximately 61.00% of the number of loans and 70.46% of the dollar amount of loans in our sample were extended within the bank's assessment area. The breakdown by loan category in the Liberty City Assessment Area is illustrated in the following tables:

Consumer Loans	Number	Percent	\$ (000's)	Percent
Inside Assessment Area	14	70.00%	46	63.01%
Outside Assessment Area	6	30.00%	27	36.99%

Residential Real Estate Loans	Number	Percent	\$ (000's)	Percent
Inside Assessment Area	21	67.74%	588	67.59%
Outside Assessment Area	10	32.26%	282	32.41%

Business Loans	Number	Percent	\$ (000's)	Percent
Inside Assessment Area	26	53.06%	940	72.81%
Outside Assessment Area	23	46.94%	351	27.19%

LENDING TO BORROWERS OF DIFFERENT INCOME AND TO BUSINESSES OF DIFFERENT SIZES:

The level of lending to borrowers of different income and to businesses of different sizes meets the standards for satisfactory performance. The distribution of loans within the assessment area reflects a reasonable penetration among borrowers of different income levels and businesses of different sizes. The bank's primary product lines are residential loans, commercial and commercial real estate loans, and consumer loans.

Morris/Cass County Assessment Area:

The distribution of residential real estate and consumer loans generally approximates the income characteristics of this assessment area. The following tables detail the results of our borrower analysis within the Morris/Cass County Assessment Area:

Lending to Borrowers of Different Income Levels Residential Real Estate Loans					
Borrower Income Category	# of Loans	Percentage	\$ (000's)	Percentage	% of Families within each Income Category
Low	54	20.45%	482	8.41%	22.13%
Moderate	56	21.21%	824	14.38%	17.00%
Middle	59	22.35%	1,267	22.11%	20.47%
Upper	95	35.99%	3,157	55.10%	40.40%
Total	264	100.00%	5,730	100.00%	100.00%

Lending to Borrowers of Different Income Levels Consumer Loans					
Borrower Income Category	# of Loans	Percentage	\$ (000's)	Percentage	% of Families within each Income Category
Low	9	52.94%	7	21.21%	22.13%
Moderate	2	11.77%	2	6.06%	17.00%
Middle	5	29.41%	23	69.70%	20.47%
Upper	1	5.88%	1	3.03%	40.40%
Total	17	100.00%	33	100.00%	100.00%

The distribution of business loans also reflects a reasonable penetration among businesses of different sizes. Based on U.S. Census information, there are 781 businesses in the assessment area with revenues less than \$1 million. This number represents 76% of all businesses within the assessment area. Based on our review, 78.57% of the business loans we sampled which originated within the Morris/Cass County Assessment Area were to small businesses with gross annual revenues of less than \$1 million. Refer to the following table for details:

Distribution of Small Business Loan Originations Sample Within the Assessment Area by Business Revenues				
Business Annual Revenues	# Loans	Percentage	\$(000's)	Percentage
Less than \$100,000	6	42.86%	349	13.35%
\$100,000 to \$250,000	2	14.28%	242	9.25%
\$250,000 to \$1,000,000	3	21.43%	1,470	56.21%
Subtotal Small Businesses	11	78.57%	2,061	78.81%
Over \$1,000,000	3	21.43%	554	21.19%
Totals	14	100.00%	2,615	100.00%
Distribution of Businesses in the Assessment Area by Annual Revenues of the Business:			< 1 Million	76%
			> 1 Million	7%
			Unknown	17%

Source: Dun & Bradstreet Business Demographic Data

Liberty City Assessment Area:

While home purchase loans to low income families are at a low level compared to the demographic information, consumer loans closely approximate the percentage of low income families. Borrowing for home purchases by low income individuals is limited due to the low level of affordable housing stock available in the assessment area. In addition, intense competition exists among other financial institutions within the Longview-Marshall MSA to provide Federal National Mortgage Association (FNMA) and Federal Housing Administration (FHA) loans which offer lower down payments and closing costs, and more flexible loan terms. The following tables detail the results of our analysis.

Lending to Borrowers of Different Income Levels Residential Real Estate Loans					
Borrower Income Category	# of Loans	Percentage	\$ (000's)	Percentage	% of Families within each Income Category
Low	1	4.76%	24	4.08%	18.52%
Moderate	9	42.86%	268	45.58%	15.27%
Middle	6	28.57%	145	24.66%	25.38%
Upper	5	23.81%	151	25.68%	40.83%
Total	21	100.00%	588	100.00%	100.00%

Lending to Borrowers of Different Income Levels Consumer Loans					
Borrower Income Category	# of Loans	Percentage	\$ (000's)	Percentage	% of Families within each Income Category
Low	7	50.00%	11	23.91%	18.52%
Moderate	3	21.43%	3	6.52%	15.27%
Middle	1	7.14%	3	6.52%	25.38%
Upper	3	21.43%	29	63.05%	40.83%
Total	14	100.00%	46	100.00%	100.00%

The distribution of business loans also reflects a reasonable penetration among businesses of different sizes. Based on U.S. Census information, there are 45 businesses in the assessment area with revenues less than \$1 million. This number represents 76% of all businesses within the assessment area. Based on our review, 100% of the business loans we sampled which originated within the Liberty City Assessment Area were to small businesses with gross annual revenues of less than \$1 million. Refer to the following table for details:

Distribution of Small Business Loan Originations Sample Within the Assessment Area by Business Revenues				
Business Annual Revenues	# Loans	Percentage	\$(000's)	Percentage
Less than \$100,000	12	46.16%	536	12.44%
\$100,000 to \$250,000	7	26.92%	844	19.58%
\$250,000 to \$1,000,000	7	26.92%	2,930	67.98%
Subtotal Small Businesses	26	100.00%	4,310	100.00%
Over \$1,000,000	0	0.00%	0	0.00%
Totals	26	100.00%	4,310	100.00%
Distribution of Businesses in the Assessment Area by Annual Revenues of the Business:			< 1 Million	76%
			> 1 Million	5%
			Unknown	19%

Source: Dun & Bradstreet Business Demographic Data

GEOGRAPHIC DISTRIBUTION OF LOANS:

A geographic analysis of lending activity within the bank's two assessment areas was not performed as it would not be meaningful. There are no low or moderate income geographies located in either assessment area. The two BNAs in Cass County which were excluded from the bank's assessment area were identified as middle income areas.

RESPONSE TO COMPLAINTS:

Management has not received any written complaints related to CRA performance since the prior CRA Examination.

RECORD OF COMPLIANCE WITH ANTIDISCRIMINATION LAWS:

A Fair Lending Examination was performed in conjunction with this examination. We reviewed a sample of unsecured consumer loan approvals and denials to test for discrimination on the basis of gender. Based on the sample we reviewed, no discriminatory practices were noted. The bank is in compliance with the substantive provisions of antidiscrimination laws and regulations.