

PUBLIC DISCLOSURE

May 5, 2003

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

**First State Bank
Certificate Number: 11910**

**911 North 287 Bypass
P.O. Box 219
Grapeland, Texas 75844-0219**

Federal Deposit Insurance Corporation

**Division of Supervision and Consumer Protection
1910 Pacific Avenue, 19th Floor
Dallas, Texas 75201**

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.

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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 **First State Bank** prepared by the **Federal Deposit Insurance Corporation**, the institution's supervisory agency, as of **May 5, 2003**. The agency rates the CRA performance of an institution consistent with the provisions set forth in Appendix A to 12 CFR Part 345.*

INSTITUTION RATING

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

First State Bank received a Satisfactory rating at the July 29, 1998 evaluation. The bank's lending focus has remained unchanged since the last evaluation. Examiners evaluated this \$62 million institution's CRA performance based on small bank lending performance criteria that includes the following: loan-to-deposit ratio; lending in the assessment area; geographic distribution of loans; and lending to borrowers of different incomes. There were no CRA-related complaints since the last examination; therefore, this factor was not considered. Management did not request the review of qualified investments and services at this evaluation.

The evaluation was based on the bank's originations of consumer and residential real estate loans within the assessment area. The performance relating to consumer lending receives more weight as this loan product represents 73 percent of the number and 31 percent of the dollar volume of loans originated within a two-year period. Although residential real estate lending also accounted for 31 percent of the dollar volume, it comprised 11 percent by number volume. Individual findings and ratings for these four factors are summarized below. A detailed discussion of each factor is provided elsewhere in this evaluation.

- The average loan-to-deposit ratio since the last examination of 58 percent reflects a reasonable responsiveness to the assessment area credit needs consistent with similarly situated banks of similar size.
- A substantial majority of the loans are within the assessment area demonstrating an excellent performance.
- The geographic distribution of consumer and residential real estate loans is poor in comparison with the number of households and the percent of owner-occupied housing units.
- An analysis of consumer and residential real estate loans revealed an overall satisfactory penetration among borrowers of different income levels.

DESCRIPTION OF INSTITUTION

First State Bank operates its main office location in a middle-income block numbering area (BNA), in Grapeland, Texas. The bank has a branch office located in a middle-income BNA in Crockett, Texas.

First State Bank reported total assets of \$61,504,000 as of December 31, 2002. Selected financial information from the Consolidated Reports of Condition and Income is presented below.

Table 1: Financial Data as of December 31, 2002

Assets	Amount \$(000)	Liabilities	Amount \$(000)
Net Loans & Leases	23,507	Total Deposits	40,368
Total Investments	17,653	Other Borrowed Money	15,954
Cash	17,481	Other Liabilities	70
Premises & Other Assets	2,863	<i>Total Liabilities</i>	56,392
		Equity Capital	5,112
Total Assets	61,504	Total Liabilities & Capital	61,504

Source: Consolidated Report of Condition and Income

First State Bank's primary business focus is directed towards consumer and residential real estate loans. The bank's largest loan category by dollar amount is residential real estate loans followed by consumer loans. Presented in Table 2 are details of loan categories within the portfolio by percent of dollar volume as of December 31, 2002.

Table 2: Loan Portfolio Mix as of December 31, 2002

Loan Type	Percent of Portfolio (%)
Consumer Loans	29
Agricultural Loans (including real estate secured)	15
1-4 Family Residential Real Estate	35
Commercial & Industrial Loans (including real estate secured)	21
Total	100

Source: Consolidated Report of Condition and Income

First State Bank offers an array of deposit services, including demand deposits, NOW, MMDA, savings and time accounts. Customers may also transact business by calling the bank's customer service department during business hours. Also, sufficient types of credit are available through various consumer loan programs, mortgage, real estate, agricultural, and commercial loans. First State Bank has adequate resources to meet the loan and deposit needs of its customers.

No legal or financial impediments exist which would prohibit the bank from meeting the credit needs of the community.

The bank offers convenient lobby operations and drive-through services at both locations. See Table 3 below for detailed banking hours.

Table 3: Banking Hours

	Main Office	Branch
Lobby Hours	Monday – Thursday 9:00 a.m. to 3:00 p.m. Friday 9:00 a.m. to 5:00 p.m.	Monday – Thursday 9:00 a.m. to 3:00 p.m. Friday 9:00 a.m. to 5:30 p.m.
Drive-through Hours	Monday – Thursday 7:00 a.m. to 3:00 p.m. Friday 7:00 a.m. to 5:00 p.m. Saturday 7:00 a.m. to 11:00 a.m.	Monday – Thursday 7:30 a.m. to 5:30 p.m. Friday 7:30 a.m. to 5:30 p.m. Saturday 7:30 a.m. to 12:00 noon

DESCRIPTION OF ASSESSMENT AREA

First State Bank’s assessment area encompasses all of Houston County and portions of Anderson and Trinity Counties. The assessment area is composed of 10 BNAs (three moderate-income and seven middle-income). There are no low-income BNAs in the assessment area. The 1990 United States Census reported 30 percent of the households in the assessment area as low-income and 15 percent as moderate-income households. Twenty-five percent of the households lived below the poverty level in 1990 compared to 25 percent according to the 2000 U.S. Census information.

The total population of the assessment area in 1990 was 31,737, while the 2000 U.S. Census information reports the total population to be 34,972. The population of the assessment area has increased approximately 9 percent. The 1990 median family income (MFI)¹ for the assessment area was \$23,893. The Department of Housing and Urban Development (HUD) estimated the 2001 and 2002 MFI for the non-metropolitan area of Texas to be \$35,800 and \$36,100, respectively.

First State Bank’s main and branch offices are located in Houston County. Based on the 2000 U.S. Census information there are 8,259 households and 5,786 families in Houston County. Sixteen percent of the families live below poverty. Further, the 2000 U.S. Census reported 10,730 housing units in Houston County and the ownership rate is 76 percent.

¹ HUD estimates of 2001 and 2002 median family incomes (MFI) for the Non - MSA are used to determine income classification for individual borrowers. *Low-income* individuals have a MFI of less than 50 percent of the respective Non - MSA figure. Likewise, the *moderate-income* individuals have a MFI of 50 percent to less than 80 percent, *middle-income* individuals have a MFI of 80 percent to less than 120 percent, and *upper-income* individuals have a MFI of 120 percent or more of the Non - MSA figure.

First State Bank is situated in Grapeland, Texas. Grapeland is located southeast of Dallas on Highway 287, between Palestine and Crockett, Texas. The branch office is located approximately 13 miles south of Grapeland in Crockett, Texas. Crockett is the county seat for Houston County. The economy of the assessment area is derived from education, health and social services followed by manufacturing, retail trade, and agriculture, forestry, fishing and hunting, and mining, respectively.

A community contact stated farming in the assessment area is diminishing, and most of the working class in Grapeland is employed at Nucor Steel Manufacturing. He further stated that some of the individuals work at the nearby prisons facility. In addition, he stated that there is a need for new homes for middle-income individuals in the assessment area.

The assessment area conforms to regulatory requirements since low- and moderate-income areas have not been arbitrarily excluded, is comprised of whole geographies, and includes the bank and its branch location.

Table 4 below shows demographic information for the assessment area derived from the 1990 U.S. Census.

Table 4: First State Bank’s Assessment Area - BNA Data by Income Level

Income Level	Number of BNAs	Percent of BNAs (%)	Population	Percent of Population (%)	Households	Percent of Households (%)
Moderate	3	30	7,153	23	2,770	23
Middle	7	70	24,584	77	9,141	77
Total	10	100	31,737	100	11,911	100

Source: 1990 U.S. Census.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

Sampling Information

The scope of the evaluation normally includes residential real estate, small business (commercial), and small farm (agricultural) lending. As depicted in Table 5, First State Bank’s consumer loans comprise the largest loan category by number and dollar volume. Residential real estate loans represent only 11 percent of the number of loans, but also 31 percent of the dollar volume of loans extended. Therefore, these two loan products were selected to evaluate the bank’s lending performance under the Community Reinvestment Act. Commercial and agricultural loans were not selected for analysis because of the decline in agricultural activity in recent years and the small number of commercial loan borrowers, which represents only 4 percent of loans originated during the analysis period. Also, the agricultural lending activity is misleading as it often includes loans to the same borrowers, resulting in a fewer number of actual borrowers, thus making an analysis less meaningful. Residential real estate loans represent a

growing loan product for the bank in recent years due to the influx of retirees with a need for home purchase loans.

In order to evaluate the lending performance of the bank, samples of consumer and residential real estate loans were selected. A random sample, using a 90 percent confidence interval and 15 percent precision level, of 42 consumer loans totaling \$349,909 originated between January 1, 2001 and December 31, 2002 was selected from a potential universe of 638 loans totaling \$6,125,110 for the same period. Because the bank is not a HMDA reporter, another random sample of 24 residential real estate loans totaling \$1,334,716 originated during the same period was selected from a potential universe of 97 loans totaling \$6,272,793. Table 5 below illustrates the breakdown of the bank's lending activity.

Table 5: Loan Origination from January 1, 2001 through December 31, 2002

Loan Type	Number	Percent (%)	Amount \$(000)	Percent (%)
Agricultural	108	12	3,305	17
Commercial	35	4	4,278	21
Residential Real Estate	97	11	6,273	31
Consumer	638	73	6,125	31
Gross Loans	878	100	19,981	100

Source: Bank records.

Bank records for 2001 and 2002 for consumer and residential real estate loans were reviewed, comparing the percent of households and the percent of owner-occupied housing, respectively, in the assessment area.

LOAN-TO-DEPOSIT RATIO

The bank's lending activity, as measured by its loan-to-deposit (LTD) ratio, is reasonable. Since loans are primarily funded through the bank's deposits, examiners reviewed the bank's LTD ratios using data from the Consolidated Report of Condition and Income for the 18 quarters since the last evaluation at July 29, 1998, which was an average of 64 percent. As of December 31, 2002, First State Bank's LTD ratio is 58 percent. Table 6 shows a list of similarly situated banks for comparison.

Table 6: Loan-to-Deposit Ratio Comparative Analysis as of December 31, 2002

Bank Name	Total Assets \$(000)	Total Net Loans \$(000)	Total Deposits \$(000)	Average LTD Ratio (%)
<i>First State Bank, Grapeland</i>	61,504	23,507	40,368	63.58
Citizens State Bank, Buffalo	97,924	36,022	86,800	56.95
Citizens National Bank, Crockett	70,109	37,925	62,914	54.39
Community State Bank, Boling	60,049	21,934	54,321	40.44

Source: Consolidated reports of Condition and Income

In comparison, Citizens State Bank, Buffalo, located approximately 40 miles southeast of Grapeland, is most similar in asset mix. Citizens National Bank is located approximately 12 miles from First State Bank and is most competitive.

After considering and reviewing First State Bank’s asset size, competition, and lending opportunities, the bank’s loan-to-deposit ratio, as compared to the above financial institutions, is reasonable.

LENDING IN THE ASSESSMENT AREA

The bank’s proportion of lending activity within the assessment area is excellent. A sample of consumer and residential real estate loans, as depicted in Table 7 below, was analyzed to determine the bank’s lending performance within its assessment area. Data in Table 7 reflects that a substantial majority of its loans are in the assessment area.

Criteria for a bank’s lending performance is based on the number and dollar volume of loans originated within the assessment area. Table 7 illustrates the bank’s lending performance in the assessment area from January 1, 2001 through December 31, 2002.

Table 7: Distribution of Loans Inside and Outside of the Assessment Area

Loan Category	Number of Loans				Total #	Dollars of Loan \$(000)				Total \$(000) \$
	Inside		Outside			Inside		Outside		
	#	%	#	%		\$	%	\$	%	
Consumer	38	90	4	10	42	282	81	68	19	350
Residential Real Estate	24	100	0	0	24	1,335	87	0	0	1,335
Total	62	94	4	6	66	1,617	96	68	4	1,685

Source: Bank Records.

Consumer and residential real estate lending inside the assessment area is reflective of an excellent performance given the small size of the bank’s designated assessment area, asset size, and resources.

GEOGRAPHIC DISTRIBUTION OF LOANS

The geographic distribution of loans reflects a poor penetration throughout the bank’s assessment area. The results of both sampled loan products support the conclusion.

Consumer Loans

A poor performance was noted regarding the bank’s geographic distribution of consumer loans. Based on the sampled loans, there were no loans made to consumers residing in moderate-income geographies as shown in Tables 8 and 9. As previously stated, typically, loans are originated in areas within close proximity of a bank’s office location. The bank’s main office

and the branch are located in middle-income geographies. There are three moderate- and seven middle-income geographies in the assessment area. Two moderate-income geographies are located in Houston County, in Crockett and Porter Springs, Texas. Competition for First State Bank is strong in Crockett, Texas. The competition includes Citizens National Bank, First National Bank of Crockett and a branch of First National Bank Huntsville. In addition to the banks mentioned in Crockett, Lovelady State Bank is also a competitor in Houston County. Competitors also include The Elkhart State Bank in Anderson County and The First National Bank and Lake Area National Bank in Trinity County.

Table 8: Geographic Distribution of Consumer Loans by Number for January 1, 2001 through December 31, 2002

Income Level of BNA	Households	Percent of Households (%)	Number of Loans (#)	Percent (%)
Moderate	2,770	23	0	0
Middle	9,141	77	38	100
Total	11,911	100	38	100

Source: 1990 U.S. Census. Bank Records

Table 9: Geographic Distribution of Consumer Loans by Dollar Volume January 1, 2001 through December 31, 2002

Income Level of BNA	Households	Percent of Households (%)	Dollar Volume of Loans \$(000)	Percent (%)
Moderate	2,770	23	0	0
Middle	9,141	77	282	100
Total	11,911	100	282	100

Source: 1990 U.S. Census. Bank Records.

The geographic distribution of consumer loans reflects a poor dispersion throughout the assessment area since the sample does not reveal any loans dispersed in the moderate-income geographies.

Residential Real Estate Loans

First State Bank's record of residential real estate lending among geographies within the assessment area, primarily the moderate-income areas, is marginally adequate. Less than 10 percent by number and dollar volume of residential real estate loans are made in moderate-income geographies as compared to 21 percent of the number of owner-occupied housing units.

As stated previously, the main and branch offices are located in middle-income geographies. Typically, loans are originated in areas within close proximity of a bank's office location. Tables 10 and 11 on the following page reflect the bank's performance in number and dollar volume when compared to the percent of owner-occupied housing units.

**Table 10: Geographic Distribution of Residential Real Estate Loans by Number for
January 1, 2001 through December 31, 2002**

Income Level of BNA	Total Owner-Occupied Housing Units	% of Total Owner-Occupied Housing Units	Number of Loans (#)	Percent (%)
Moderate	1,836	21	2	8
Middle	7,116	79	22	92
Total	8,952	100	24	100

Source: 1990 U.S. Census. Bank Records

**Table 11: Geographic Distribution of Residential Real Estate Loans by Dollar volume for
January 1, 2001 through December 31, 2002**

Income Level of BNA	Total Owner-Occupied Housing Units	% of Total Owner-Occupied Housing Units	Dollar Volume of Loans \$(000)	Percent (%)
Moderate	1,836	21	51	4
Middle	7,116	79	1,284	96
Total	8,952	100	1,335	100

Source: 1990 U.S. Census. Bank Records.

Seventy-three percent of the residential mortgage loans sampled inside the assessment area originated in the middle-income geography where the bank is located. Twenty percent of the residential mortgage loans were originated in the middle-income geography of the branch location. In addition, the 2000 U.S. Census information revealed that 41 percent of the families in the moderate-income geography in Trinity County lived below poverty level, and 32 percent and 40 percent of the families in the moderate-income tracts of 9502 and 9504, respectively, in Houston County are below poverty status. These families are least likely to qualify for mortgage loans.

Considering the location of the bank to its moderate-income geographies, the bank's competition in those areas, and the economic status of many of the individuals living in the moderate-income tracts, First State Bank's residential real estate lending performance is considered marginally adequate when compared to the percent of owner-occupied housing units.

The bank's dispersion of loans in geographies of different incomes, based on the poor performance of consumer lending and marginally adequate record for residential real estate lending, reflects an overall poor performance in relation to the geographic makeup of the assessment area, the location of its offices, and levels of families below poverty.

LENDING TO BORROWERS OF DIFFERENT INCOMES

The overall performance for this factor is satisfactory after taking into consideration the bank's lending focus and competitive nature of the market. The distribution of consumer and residential real estate loans demonstrates a satisfactory penetration among borrowers of different incomes. The consumer lending record to low- and moderate-income borrowers is satisfactory; however,

the lending record for residential real estate is marginally satisfactory. Nevertheless, examiners focused more on the bank's consumer lending record in arriving at the overall rating for this factor.

Consumer Loans

The bank's performance of extending consumer credit to borrowers of different incomes is satisfactory. Tables 12 and 13 below present a comparison of the number and dollar volume of consumer loans extended within the bank's assessment area and the percent of assessment area households with incomes in the different ranges.

The data in the tables reveal that the bank has demonstrated satisfactory performance in the number of loans originated to low- and moderate-income borrowers when compared to the percent of assessment area households. The distribution of the number of consumer loans is typically weighted to lower-income borrowers. Consumer loans are often more in demand by low- and moderate-income borrowers due to their smaller loan size. Additionally, middle- and upper-income borrowers generally have access to more sources of funding for these types of credit.

**Table 12: Distribution of Consumer Loans by Borrower Income
January 1, 2001 through December 31, 2002**

Borrower Income Level	Households	Percent of Households (%)	Number of Loans (#)	Percent (%)
Low	3,591	30	16	42
Moderate	1,766	15	6	16
Middle	1,749	15	10	26
Upper	4,805	40	6	16
Total	11,911	100	38	100

Source: 1990 U.S. Census, Bank Records.

Table 13 illustrates that by dollar volume, the performance for low- and moderate-income consumer loan borrowers is marginally adequate. However, in terms of consumer loans, more weight is given to the bank's record by number than by dollar volume because small dollar consumer loans do not positively impact the percentages.

**13: Distribution of Consumer Loans by Borrower Income
January 1, 2001 through December 31, 2002**

Borrower Income Level	Households	Percent of Households (%)	Dollar Volume of Loans \$(000)	Percent (%)
Low	3,591	30	62	22
Moderate	1,766	15	30	11
Middle	1,749	15	97	34
Upper	4,805	40	93	33
Total	11,911	100	282	100

Source: 1990 U.S. Census, Bank Records.

Residential Real Estate Loans

The bank displays a marginally satisfactory level of performance in lending to borrowers of different incomes. Tables 14 and 15 below illustrate the bank’s performance among borrowers of different income levels when compared to the percent of assessment area households. The number and dollar volume of residential real estate loans made to low- and moderate-income borrowers is below the percentage of assessment area households of those borrowers, but within a reasonable range. U.S. Census information for 1990 revealed that 30 percent of the households were low-income and 25 percent lived below poverty. Based on the 2000 U.S. Census information, 25 percent of the households in the assessment area remain below poverty level. Usually these individuals have difficulty in qualifying for a home loan. In addition, a community contact indicated that many of the low- and moderate-income individuals are older retired individuals on fixed incomes and could not afford a new home.

**Table 14: Distribution of Residential Real Estate Loans by Borrower Income
January 1, 2001 through December 31, 2002**

Borrower Income Level	Households	Percent of Households (%)	Number of Loans (#)	Percent (%)
Low	3,591	30	2	8
Moderate	1,766	15	2	9
Middle	1,749	15	7	29
Upper	4,805	40	13	54
Total	11,911	100	24	100

Source: 1990 U.S. Census. Bank Records

The distribution of residential real estate loans by dollar volume is very similar to the record by number of loans. Generally, examiners emphasize on the bank’s record by number, which gives a better indication of the penetration among borrowers of different incomes.

**Table 15: Distribution of Residential Real Estate Loans by Borrower Income
January 1, 2001 through December 31, 2002**

Borrower Income Level	Households	Percent of Households (%)	Dollar Volume of Loans \$(000)	Percent (%)
Low	3,591	30	29	2
Moderate	1,766	15	128	10
Middle	1,749	15	245	18
Upper	4,805	40	933	70
Total	11,911	100	1,335	100

Source: 1990 U.S. Census. Bank Records.

Considering the facts mentioned above, the distribution of residential real estate loans by borrower income is considered marginally adequate.

Overall, the bank has demonstrated marginally adequate performance in originating loans to low- and moderate-income borrowers.

RESPONSE TO CRA-RELATED COMPLAINTS

The bank did not receive any CRA-related complaints since the previous evaluation. Management has procedures in place to address complaints of this nature.

COMPLIANCE WITH ANTI-DISCRIMINATION LAWS

No substantive violations of the anti-discrimination laws were identified. First State Bank has adequate procedures in place to ensure ongoing compliance with the technical requirements of the laws, including review, monitoring, and training procedures.

GLOSSARY

Block Numbering Areas (BNAs) - a small locally demarcated area, usually in a metropolitan neighborhood.

Census Tract - a small locally demarcated area, usually in a metropolitan neighborhood, defined by the Census Bureau to generally consist of stable boundaries and an average population of 4,000.

Dun & Bradstreet – a leading provider of business information for credit, marketing and purchasing decisions in the U.S. and worldwide.

Low-income -

- for a census tract - this refers to income levels less than 50% of the MFI for the MSA in which the tract is located.
- for individuals - this refers to income levels less than 50% of the most recent year's estimation of the MFI by the Department of Housing and Urban Development (HUD).

MFI - median family income as determined by the Census Bureau or HUD.

Middle-income - determined using the same methodology as for low-income. The percentage used for middle-income designation is $80\% \leq 120\%$.

Moderate-income - determined using the same methodology as for low-income. The percentage used for moderate-income designation is $50\% \leq 80\%$.

MSA - metropolitan statistical area as determined by the Census Bureau. Usually consists of contiguous census tracts and block numbering areas comprising one or more counties including a large population nucleus and nearby communities that have a high degree of interaction and which usually have a combined population of greater than 50,000.

Upper-income - determined using the same methodology as for low-income. The percentage used for upper-income designation is 120% or greater.