

PUBLIC DISCLOSURE

January 12, 2004

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

**First State Bank
Certificate Number: 3272**

**100 West Main Street
Post Office Box 929
Italy, Texas 76651-0929**

**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 **January 12, 2004**. 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**.

The FDIC assigned a Satisfactory rating at the bank's previous CRA evaluation dated June 3, 1999.

First State Bank is a \$12.5 million full-service institution offering a variety of deposit and loan products at its single office location. As required by regulation, performance factors applicable to small banks were reviewed to arrive at an overall rating. These factors are: loan-to-deposit ratio, lending to borrowers of different incomes, lending in the assessment area, geographic distribution of lending, and response to CRA related complaints. Since there were no complaints received since the last evaluation, this factor was not considered in the overall rating. Management did not request a review of its investments and services for consideration of an outstanding rating.

This evaluation is based upon the bank's origination of commercial and consumer loans. The performance relating to commercial loans received greater weight as this product represents the largest percentage of the loan portfolio by dollar volume. Individual conclusions for each performance factor are summarized below. Performance under each test is detailed elsewhere in this evaluation.

- The average loan-to-deposit ratio of 45 percent is considered adequate when compared to similarly situated institutions in the assessment area and the Texas statewide average for banks of this size.
- The bank's lending activities meets standards for lending inside the assessment area. A majority of consumer and commercial lending was inside the assessment area by number and dollar volume.
- First State Bank has established a satisfactory record of lending to borrowers of different incomes and businesses of different sizes. The bank's distribution of commercial loans is reasonable. Extensions of credit to consumer borrowers demonstrate outstanding performance.
- The bank's distribution of loans is reasonable and consistent with the demographic configuration of the assessment area and local competition.

DESCRIPTION OF INSTITUTION

First State Bank's office is located in Italy, Texas, approximately 45 miles south of Dallas along Interstate Highway 35. The bank is a wholly owned subsidiary of First FSB Bancshares, Inc., a two-bank holding company. The bank offers a variety of deposit and loan products. Lobby hours are reasonable, with extended hours on Friday.

The bank has a balanced portfolio. As of the September 30, 2003, Report of Condition and Income, the bank reported \$12,504 in total assets, 48 percent of which are loans. There are no financial impediments or legal or statutory constraints that would prevent the bank from meeting the credit needs of the assessment area. The bank's current legal lending limit is \$ 250,000.

Table 1 illustrates the components of the loan portfolio by dollar amount and as a percentage of total loans.

Table 1 - Loan Distribution as of 09/30/2003		
Loan Type	Dollar Amount (000s)	Percent of Total Loans (%)
Construction and Land Development	1,190	19.8
Secured by Farmland	141	2.4
1-4 Family Residential	1,487	24.8
Multi-Family (5 or more) Residential	0	0
Commercial	594	9.9
Total Real Estate Loans	3,412	56.9
Commercial and Industrial	1,226	20.4
Agricultural	73	1.2
Consumer	1,280	21.4
Other	6	.1
Less: Unearned Income	0	0
Total Loans	5,997	100

DESCRIPTION OF ASSESSMENT AREA

First State Bank has defined its assessment area as eleven census tracts in Ellis County. Of the eleven tracts two are upper- income (tracts 602.05 and 602.03), eight middle-income (tracts 603, 605, 606, 609,610,611,612, and 613), and one moderate (tract 604). First State Bank’s office is located in census tract 610. The tract lies in the southernmost boarder of Ellis County. The primary population centers are Italy, Waxahachie, Forreston, Avalon, and Milford. The assessment area is part of the Dallas Metropolitan Statistical Area (MSA).

According to the 2000 Census data, the population for the assessment area is 49,677. There are 16,634 households in the assessment area. *Table 2* presents additional 2000 Census demographic data.

Table 2 – Demographic & Economic Characteristics of the Assessment Area	
<u>Dallas MSA Median Family Income:</u>	
2002 Median Family Income	\$66,500
*2003 Estimated Median Family Income	\$65,000
<u>Percentage of Households by Income Level of Household:</u>	
Low-Income	21.0
Moderate-Income	15.8
Middle-Income	21.7
Upper-Income	41.5
<u>Percentage of Total Housing Units:</u>	
1-4 Family Residential	81.48
Multi-Family	6.31
Mobile Home or Trailer	12.07
Other	.14
Owner-Occupied Housing Units	70.89
Rental Housing Units	22.97
Vacant Housing Units	6.14
<u>Median Housing Characteristics:</u>	
Median Age in Years	21
Median Home Value	\$93,696
Median Gross Rent	\$583
<u>**Percentage of Businesses by Gross Annual Revenues:</u>	
≤ \$1 million	65.67
> \$1 million	4.69
Revenues Not Reported	29.64

Source - 2000 U.S. Census

**This figure is based on estimates from the Department of Housing and Urban Development (HUD).*

***2003 Business Geodemographic Data. May not total 100% due to rounding.*

The area’s largest employers are: Italy ISD, Kimberly Clark, Monolithic Construction, and the City of Italy.

A community contact indicated the town of Italy consists of an array of low- to upper- income families. The interviewee added both institutions in town are involved in local activities and help meet the credit needs of the community. The interviewee also indicated that the town of Italy needs low-income housing.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

Scope of Test

The bank's lending performance was evaluated using loan originations in the 24-month period from January 1, 2002, through December 31, 2003. *Table 3* stratifies these originations by loan types.

Table 3 – Loan Originations				
Loan Type	Dollar Amount	Percent	Number of Loans	Percent
Construction	2,188,570	29	15	5
1-4 Family	1,092,984	15	17	6
Commercial	2,497,247	34	48	16
Consumer	1,450,583	19	211	70
Agriculture	225,397	3	9	3
Total	7,454,781	100	300	100

There were an insufficient number of loans for a meaningful analysis of construction, residential, or agricultural lending. As such, consumer and commercial loans were sampled. During the evaluation period, the bank originated or purchased 300 loans, of which 211 were for consumer and 49 for commercial purposes. The analysis of *Lending in the Assessment Area* included all commercial and consumer loans originated during the period reviewed. For the analysis of *Lending to Borrowers of Different Incomes* and the *Geographic Distribution of Loans*, a randomly chosen sample of 44 consumer loans originated within the assessment area totaling \$276,459 was chosen for review. All commercial loans within the assessment area totaling \$840,456 were used for the analysis of *Lending to Borrowers of Different Incomes* and the *Geographic Distribution of Loans*.

Loan-to-Deposit Ratio

First State Bank's loan-to-deposit ratio is satisfactory. The loan-to-deposit ratio (LTD) is a means of measuring a bank's lending activity by comparing it to the volume of deposits held. *Table 4* presents a summary of LTD ratios for this institution and seven comparable banks serving the same general area and offering similar products. The banks are listed in alphabetical order by headquarters location, and no ranking is expressed or implied.

Table 4 – Comparison to Similarly Situated Banks					
Bank Name	City/County	Total Assets (000s)	Total Loans (000s)	Loan-to-Deposit Ratio	Average Loan-to-Deposit Ratio
First Bank & Trust Company	Dawson/Navarro	22,183	12,175	58.89	68.70
First State Bank	Grandview/Johnson	54,981	34,387	69.04	67.37
<i>First State Bank</i>	<i>Italy/Ellis</i>	<i>12,504</i>	<i>5,941</i>	<i>52.10</i>	<i>45.38</i>
First State Bank	Maypearl/Ellis	21,278	12,149	64.79	64.04
First State Bank	Mount Calm/Hill	15,733	3,993	27.34	27.06
Commercial State Bank	Palmer/ Ellis	49,958	20,595	45.62	47.05
First State Bank	Rice/Navarro	9,646	3,496	41.69	35.93
First National Bank in Whitney	Whitney/Hill	53,068	10,391	22.02	19.13

Source: September 30, 2003 Consolidated Reports of Condition and Income

The bank’s average LTD ratio is comfortably within the parameters of these comparable banks. Over the past eighteen quarters, the LTD ratio has ranged from a low of 38.66 percent in June 30, 1999 to the high of 53.84 percent in June 30, 2001. Based on June 30, 2003 Texas statewide aggregate data, the loan-to-deposit ratio for banks with total assets under \$25 million is 51 percent. First State Bank’s loan-to-deposit ratio for this date was 52 percent.

Overall, the bank’s performance under this factor is considered reasonable when compared to similarly situated institutions in the assessment area and the Texas statewide average for banks of comparable size.

Lending in the Assessment Area

The bank’s performance under this factor is satisfactory.

The analysis of lending in the assessment area takes into consideration the size of the assessment area as well as the size of the bank. *Table 5* illustrates the number and dollar volume of loans originated inside the defined assessment area.

Table 5 - Distribution of Loans Inside and Outside of the Assessment Area										
Loan Category or Type	Number of Loans					Dollars in Loans				
	Inside		Outside		Total	Inside		Outside		Total
	#	%	#	%		\$	%	\$	%	
Consumer	174	82	37	18	211	1,148,227	79	302,356	21	1,450,583
Commercial	27	56	21	44	48	840,456	34	1,656,791	66	2,497,247
Total	201	78	58	22	259	1,988,683	51	1,959,147	49	3,947,830

Source: Bank records

As illustrated in the above table, a majority of commercial and consumer loans, by number and dollar, were originated inside the bank's delineated assessment area. Due to limited local loan demand, the bank purchased eight large commercial loans outside the ir assessment area. This caused the dollar volume of commercial loans to be greater than fifty percent outside the assessment. However, the bank still meets standards for this performance factor.

Lending to Borrowers of Different Incomes and Businesses of Different Sizes

The bank has achieved an overall satisfactory penetration of lending to businesses of different sizes and borrowers of different incomes. This conclusion is based on the reasonable distribution of commercial loans and the excellent lending performance to consumers.

Commercial Loans

Performance under this factor is considered reasonable.

Table 6 illustrates the number and dollar volume of commercial loan originations stratified by loan size.

Table 6 - Distribution of Business Loans by Loan Size				
Loan Size	Number of Loans		Dollars in Loans (000s)	
	#	%	\$	%
\$50,000 or less	22	81.5	258	30.7
\$50,001 - \$99,999	2	7.4	104	12.4
\$100,000 - \$250,000	2	7.4	207	24.6
\$250,001 - \$500,000	1	3.7	271	32.3
TOTAL	27	100	840	100

All commercial loans sampled were originated in amounts less than \$1 million, which is the monetary criterion for a “small business loan.” This analysis supports the bank’s performance relative to serving the needs of small businesses in the assessment area. Of further note, approximately 89 percent of the sample by number was originated at amounts less than \$100 thousand, further substantiating the adequacy of this criterion. Considering the bank’s asset size and legal lending limit, this performance appears reasonable.

Table 7 stratifies the gross annual revenues of the loans reviewed and compares the distribution of loans to the percentage of business within each revenue category. A total of 2027 businesses within the banks assessment area reported revenues.

Table 7- Distribution of Business Loans by Gross Annual Revenues of Business					
Gross Annual Revenues (000s)	Commercial Revenue levels*	Number of Loans		Dollars in Loans (000s)	
	%	#	%	\$	%
\$50,000 or less	22	13	48.2	304	36.2
\$50,001 - \$100,000	25	8	29.6	205	24.4
\$100,001 - \$250,000	28	2	7.4	78	9.3
\$250,001 ≤ \$1Million	18	0	0	0	0
>\$1Million	7	4	14.8	253	30.1
TOTAL	100	27	100	840	100

*2003 Dun & Bradstreet business demographic data

Data provided by Dun & Bradstreet is commonly used for quantifying a bank’s performance for lending to businesses of different sizes. The most recent business data from Dun & Bradstreet indicated that approximately 93 percent of the non-farm businesses in the assessment area generate revenues of less than \$1 million annually. The bank’s lending activity was slightly under the D&B percentage at 85 percent. However, approximately 78 percent of the bank’s lending was to small businesses with revenues under \$100,000, demonstrating the bank’s commitment and focus in serving small businesses.

Consumer Loans

The consumer lending performance is considered strong. Borrower income levels for consumer loans are based upon median family income as established annually by the Department of Housing and Urban Development (HUD). *Table 8* stratifies the 2002 and 2003 median family incomes by borrower income level.

Table 8 - Borrower Income Levels		
Income Level	Percent of Median Family Income	*Dallas MSA Median Family Income: 2002: \$66,500 2003: \$65,000
Low	Less than 50%	2002: Less than \$33,250 2003: Less than \$32,500
Moderate	50% to <80%	2002: \$33,250 – 53,200 2003: \$32,500 – 52,000
Middle	80% to <120%	2002: \$53,200 – 79,800 2003: \$52,000 – 78,000
Upper	120% and over	2002: \$79,800 and greater 2003: \$78,000 and greater

*Department of Housing and Urban Development; *HUD Estimate*

Table 9 reflects the bank's performance with regard to consumer lending to borrowers of different incomes.

Table 9 - Distribution of Consumer Loans by Borrower Income					
Borrower Income Level	% of Total Households*	# of Loans	% of #	\$ of Loans	% of \$
Low	21	31	70.4	143,035	24
Moderate	16	9	20.5	50,767	30
Middle	22	3	6.8	26,519	32
Upper	41	1	2.3	56,138	14
Total	100	44	100	276,459	100

**Source: 2000 Census*

The bank’s level of consumer lending, by number, to both low- and moderate-income borrowers and by dollar volume to moderate-income borrowers considerably exceeds the percentages of low- and moderate-income households within the assessment area. Generally, consumer loan distribution data favors low- and moderate-income borrowers as the middle- and upper-income consumers routinely have access to a greater number of funding sources for this type of small dollar credit. However, the bank’s performance in lending to low- and moderate-income borrowers is at such a high level in relation to the demographic composition of the assessment area that the bank’s performance exceeds standards in lending to borrowers of different income levels.

Overall, the analysis of commercial and consumer lending reflects a satisfactory distribution of loans to businesses of different sizes and borrowers of varying income levels.

Geographic Distribution of Loans

First State Bank’s has exhibited satisfactory performance regarding the geographic distribution of commercial and consumer loans. This performance factor evaluates how a bank's loans are distributed among the various census tract income levels. As expected, the loans sampled were spread throughout the assessment area with a large concentration in and around the town of Italy, where the bank has its main office.

Commercial Loans

Commercial lending performance is considered satisfactory. *Table 10* presents the dispersion of commercial loans among the various tract income levels and compares it to the percentage of businesses in each tract category.

Table 10 – Distribution of Commercial Loans by Income Level of Census Tract						
Tract Income Level	% of Census Tracts	% of Businesses	# of loans	% of Number	\$ Volume (000)	% of Volume
Moderate	9	15	3	11.1	56	6.7
Middle	73	52	23	85.2	733	87.2
Upper	18	33	1	3.7	51	6.1
TOTAL	100	100	27	100	840	100

Source: 2002 Business Geodemographic Data; Bank Records; Percentages may not add to 100 due to rounding

The bank's lending performance in moderate-income census tracts is similar to the percentage of businesses in that category by number. The bank’s performance is slightly less by dollar amount but within reason. The bank's lending is well dispersed among the various tract categories.

Consumer Loans

Consumer lending distribution is considered reasonable. *Table 11* illustrates the dispersion of 44 consumer loans among the various census tract categories and compares the distribution of loans to the percentage of households.

Table 11 – Distribution of Consumer Loans by Income Level of Census Tract						
Geography Income Level	Number of tracts	% of Households*	# of loans	% of Number	\$ Volume	% of \$ Volume
Moderate	1	7	1	2.3	56,138	20.3
Middle	8	60	42	95.4	215,321	77.9
Upper	2	32	1	2.3	5,000	1.8
Total	11	100%	44	100%	276,459	100%

**Source: 2000 Census*

The table demonstrates an adequate distribution of credit among the geographies. A majority of the lending took place in and around the bank’s location and lending in the census tract furthest from the bank’s office was limited. The assessment area contains one moderate-income census tract fifteen miles north of Italy and is located in Waxahachie. There is a bank and a credit union located within the moderate-income tract and five other financial institutions within two miles. Therefore, it is reasonable that First State Bank originates fewer consumer loans in this geography given the presence of these institutions and the distance from the bank’s location.

Overall, performance for this factor is satisfactory.

Response to Complaints

No CRA-related complaints were received by the institution since the last evaluation.

Compliance with Anti-discrimination Laws and Regulations

No violations of the provisions of anti-discrimination laws and regulations were identified.

GLOSSARY

GEOGRAPHY TERMS

Assessment Area: A geographic area delineated by the bank in accordance with the requirements of the Community Reinvestment Act.

Census Tract: Small subdivisions of metropolitan and other densely populated counties. Census tract boundaries do not cross county lines; however, they may cross the boundaries of metropolitan statistical areas. They usually have between 2,500 and 8,000 persons, and their physical size varies widely depending upon population density. Census tracts are designed to be homogeneous with respect to population characteristics, economic status, and living conditions to allow for statistical comparisons.

Geography: A census tract or block numbering area delineated by the United States Bureau of the Census in the most recent decennial census.

Metropolitan Statistical Area (MSA): One or more metropolitan areas that have economic and social ties.

Non-Metropolitan Area: All areas outside of metropolitan areas. The definition of a non-metropolitan area is not consistent with the definition of rural areas. Urban and rural classifications cut across the other hierarchies; for example, there is generally both urban and rural territory within both metropolitan and non-metropolitan areas.

HOUSING TERMS

Household: Includes all persons occupying a housing unit. Persons not living in households are classified as living in group quarters. In 100 percent tabulations, the count of households always equals the count of occupied housing units.

Housing Unit: Includes a house, an apartment, a mobile home, a group of rooms, or a single room that is occupied as separate living quarters.

Owner-Occupied Units: Includes units occupied by the owner or co-owner, even if the unit has not been fully paid for or is mortgaged.

INCOME TERMS

Median Income: The median income divides the income distribution into two equal parts, one having incomes above the median and the other having incomes below the median.

Area Median Income: The median family income for the MSA, if a person or geography is located in an MSA; or the statewide non-metropolitan median family income, if a person or geography is located outside an MSA.

Family Income: Includes the income of all members of a family that are age 15 and older.

Household Income: Includes the income of the householder and All other persons that are age 15 and older in the household, whether related to the householder or not. Because many households consist of only one person, median household is usually less than median family income.

Low-Income: Individual income that is less than 40 percent of the area median income, or a median family income that is less than 50 percent in the case of a geography.

Moderate-income: Individual income that is at least 50 percent and less than 80 percent of the area median income, or a median family income that is at least 50 percent and less than 80 percent in the case of a geography.

Middle-income: Individual income that is at least 80 percent and less than 120 percent of the area median income, or a median family income that is at least 80 percent and less than 120 percent in the case of a geography

Upper-income: Individual income that is more than 120 percent of the area median income, or a median family income that is more than 120 percent in the case of a geography.

HUD Adjusted Income Data: The U.S. Department of Housing and Urban Development (HUD) issues annual estimates that update median family income from the metropolitan and non-metropolitan areas. HUD starts with the most recent U.S. Census data and factors in information from other sources to arrive at an annual estimate that more closely reflects current economic conditions.

OTHER TERMS

Family: A family includes a householder and one or more other people living in the same household who are related to the householder by birth, marriage, or adoption. A household can only contain one family for purposes of census tabulations. Not all households contain families since a household may be comprised of a group of unrelated people or of one person living alone.

Household: A household includes all the people who occupy a housing unit. A housing unit is a house, an apartment, a mobile home, a group of rooms, or a single room occupied as separate living quarters (or if vacant, intended for occupancy). The occupants may be a single family, one person living alone, two or more families living together, or any other group of related or unrelated people who share living quarters.

Small Business Loan: A loan included in “loans to small businesses” as defined in the Consolidated Report of Condition and Income (Call Report). These loans have original amounts of \$1 million or less and are either secured by nonfarm nonresidential properties or are classified as commercial and industrial loans.

Dun & Bradstreet: The Dun & Bradstreet Corporation is a provider of business and financial information drawn from a global database of more than 50 million businesses.