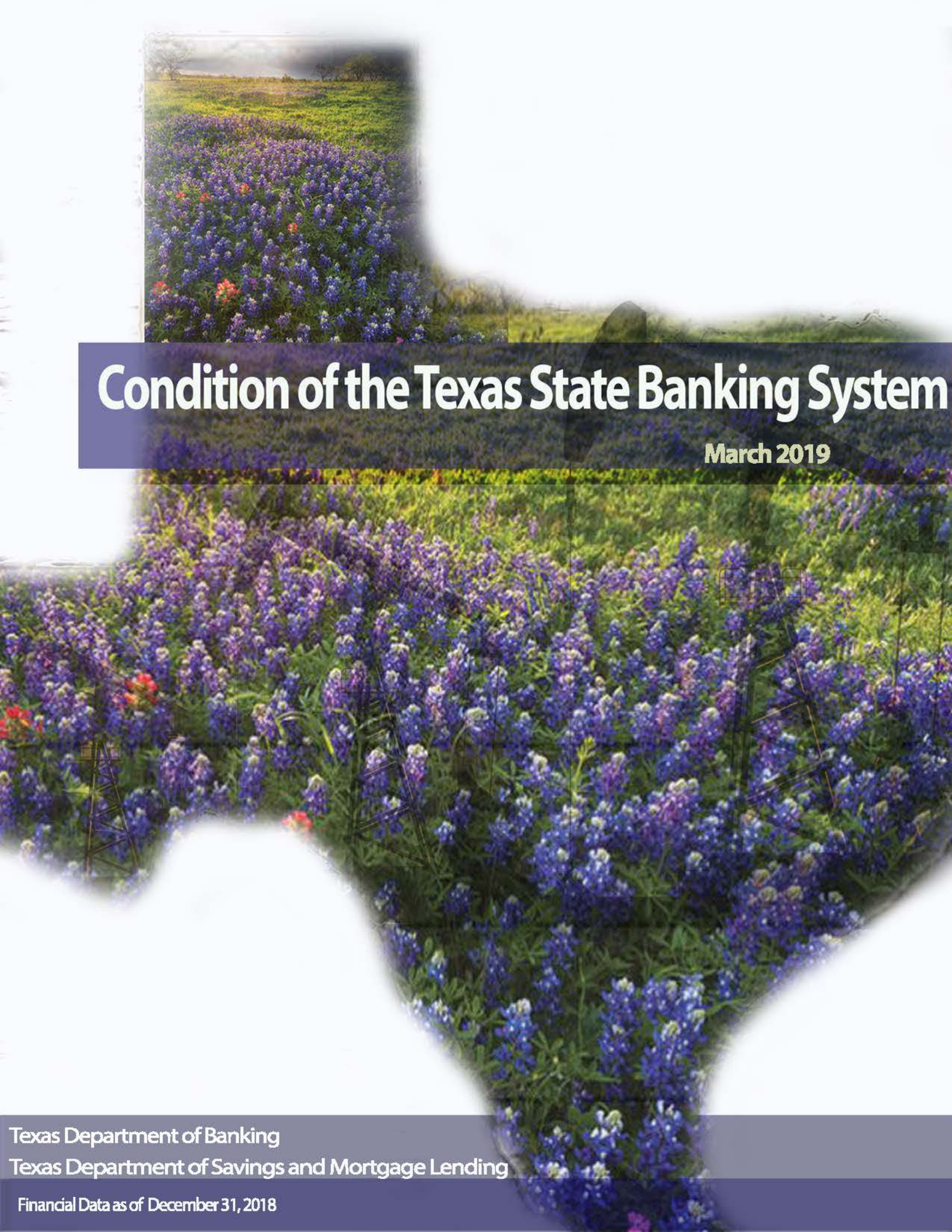




Condition of the Texas State Banking System

March 2019

Texas Department of Banking
Texas Department of Savings and Mortgage Lending

Financial Data as of December 31, 2018



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<u>Symbols Used Throughout this Report:</u>	<u>Abbreviations Used Throughout this Report:</u>
↑ Improving or strong conditions	FDIC – Federal Deposit Insurance Corporation
↓ Deteriorating or weak conditions	OCC – Office of the Comptroller of the Currency
↕ Mixed conditions	FRB – Federal Reserve Board

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This publication is also located on the Texas Finance Commission website: www.fc.texas.gov

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ECONOMIC REVIEW AND OUTLOOK

Despite getting off to a fast start in 2018, the Texas economy began to slow by year's end. The Federal Reserve Bank (FRB) of Dallas reported that the state's economy moderated over the fourth quarter, reflected by a broad-based deceleration across several sectors.

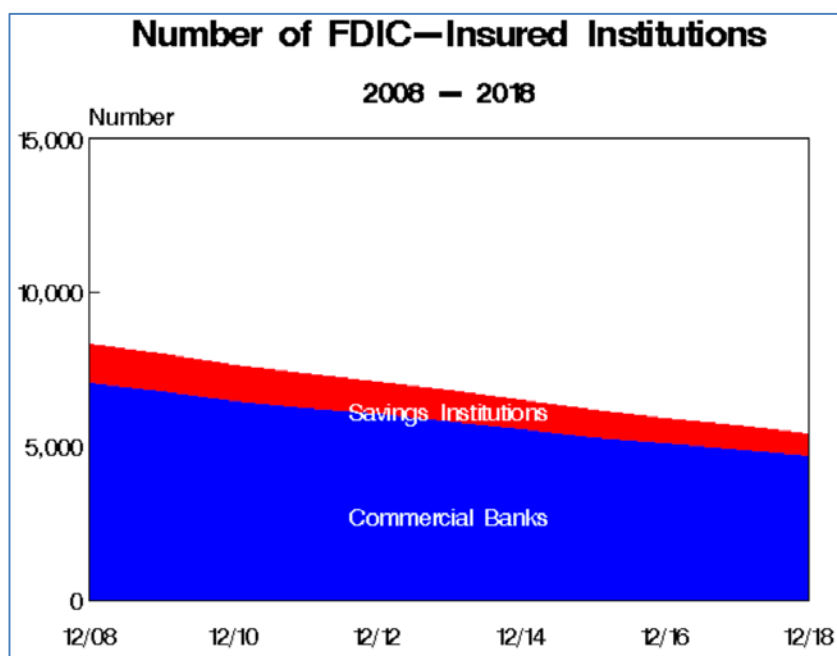
The FRB-Dallas' fourth-quarter Company Outlook Index posted its first negative reading since first-quarter 2016, tumbling 57 points to -10.2. Shifting trade relations, rising interest rates, and softening oil prices all were cited as factors creating a more uncertain lending environment.

In 2018, President Trump imposed a series of tariffs on numerous trading partners and products, including imported steel and aluminum. As the nation's top consumer, Texas imports more than \$8.3 billion in steel and aluminum annually, twice as much as any other state, meaning it could be negatively affected. Tariffs are expected to tighten operating margins and risk job growth in the energy sector, which is dependent on steel for the production, processing, storage, and transportation of oil and gas. Should this occur, the impact could have a ripple effect on the Texas economy.

The Trump administration in 2018 also renegotiated the 25-year old North American Free Trade Act (NAFTA). The U.S., Canada, and Mexico signed an agreement in November to replace NAFTA, creating the United States, Mexico, Canada Agreement (USMCA). Many of the core aspects of NAFTA remain the same; however, the new agreement gives the U.S. greater access to Canadian dairy markets while calling for a larger percentage of parts for automobiles manufactured in Mexico to be made in North America.

Canada and Mexico are crucial trading partners for the U.S., accounting for 34% of exports and over 26% of imports. Texas is the nation's top exporting state – \$315 billion in 2018 – and accounts for 19% of all U.S. exports; approximately one out of every six dollars of U.S. trade originates from Texas, making the new agreement an important milestone for the state.

Bankers are keeping an eye on events in Washington, D.C., as the 2018 mid-term elections brought new leadership to key Congressional committees. Representative Maxine Waters now chairs the House Financial Services Committee who, based on past comments, may provide more aggressive oversight of both Wall Street and the banking industry. There is some concern within the industry that the committee could reverse regulatory relief legislation passed by the House last year.



Source: FDIC

Finally, the national trend of diminishing institutions continued. 2018 ended with 691 FDIC-insured thrifts, down 61 from the previous year, and 4,715 FDIC-insured commercial banks, 203 fewer than at year-end 2017.

STATE-CHARTERED BANKING PROFILE (DEPARTMENT OF BANKING)

There were 233 Texas-chartered banks as of December 31, 2018, four fewer than at June 30, 2018. The net reduction of four in the number of state banks during the second half of 2018 was the result of two banks merging into Texas national banks and two merging into Texas state-chartered banks.

During the same period, the Department processed 141 filings related to banks, with approximately 54% involving office facilities and loan production office activity, 26% involving bank identification and corporate governance issues, 15% involving changes in ownership/control or chartering authority, 3% involving subsidiary formations, and 2% involving foreign bank activity.

Despite the modest decline in the number of Texas state-chartered banks, the overall asset size of Texas state-chartered banks increased from \$257.8 billion as of June 30, 2018, to \$262.4 billion at year-end 2018. The asset growth occurred from a combination of \$2.4 billion in net merger activity and \$2.2 billion of internal asset growth.

STATE-CHARTERED THRIFT PROFILE (DEPARTMENT OF SAVINGS AND MORTGAGE LENDING)

State-chartered thrift assets under the Department's jurisdiction totaled \$24.4 billion as of December 31, 2018, an increase of 7.7% or \$1.7 billion over the prior six months, and 9.3% or \$2 billion from year-end 2017.

Through December 31, 2018, state thrifts had \$286.3 million in year-to-date net income. Increased profitability occurred in 70.8% of the thrift institutions during 2018 due to an increase in the volume of loans at most institutions, while overhead expenses remained at 2.5%. No thrift charters were unprofitable as of December 31, 2018, compared to one unprofitable charter at the end of 2017. Thrifts' net interest margins (NIMs) have recovered slightly since the low of 3.49% in June 2018 to 3.57% in December 2018 due to increases in yields on earning assets. However, noninterest income decreased from a peak of 1.31% of assets in June 2018 to 0.89% of assets in December 2018.

The level of nonperforming loans and other real estate foreclosed remains low in state-chartered thrifts at 1.2% of total assets, which is down from 1.9% in June 2018. Despite these low levels, state and federal regulators continue to closely monitor past due and nonaccrual loans, as well as foreclosed real estate.

The Department continues to receive and process applications, administering eight branch office applications, three merger/reorganization applications, one purchase and assumption application, one change of control application, and nine various other applications during the past 12 months.

TEXAS ECONOMIC PROFILE

The Texas economy continued the expansion it began in early 2018. Third-quarter job growth was strong at 2.7% and fourth-quarter employment remained above the state's long-run trend of 2.5%, but by year's end Texas economic indicators were slowing.

Moderate oil prices (approximately \$50 a barrel), softening global economic activity, and uncertainty over multiple international trade agreements were among the factors leading to the slight deceleration in the economy that began in November.

The FRB-Dallas' Texas Leading Index (a measure of future directional changes in the business cycle) rose 2.6% annually for most of 2018 before declining in November and December due in part to lower oil prices and the declining stock prices of Texas companies.

For the major Metropolitan Statistical Areas (MSAs), the Austin economy continued to outpace the rest of the state, with a positive index of 6.13, followed by Dallas (4.01), Houston (3.96), Fort Worth (3.81), and San Antonio (2.77). Statewide, the FRB-Dallas' Texas Business Cycle Index, which assesses conditions in the state's manufacturing, service, and retail sectors, rose from 3.55 in 2017 to 4.32 by the end of December 2018.

The state's service sector continued to grow in 2018, albeit at a slower pace at year's end, according to the FRB-Dallas' Texas Service Sector Outlook Survey (TSSOS). The service-providing sector increased 2.4%, generating 249,200 jobs statewide. Every subsector expanded except information services.

The TSSOS portrayed that broader economic conditions decreased, as uncertainty increased by the end of the fourth quarter. The general business activity index fell over 16 points to -5.0, its lowest reading since early 2016, while the company outlook index saw a similar decline from 12.0 in November to -4.4 in December.

Retailers' perceptions of broader economic conditions also deteriorated in December. The general business activity index slid into negative territory, dropping 24 points to -16.8. The company outlook index fell from 4.1 in November to -15.6 in December, its weakest reading in nearly 10 years.

Elsewhere, the goods-producing sector added a record high 103,700 jobs in 2018, with mining and manufacturing rebounding after three years of lackluster growth. Manufacturers added 26,600 jobs, most of which occurred in Houston and North Texas; Texas now produces 9% of all U.S. manufactured goods.

Texas factory activity continued to expand rather modestly at year's end, according the FRB-Dallas' Texas Manufacturing Outlook Survey (TMOS). The production index, a key measure of state manufacturing conditions, inched down one point to 7.3.

Respondents to the TMOS, however, indicated perceptions of broader business conditions among business executives turned negative in December; the general business activity index dropped 23 points to -5.1, hitting its lowest level since mid-2016.

Texas' construction industry enjoyed a positive year, creating 44,300 new jobs; however, momentum tapered off in the fourth quarter to more typical levels. The total value of construction leveled off at \$60.6 trillion as the commercial sector pulled back after multiple years of strong growth.

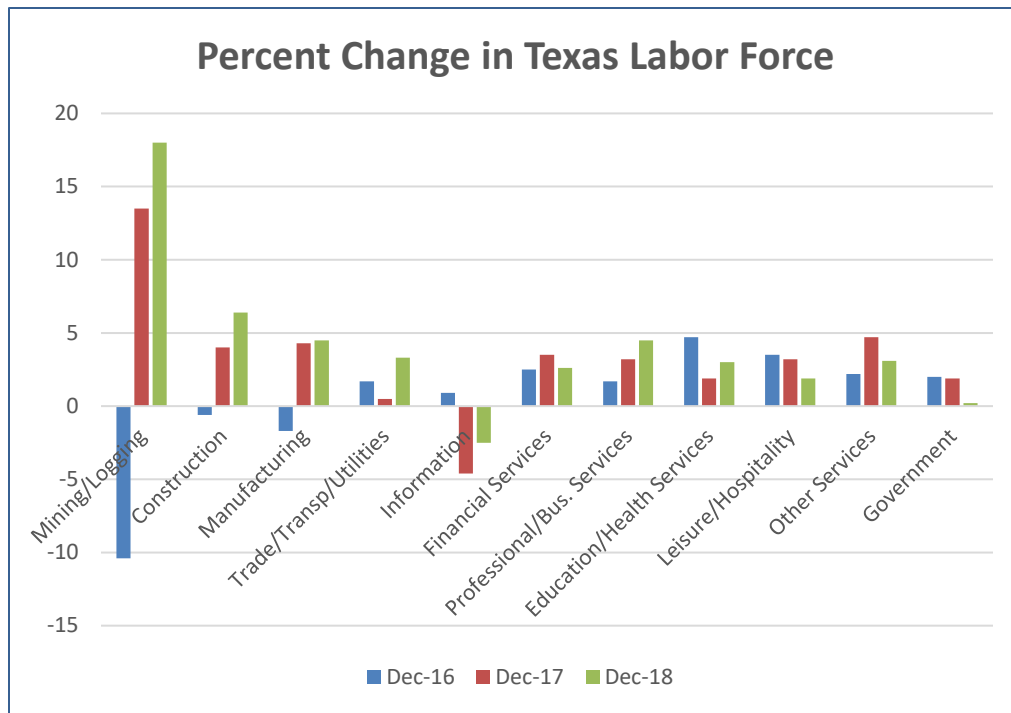
The state's robust economy for most of 2018 helped Texas absorb most of the economic shock of Hurricane Harvey; spending to rebuild after the 2017 disaster resulted in a projected \$800 million gain in economic activity, according to the Texas Comptroller of Public Accounts. An additional \$625 million in disaster recovery funds was allocated to Texas as recently as February 2019 from the U.S. Department of Housing and Urban Development.

EMPLOYMENT

Texas continued its standing in 2018 as the state for job seekers, ending the fourth quarter at historically low unemployment rates for a third straight month.

All Texas metro areas except for Victoria and Beaumont-Port Arthur had more jobs in December 2018 than in December 2017. Midland, in the heart of the Permian Basin oilfield, ranked first in job creation, followed by the Houston, Sherman-Denison, Dallas, and Austin MSAs.

The state's seasonally adjusted unemployment rate in December was 3.7% and remained at the same historic 43-year low since October 2018. However, state job growth was slower at year's end compared with the first half of the year.



Source: U.S. Bureau of Labor Statistics

Texas also ended 2018 experiencing its 29th consecutive month of employment growth, gaining 391,800 nonagricultural jobs from December to December, an annual growth rate of 3.2%, higher than the nation's employment growth rate of 1.8%. This marked 104 consecutive months of annual growth.

Over the year, Texas' nonfarm employment reached a new high of 12,744,100. Of this figure, the highest percentage of employment by industry was in the trade industry, followed by the

government sector, professional and business services, education and health services, leisure and hospitality, and manufacturing.

Total employment in the private sector equaled 10,798,400 jobs at the end of 2018, an increase of 388,800 from the previous year, representing a 3.6% rise in employment.

Despite this, the Texas economy experienced a slight deceleration in job growth in the fourth quarter. Texas employers added jobs at a moderate 2.5% pace in the fourth quarter, a rate slightly slower than the third-quarter growth of 2.7%. The state nevertheless still managed to outpace the rest of the country in terms of job growth, increasing wage pressures and making it harder for many employers to find well-qualified labor.

Entering the fourth quarter of 2018, eight Texas MSAs had an unemployment rate *below* 3%: Amarillo (2.4%), Austin-Round Rock (2.6%), Bryan-College Station (2.5%), Lubbock (2.6%), Midland (2.4%), San Angelo (2.9%), San Antonio-New Braunfels (2.9%), and Sherman-Denison (2.9%).

No one wishes for higher levels of unemployment, but low unemployment has its drawbacks; labor shortages, especially in the housing, oil and gas, and construction industries began to affect portions of the state's economy by year's end.

Nevertheless, the state was awarded *Site Selection Magazine's* Governor's Cup Award in March 2019 for a record-breaking seventh year in a row. The award, which highlights top-performing states for job creation, capital investment, and business innovation, was the 15th overall win for Texas, more than any other state.

POPULATION

With five MSAs with populations greater than 2 million, Texas has more large cities per capita than most states. Dallas–Fort Worth and Houston rank among the top six largest metropolitan areas in the country in terms of both population and economic output.

In fact, Texas is the only state to have two major metros in the top 10 in both categories. The state is also home to three of the nation's top 10 MSAs with the largest increases in population since the 2010 Census: Dallas-Fort Worth-Arlington, Houston-The Woodlands-Sugar Land, and Austin-Round Rock.

The state is now home to an estimated 28.7 million residents. Approximately 72% of these reside in the state's largest metropolitan areas, a proportion which has been rising over time. The long-term forecast from the Waco-based The Perryman Group projects that through 2045, over 80% of new jobs will be created in one of the seven largest MSAs in Texas.

When examining where this growth originates, the full answer depends on the locality in question: Texas suburbs or its large urban centers.

Demographers examine two types of migration: domestic and international. Today, domestic migration in Texas occurs primarily as the result of households moving into the suburbs and out of big cities, or from other parts of Texas and the U.S. Examples include New Braunfels, Conroe, Cedar Park, or McKinney, all of which have experienced explosive growth since the 2010 Census.

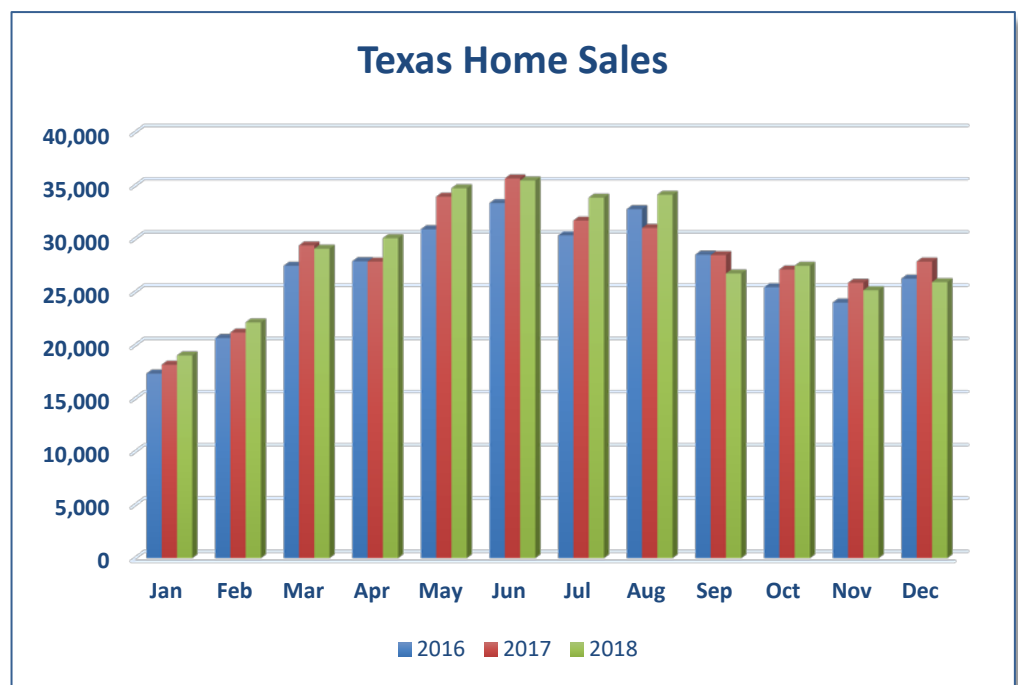
California represents a significant percentage of households moving to Texas from another state. More than 63,000 Californians left home in 2017 headed for Texas, according to the most recent U.S. Census Bureau's American Community Survey figures.

The state's urban cores, on the other hand, are seeing more growth through international migration. Houston and Dallas in particular are growing due in part to migration from Mexico, El Salvador, Honduras, and increasingly China, India, and Africa.

HOUSING

After an extended period of growth fueled by low mortgage rates, the availability of cheap land, and a plentiful labor supply, the Texas housing market began slowing in the fourth quarter of 2018.

Despite a record 343,833 homes sold through Multiple Listing Services in 2018, the rate of increase decreased from 4.1% during the previous year to just 1.7%. Home sales in 2017 exceeded sales in 2018 in five of 12 months.



Source: Real Estate Center at Texas A&M University

This slowdown was matched by a drop in home construction that began in the second half of 2018. Single-family housing permits fell off sharply at the beginning of the fourth quarter, as builders began reporting numerous factors affecting home affordability, including higher land, labor, and construction costs.

A shortage of land and labor has led to a constricted housing supply. As a result of these market forces – coupled with rising mortgage rates – the state's housing affordability continued a steady decline at year's end that can be traced as far back as 2013.

In fact, home prices hit record highs in 2018. The median home price in Austin topped the \$300,000 plateau in November at an average of \$308,153. Austin was followed by Dallas (median price: \$288,338), Houston (median price: \$238,039), and Fort Worth (median price: \$233,235).

The Texas Real Estate Center's Housing Affordability Index fell as a result to 1.4, indicating that a household earning the median income could afford a home 40% more than the median sale price. By comparison, for much of the past decade Texans enjoyed the luxury of affording homes priced twice that of the median.

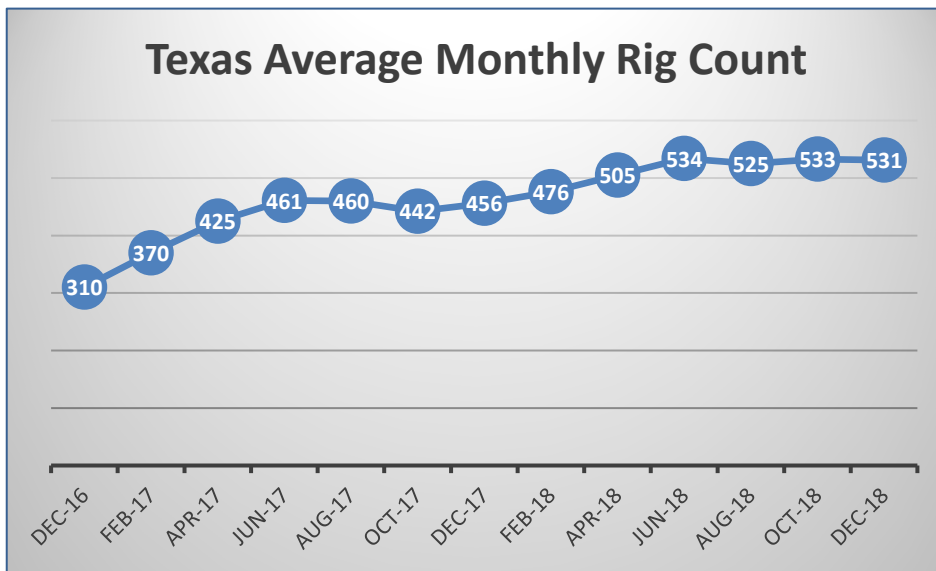
Analysts expect slowing economic and employment growth, combining with affordability issues and increasing mortgage interest rates, will cause housing sales activity to continue to soften. Price pressures are projected to ease as housing sales weaken and homebuilders struggle to increase production in the important entry and first move-up markets.

OIL AND GAS

Texas oil production continued to set new records in 2018, as the state solidified its position as the nation's largest producer of oil and natural gas. The state's oil and gas (O&G) industry saw record highs in production, hitting figures above 4.8 million barrels per day in November. Texas is home to approximately 30% of U.S. refinery capacity and 75% of U.S. petrochemical production.

Permian Basin oil production reached approximately 3.7 million barrels per day in December, while Eagle Ford production figures were roughly 1.4 million barrels per day.

Despite increases in production, lower oil prices, a strong dollar, tariffs on steel, higher interest rates, and labor constraints increased uncertainty within the industry by year's end.



Source: Baker Hughes

Oil prices continued a steep slide in December that began in October, as concerns that slowing global growth could further dampen demand for crude outweighed production cuts by the Organization of the Petroleum Exporting Countries. West Texas Intermediate futures, the U.S. standard, were down nearly 6% from October, closing at \$45.41 a barrel on December 31, 2018.

This represents the first annual decline in oil prices since 2015. In fact, the price of oil was down more

than 20% from its opening 2018 price of about \$60 a barrel and 40% from its peak of \$76.41 in October.

The state's oil rig count flattened out in December at 531 after reaching a 2018 high of 534 in June, and significantly short of the 932 rigs seen in June 2012. The FRB-Dallas traces this dip in part to pipeline constraints resulting from tariffs President Trump placed on foreign steel, as well as transportation bottlenecks in far West Texas.

Since a new series of U.S. tariffs were imposed in July, Texas businesses have paid an extra \$1.1 billion in import fees, according to the Washington, D.C.-based The Trade Partnership, impacting the energy sector disproportionately. Of those extra costs, steel tariffs have accounted for \$629 million (60% of total cost), making new pipelines both more difficult and expensive to develop.

O&G drilling companies, as a result, increased the number of drilled but uncompleted (DUC) wells which are waiting to be hydraulically fractured, or fracked, to begin production. There are more than 3,800 DUC wells in the Permian Basin, approximately 44% of all DUC wells in the entire country.

As a consequence of this uncertainty, more than a third of O&G respondents to a recent FRB-Dallas survey expect general business activity to worsen in the first quarter of 2019.

AGRIBUSINESS

The potential negative affect on Texas agriculture resulting from ongoing trade disputes, specifically with China, could be offset to an extent by the new USMCA trade agreement.

Soybeans, a commodity that accounts for approximately \$60 million in Texas each year, were negatively impacted when the U.S. and China exchanged trade tariffs beginning in July 2018. Although the full impact depends on how long the tariffs remain in place, it could be significant; 50% of the U.S. soybean crop is exported, most of it to China, accounting for about \$12 billion in exports last year.

Conversely, the USMCA trade agreement could lessen the impact, due to Texas' role as a major trading partner to our North American neighbors. Nearly 37% of the state's exports go to Mexico (Texas' largest partner) with another 9% heading to Canada, the state's second-largest export market, with the main agricultural exports including cotton, corn, grain and feed, rice, and beef.

Meanwhile, the FRB-Dallas' fourth-quarter agricultural survey indicated conditions were much improved over 2017, when extremely dry or outright drought conditions severely affected Texas agriculture. Ample soil moisture has boosted crop conditions and improved prospects for the agricultural sector. A majority of bankers responding to the survey confirmed improved conditions across most regions. Crop yields have been good in most areas of the state, particularly for corn, milo, wheat, and cotton, although other areas have suffered either from flooding that hit in late 2018 – ironically, given 2017 conditions – or high winds and generally poor weather that affected harvesting.

Demand for agricultural loans overall declined in late 2018 for a 13th consecutive quarter. Loan renewals and extensions also decelerated, and the rate of loan repayment declined at year's end after plateauing in the third quarter. Loan volume fell across all major categories compared with 2017, with the sharpest declines in dairy, farm machinery, and feeder cattle loans.

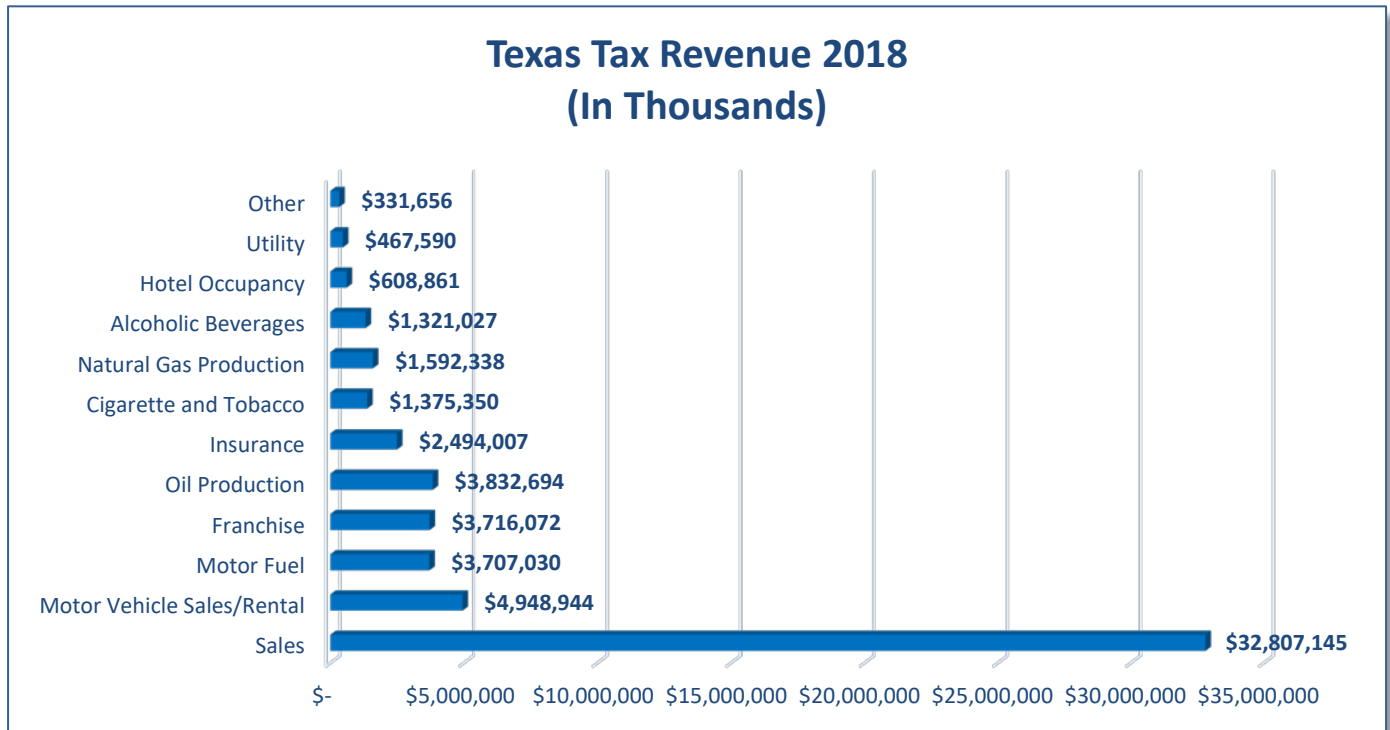
TAX REVENUE

Sales tax receipts for 2018 soared to \$57.2 billion, an 11.6% increase over 2017 totals, thanks to an economy that expanded at a rapid pace for most of the year. All sources of revenue saw an across-the-board increase last year, except for those derived from the sale of cigarettes and tobacco products. Taxes from this category fell 4.2% from slightly more than \$1.4 billion to approximately \$1.3 billion.

This loss was more than offset by significant increases in sales tax revenue (\$32.8 billion, up 9.9%), oil production taxes (\$3.8 billion, up 62.1%), and natural gas production taxes (\$1.5 billion, up 40.1%).

Evidence of last year's robust economy can be found in figures for revenue generated from franchise taxes; receipts from this category increased to \$3.7 billion from \$3.3 billion, a 12% increase. Franchise taxes accounted for 6.5% of all state revenue in 2018, essentially the same as the previous year, even though tax dollars collected from this category actually *decreased* in each of the last four months of 2017.

Sales tax revenue, on the other hand, continued to account for the largest percentage of income for the state, totaling 57.4% of all taxes, followed by motor vehicle sales and rental taxes at 8.7% and oil production taxes, which accounted for 6.7%.



Source: Texas Comptroller of Public Accounts

SUPERVISORY CONCERNS

There are several factors that can affect and challenge the banking industry at any point in time. The Texas Department of Banking and the Texas Department of Savings and Mortgage Lending monitor a variety of risk areas giving each department the ability to proactively provide guidance to regulated entities or to implement other supervisory action as warranted.

Executives of state-chartered banks receive a survey from the Department of Banking on a quarterly basis. One question requests the bankers to rank the greatest risks facing their bank today. The top risks identified in the fourth-quarter survey closely mirror those of regulators.

CYBERSECURITY RISK

At the top of the list is cybersecurity – for both bankers and regulators.

The financial services industry is a primary target for cyberattacks. Cyber criminals look to profit from their attacks and therefore focus on financial institutions and other entities that hold valuable information that can be used to infiltrate an individual's financial affairs. A report released by Carbon Black and Optiv, two cybersecurity and technology companies, reveals an increase in cyberattacks with criminals becoming more sophisticated and changing their tactics frequently.

Destructive attacks are costly and a major concern for regulators and bankers alike. Bank management and information technology personnel are encouraged to monitor their digital footprint and mitigate their cyber risk by developing a strategy that considers the infrastructure and operations of the bank, its networks, and customers.

The Texas Department of Banking and Texas Department of Savings and Mortgage Lending have been assessing financial institutions cyber risk profiles and cybersecurity maturity levels since January 2016.

But state regulators are not the only ones concerned with cybersecurity. Federal Reserve Chairman Jerome Powell spoke on Capitol Hill in late February 2019 and was questioned about the Fed's actions to review cybersecurity efforts at community banks. The Chairman stated that cybersecurity table top exercises are one way that an entity can assess the preparedness of its personnel and financial institution. Exercises to help test an institution's preparedness are available from various sources, including the Financial Services-Information Sharing and Analysis Center (FS-ISAC), FDIC, the Conference of State Bank Supervisors (CSBS) and the Center for Internet Security (CIS).

COMPETITION FOR DEPOSITS AND ACCESS TO LIQUIDITY

Regulators recognize that competition for new customers, low-cost deposit accounts, and quality loans is intense. Moreover, they recognize that deposit accounts are the primary source of funds for both liquidity and lending in community banks. Community banks who struggle to attract deposits, can face challenges when it comes to funding loans. Although many banks continue to contain deposit costs while benefiting from higher yields on both loans and investment securities, bank management should evaluate their strategy for attracting deposits. This increased level of competition requires Texas bankers to exercise higher levels of diligence in all banking activities to ensure prudent decisions are being made.

As competition for deposits rises, financial institutions will be forced to raise their rates which will affect borrowers looking for credit in order to maintain their net interest margins. In the search for more customers, larger financial institutions may employ the strategy of seeking customers in rural areas that are considered deposit-rich. Smaller institutions may be impacted as they may not be accustomed to competition in their rural communities.

Liquidity management is a concern for financial institutions overly reliant on non-core and wholesale funding sources. These funding sources are generally more expensive and less stable than insured core deposits. Further, these funding sources may be difficult or costlier to replace, especially if the institution becomes less than well-capitalized. A well-managed institution with a prudent asset-liability management program and strong risk management, monitoring, and controls can successfully integrate these funding sources and borrowings into their liquidity and funding strategy. However, having a concentrated amount of non-core funds can be problematic and lead to liquidity issues if not properly planned and managed.

GENERAL

There have been efforts to change and reduce regulatory burden for community banks, including a new community bank leverage ratio, a proposal to raise the value threshold for a mandatory mortgage appraisal, and an exemption from the Volcker Rule for community banks. However, the effects of these changes are yet known.

Smaller institutions remain well-capitalized; however, bank management and regulators need to continue to monitor credit concentrations in commercial real estate and agricultural lending. It is imperative that bank management actively manage concentrations of credit risk and be aware that strong lending activity can strain liquidity.

Finally, the implementation of the Current Expected Credit Loss (CECL) standard proposed by the Financial Accounting Standards Board is looming over community banks and regulators. This standard is a significant accounting change for the financial services industry. By requiring financial institutions to account for the expected lifetime losses of a loan at the time of origination, CECL may lead to the disruption of some lending services, especially for smaller community banks who cannot absorb the additional cost of implementation. Both departments are monitoring the industry's transition into this new accounting standard.

DEPARTMENTAL SUPERVISORY MEASURES BEING TAKEN

The supervisory practices of the agencies are designed to identify trends in the industry, and practices of individual banks that could threaten the safety and soundness of an institution or the industry. Each department is sensitive to any economic challenge or natural disasters that may lie ahead. It is imperative to identify individual banks that demonstrate difficulty as soon as possible. The supervisory measures of each department are designed to identify potential risks that could impact an institution's financial condition. Actions taken to mitigate or eliminate these risks include the following:

TEXAS DEPARTMENT OF BANKING

- ❖ Assess institutions' preparedness to identify, detect, respond to, protect against, and recover from cyber-attacks and perform follow-up evaluations for those below a base-line level of readiness;
- ❖ Provide all examination personnel with additional cybersecurity training;
- ❖ Evaluate underwriting criteria during on-site examinations to assess the sensitivity of asset quality metrics to changes in economic conditions;
- ❖ Monitor efforts to prudently assess and mitigate concentration risks in commercial real estate, oil and gas, and agriculture lending;
- ❖ Assess bank liquidity levels, including dependence upon potentially volatile funding sources, funding concentrations, and deposit costs relative to local competition;
- ❖ Assess risks posed by increasing market interest rates on net interest margins, extended durations of investment securities, and economic value of equity;
- ❖ Monitor bank preparations for the industry's pending transition to CECL;
- ❖ Conduct off-site monitoring of institution's key financial performance metrics and analyze exceptions;
- ❖ Initiate enforcement actions early in the detection of deteriorating trends;
- ❖ Conduct frequent on-site examinations or visitations of problem institutions;
- ❖ Communicate and coordinate joint enforcement actions and other supervisory activities with federal regulators;
- ❖ Participate in monthly calls to state banks to obtain industry input regarding prevailing economic conditions;
- ❖ Monitor state, national, and world political and economic events impacting the industry; and
- ❖ Engage and increase internal communication and training to improve examiner awareness of pertinent issues.

DEPARTMENT OF SAVINGS AND MORTGAGE LENDING

- ❖ Close coordination with other state and federal regulators;
- ❖ Engage in regular correspondence with state savings banks regarding institution-specific issues;
- ❖ Engage in regular correspondence with state savings banks as an industry by means such as Emerging Issues monthly calls, and Thrift Industry Day on industry wide issues;
- ❖ Perform targeted examinations of high-risk areas of state savings banks;
- ❖ Issue enforcement actions and placing supervisory agents when deemed necessary;
- ❖ Conduct 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);
- ❖ Develop regular assessments of each institution's activities, strengths, weaknesses, 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 primary federal regulator;
- ❖ Monitor any impact from volatility within the energy industries;
- ❖ Assess interest rate risk;
- ❖ Monitor lending, investment, and funding concentrations;
- ❖ Monitor local, state, national and world political and economic events impacting the industry;
- ❖ Participate in federal compliance examinations of each institution; and
- ❖ Respond promptly to state or national events that can impact the state savings bank industry.

PERFORMANCE SUMMARY AND PROFILE: TEXAS BANKING SYSTEM

STATE-CHARTERED BANKS

Although the Texas banking system lost seven state-chartered banks in 2018, these institutions reported \$3.9 billion in net income at the end of 2018, an increase of \$916 million from year-end 2017. The positive income figure is attributed to an increase in interest revenue, changes in the tax law effectively lowering the tax expense, and lower provisions for loan and lease losses from the previous year.

Collectively, the 233 state banks performed well in 2018, with an average return on assets (ROA) of 1.5%, up from 1.2% a year ago. Commercial state banks with assets greater than \$1 billion are driving the positive ROA, while Texas state-chartered banks with assets less than \$1 billion are facing a slightly lower ROA of 1.4%. NIMs have also improved from the previous year by 28 basis points (BP) ending at 3.7%. Over 83% of financial institutions reported gains at the end of 2018, with less than 3% reporting losses.

The Department of Banking anticipates continued merger and acquisition activity in calendar year 2019. However, this activity has not deterred total assets from rising since year-end 2010, as state banks have generally been the acquiring institution. At year-end 2018, total assets rose by approximately \$3 billion to \$262.4 billion.

Asset quality indicators improved in 2018 with the noncurrent loan rate at 0.6%, an improvement from 0.9% during the same period in 2017. Net charge-offs to loans and leases also declined favorably by 10 BP to 0.2%. Likewise, noncurrent assets plus other real estate owned as a percent of total assets improved by 24 BP to 0.4%.

Loan growth remains strong with total loans increasing by \$6.3 billion to \$165.7 billion. The largest increase occurred in commercial real estate secured by nonfarm nonresidential properties (up \$2.4 billion), which includes loans secured by hotels, motels, dormitories, nursing

homes, assisted-living facilities, mini-storage warehouse facilities, and comparable properties. Banks set aside \$231 million in provisions for loan losses in 2018, a year-over-year decrease of \$85 million. As a result, banks reduced their allowance for loan and lease losses (ALLL) by \$38.8 million compared to December 2017.

Depositors and creditors continue to be well protected by industry capital, as the margin of protection has increased in the last year. The leverage ratio for state-chartered banks increased 50 BP from 10.3% at year-end 2017 to 10.8% in 2018.

As of March 1, 2019, problem state-chartered financial institutions declined, with eleven state banks being classified as a regulatory concern. The Department considers any institution with a Uniform Financial Institutions Composite Rating of 3, 4, or 5 a problem institution.

STATE-CHARTERED THRIFTS

From June 30, 2018, to date, state thrifts had \$115.8 million in net income, compared to \$170.5 million for the first half of 2018. The pretax return on average assets remains strong at 1.7%. From June 30, 2018 to date, non-interest income to assets decreased 42 basis points, while non-interest expense decreased 3 basis points.

The Texas thrift ratio of nonperforming loans plus other real estate owned to total assets has decreased from 1.6% to 1.2% in the last 12 months, and from 2% at June 2018.

State thrifts experienced an increase in the core capital levels compared to one year earlier, from 10.9% to 11.4%, despite the growth in total assets due to strong earnings, capital injections, and lower dividends paid. Total risk-based capital ratios grew 56 basis points from year end 2017 but decreased 78 basis points from June 2018.

NUMBER OF INSTITUTIONS AND TOTAL ASSETS

FDIC financial data is reflective of FDIC insured institutions only.
Assets in Billions

	12-31-2018		12-31-2017		Difference	
	<u>No. of Institutions</u>	<u>Assets</u>	<u>No. of Institutions</u>	<u>Assets</u>	<u>No. of Institutions</u>	<u>Assets</u>
Texas State-Chartered Banks	233	\$262.4	240	\$259.4	-7	+\$3.0
Texas State-Chartered Thrifts	<u>24</u>	<u>\$24.4</u>	<u>25</u>	<u>\$23.1</u>	<u>-1</u>	<u>+\$1.3</u>
	257	\$286.8	265	\$282.5	-8	+\$4.3
Other states' state-chartered:						
Banks operating in Texas*	41	\$69.7	38	\$62.5	+3	+\$7.2
Thrifts operating in Texas*	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
	41	\$69.7	38	\$62.5	+3	+\$7.2
Total State-Chartered Activity	298	\$356.5	303	\$345.0	-5	+\$11.5
National Banks Chartered in Texas	176	\$137.5	183	\$133.3	-7	+\$4.2
Federal Thrifts Chartered in Texas	<u>5</u>	<u>\$83.8</u>	<u>6</u>	<u>\$83.3</u>	<u>-1</u>	<u>+\$0.5</u>
	181	\$221.3	189	\$216.6	-8	+\$4.7
Other states' federally-chartered:						
Banks operating in Texas*	28	\$410.8	24	\$405.7	+4	+\$5.1
Thrifts operating in Texas*	<u>6</u>	<u>\$1.0</u>	<u>6</u>	<u>\$0.3</u>	<u>0</u>	<u>+\$0.7</u>
	34	\$411.8	30	\$406.0	+4	+\$5.8
Total Federally-Chartered Activity	215	\$633.1	219	\$622.6	-4	+\$10.5
Total Banking/Thrift Activity	513	\$989.6	522	\$967.6	-9	+\$22.0

*Indicates estimates based on available FDIC information.

RATIO ANALYSIS

As of December 31, 2018
FDIC financial data is reflective of FDIC insured institutions only.

	<u>State-Chartered Banks</u> 233	<u>Texas National Banks</u> 176	<u>All Texas Banks</u> 409	<u>State-Chartered Thrifts</u> 24	<u>Texas Federal Thrifts</u> 5	<u>All Texas Thrifts</u> 29
% of Unprofitable Institutions	2.58%	2.27%	2.44%	N/A	N/A	N/A
% of Institutions with Earnings Gains	83.26%	79.55%	81.66%	70.83%	80.00%	72.41%
Yield on Earning Assets	4.26%	4.34%	4.29%	4.48%	5.06%	4.94%
Net Interest Margin	3.74%	3.72%	3.73%	3.57%	4.86%	4.59%
Return on Assets	1.52%	1.44%	1.49%	1.23%	1.27%	1.26%
Return on Equity	12.52%	13.46%	12.82%	10.59%	13.45%	12.72%
Net Charge-offs to Loans	0.15%	0.24%	0.18%	0.12%	1.40%	1.08%
Earnings Coverage of Net Loan C/Os	20.62	11.65	16.36	21.77	2.92	3.43
Loss Allowance to Loans	1.09%	1.08%	1.09%	0.78%	1.63%	1.41%
Loss Allowance to Noncurrent Loans	197.97%	151.11%	178.25%	49.35%	114.62%	96.79%
Noncurrent Assets+OREO to Assets	0.42%	0.54%	0.46%	1.15%	0.82%	0.89%
Net Loans and Leases to Core Deps	82.46%	89.85%	84.98%	115.89%	70.78%	78.54%
Equity Capital to Assets	12.39%	10.52%	11.75%	11.78%	9.89%	10.31%
Core Capital (Leverage) Ratio	10.77%	10.44%	10.66%	11.37%	9.99%	10.30%
Common Equity Tier 1 Capital	13.61%	13.58%	13.60%	15.52%	15.08%	15.18%

Data for other state-chartered institutions doing business in Texas is not available and therefore excluded.
Information derived from the FDIC website.

RATIO ANALYSIS BY ASSET GROUPS FOR STATE-CHARTERED BANKS

As of December 31, 2018
FDIC financial data is reflective of FDIC insured institutions only.
Assets in Billions

	<u>< \$1</u> <u>204</u>	<u>\$1 - \$10</u> <u>25</u>	<u>>\$10</u> <u>4</u>
% of Unprofitable Institutions	2.94%	NA	NA
% of Institutions with Earnings Gains	82.84%	84.00%	100.00%
Yield on Earning Assets	4.56%	4.67%	3.94%
Net Interest Margin	3.97%	3.97%	3.54%
Return on Assets	1.36%	1.52%	1.58%
Return on Equity	12.24%	11.28%	13.35%
Net Charge-offs to Loans	0.12%	0.17%	0.15%
Earnings Coverage of Net Loan C/Os	22.17	17.03	22.51
Loss Allowance to Loans	1.20%	0.93%	1.15%
Loss Allowance to Noncurrent Loans	205.25%	186.08%	201.30%
Noncurrent Assets+OREO to Assets	0.44%	0.48%	0.37%
Net Loans and Leases to Core Deps	76.40%	100.59%	76.51%
Equity Capital to Assets	11.16%	14.17%	11.94%
Core Capital (Leverage) Ratio	11.24%	11.76%	10.06%
Common Equity Tier 1 Capital	16.66%	14.47%	12.15%

RATIO ANALYSIS BY ASSET GROUPS FOR STATE-CHARTERED THRIFTS

As of December 31, 2018
FDIC financial data is reflective of FDIC insured institutions only.
Assets in Billions

	<u>< \$1</u> <u>19</u>	<u>\$1 - \$10</u> <u>5</u>	<u>>\$10</u> <u>0</u>
% of Unprofitable Institutions	NA	NA	NA
% of Institutions with Earnings Gains	68.42%	80.00%	NA
Yield on Earning Assets	4.70%	4.40%	NA
Net Interest Margin	3.83%	3.46%	NA
Return on Assets	0.98%	1.33%	NA
Return on Equity	9.93%	10.80%	NA
Net Charge-offs to Loans	0.09%	0.13%	NA
Earnings Coverage of Net Loan C/Os	20.09	22.23	NA
Loss Allowance to Loans	0.96%	0.71%	NA
Loss Allowance to Noncurrent Loans	185.18%	35.98%	NA
Noncurrent Assets+OREO to Assets	0.42%	1.40%	NA
Net Loans and Leases to Core Deps	94.19%	126.79%	NA
Equity Capital to Assets	10.54%	12.22%	NA
Core Capital (Leverage) Ratio	10.58%	11.67%	NA
Common Equity Tier 1 Capital	15.32%	15.59%	NA

COMPARISON REPORT

Select Balance Sheet and Income/Expense Information
FDIC financial data is reflective of FDIC insured institutions only.
December 31, 2018

	State Banks*		State Thrifts	
	<u>End of Period</u>	<u>% of Total Assets</u>	<u>End of Period</u>	<u>% of Total Assets</u>
Number of Institutions	233		24	
Number of Employees (full-time equivalent) (In millions)	41,128		3,231	
Total Assets	\$262,401		\$24,434	
Net Loans and Leases	\$163,843	62.44%	\$16,170	66.18%
Loan Loss Allowance	\$1,812	0.69%	\$127	0.52%
Other Real Estate Owned	\$178	0.07%	\$22	0.09%
Goodwill and Other Intangibles	\$6,070	2.31%	\$305	1.25%
Total Deposits	\$214,662	81.81%	\$17,635	72.17%
Federal Funds Purchased and Repurchase Agreements	\$2,733	1.04%	\$4	0.02%
Other Borrowed Funds	\$9,615	3.66%	\$3,653	14.95%
Equity Capital	\$32,512	12.39%	\$2,878	11.78%
<u>Memoranda:</u>				
Noncurrent Loans and Leases	\$916	0.35%	\$258	1.05%
Earning Assets	\$239,321	91.20%	\$22,568	92.36%
Long-term Assets (5+ years)	\$71,472	27.24%	\$7,652	31.32%
	<u>Year-to-Date</u>	<u>% of Avg. Assets[†]</u>	<u>Year-to-Date</u>	<u>% of Avg. Assets[†]</u>
Total Interest Income	\$10,027	3.89%	\$968	4.16%
Total Interest Expense	\$1,223	0.47%	\$198	0.85%
Net Interest Income	\$8,803	3.41%	\$770	3.31%
Provision for Loan and Lease Losses	\$231	0.09%	\$18	0.08%
Total Noninterest Income	\$2,990	1.16%	\$207	0.89%
Total Noninterest Expense	\$6,904	2.68%	\$577	2.48%
Securities Gains	-\$27	-0.01%	\$0	0.00%
Net Income	\$3,912	1.52%	\$286	1.23%
<u>Memoranda:</u>				
Net Loan Charge-offs	\$237	0.09%	\$18	0.08%
Cash Dividends	\$2,233	0.87%	\$124	0.53%

*Excludes branches of state-chartered banks of other states doing business in Texas. As of December 31, 2018, there are an estimated 39 out-of-state state-chartered institutions with \$65.4 billion in assets. Assets are based upon the June 30, 2017, FDIC Summary of Deposits.

†Income and Expense items as a percentage of average assets are annualized.

No branches of state-chartered thrifts of other states conducted business in Texas as of June 30, 2018.

PERFORMANCE SUMMARY: UNITED STATES BANKING SYSTEM

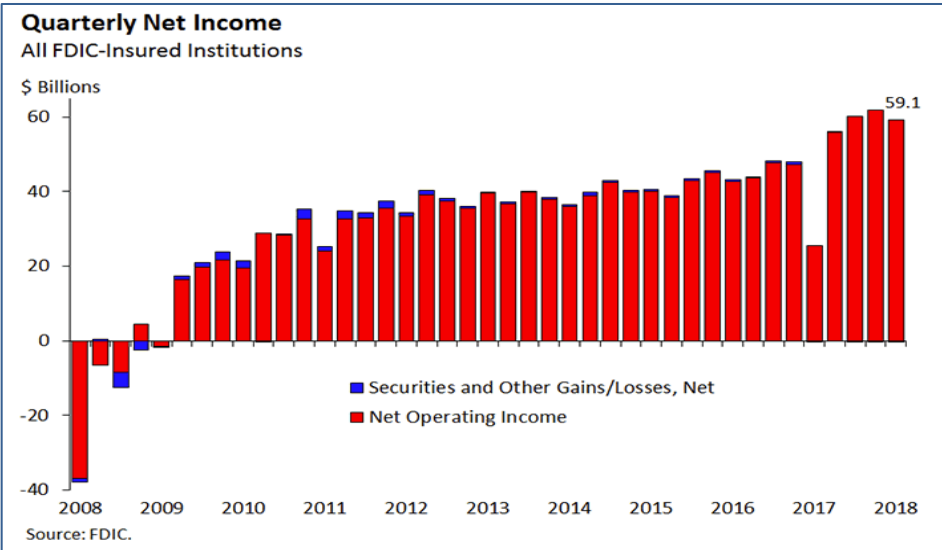
FDIC QUARTERLY BANKING PROFILE

Fourth Quarter 2018 - www.fdic.gov

All Institutions Performance

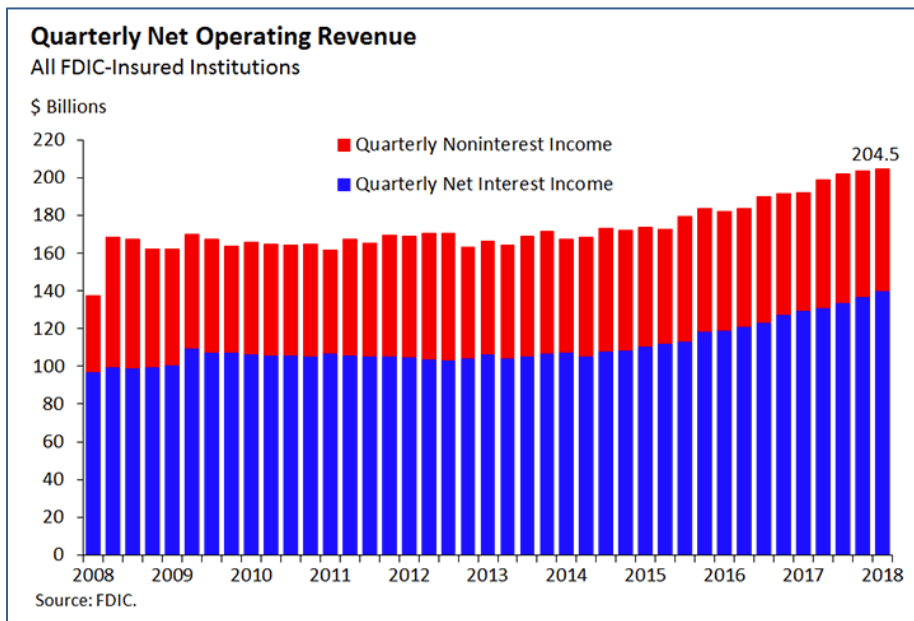
↑ Net Income Rises \$33.8 Billion Over Fourth Quarter 2017 to \$59.1 Billion

The 5,406 FDIC-insured commercial banks and savings institutions reported quarterly net income of \$59.1 billion in the fourth quarter, an increase of \$33.8 billion (133.4%) from a year earlier. Improvement in quarterly net income was attributable to higher net operating revenue (the sum of net interest income and noninterest income) and lower income tax expenses. Assuming the effective tax rate before the new tax law, quarterly net income would have totaled an estimated \$50.3 billion, up \$7.9 billion (18.5%) from 12 months ago. The average return on assets was 1.33% for the quarter, up from 0.58% in fourth quarter 2017. The percentage of unprofitable banks in the fourth quarter declined to 6.5% from 16.6% a year ago.



↑ Full-Year 2018 Net Income Grows to \$236.7 Billion

Growth in net operating revenue (up \$53.1 billion, or 7%), coupled with lower income tax expenses (down \$36.9 billion, or 37.7%) and loan-loss provisions (down \$1.1 billion, or 2.2%), lifted full-year 2018 net income to \$236.7 billion, an improvement of \$72.4 billion (44.1%) from 2017. Assuming the effective tax rate before the new tax law, full-year 2018 net income would have totaled an estimated \$207.9 billion, compared with \$183.1 billion in 2017. The average NIM rose



from 3.25% in 2017 to 3.40%, as average asset yields (up 43 basis points) exceeded average funding costs (up 28 basis points). The average return on assets for 2018 was 1.35%, up from 0.97% for 2017.

↓ Loan-Loss Provisions Increase Modestly

Banks set aside \$14 billion in loan-loss provisions during the fourth quarter, the highest level since fourth quarter 2012. Loan-loss provisions rose by \$397.3 million (2.9%) from fourth quarter 2017, with close to 40% of all banks reporting increases. Loan-loss provisions as a percent of net operating revenue declined from 8.3% at year-end 2017 to 8.2%.

↕ Noninterest Income Expands from a Year Earlier

Noninterest income increased \$1.6 billion (2.6%) from a year earlier, as all other noninterest income grew by \$3.5 billion (11.9%) and net gains on sales of other assets rose by \$393 million (120.3%). Despite the overall increase in noninterest income, trading revenue declined by \$1.5 billion (25.9%) and servicing fees fell by \$850.9 million (36.1%). Slightly more than half of all banks (53.6%) reported increases in noninterest income compared with the year-ago quarter.

↓ Noninterest Expense Increases from Fourth Quarter 2017

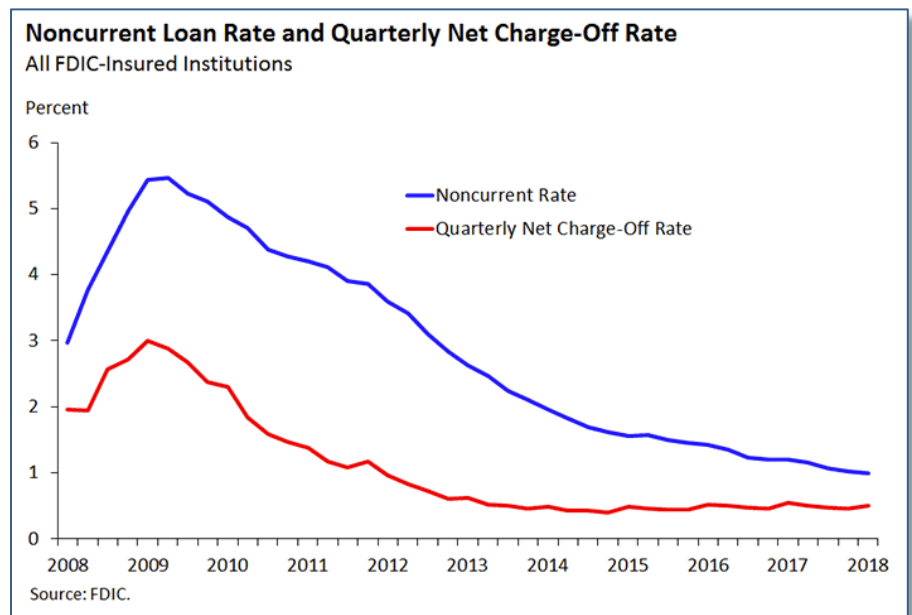
Noninterest expense posted a modest increase of \$194.9 million (0.2%) over the past 12 months. Increases in other noninterest expense (up \$2.6 billion, or 5%) and salary and employee benefits (up \$717 million, or 1.3%) were partially offset by a decline in premises and fixed asset expense (down \$2.7 billion, or 22.5%). The average assets per employee increased from \$8.4 million in fourth quarter 2017 to \$8.7 million.

↑ Net Charge-Offs Decline 4.6 % from a Year Ago

Banks charged off \$12.6 billion in uncollectable loans during the quarter, a decline of \$ 605.9 million (4.6%) from a year ago. This marks the first time since third quarter 2015 that net charge-offs registered a year-over-year decline. Credit card balances registered the largest annual dollar increase in net-charge offs (up \$347.7 million, or 4.4%), while commercial and industrial loans had the largest annual dollar decline (down \$522.6 million, or 23.4%). The average net charge-off rate declined from 0.55% in fourth quarter 2017 to 0.50%.

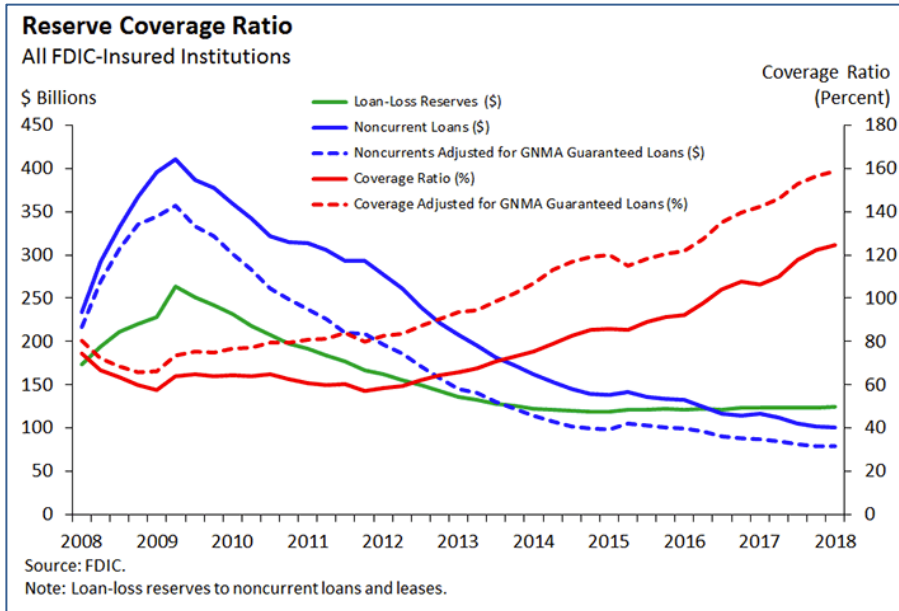
↑ Noncurrent Loan Rate Falls Below 1 Percent

Noncurrent loan balances (90 days or more past due or in nonaccrual status) were \$1 billion (1%) lower than the previous quarter. More than half of all banks (53.3%) reported lower noncurrent loan balances. The quarter-over-quarter decline was reflected in residential mortgages balances, which declined by \$2 billion (4.4%), and commercial and industrial loan balances, which fell by \$554.3 million (3.6%). Credit card balances continued to register the largest quarterly dollar increase, growing by \$1.6 billion (13.8%). The average noncurrent rate was 0.99% during the current quarter, down 3 basis points from the previous quarter. This is the first time since second quarter 2007 that the noncurrent rate was below 1%.



↓ Loan-Loss Reserves Increase from Third Quarter 2018

Loan-loss reserves totaled \$124.7 billion at the end of the fourth quarter, an increase of \$1 billion (0.8%) from third quarter 2018. The banking industry continued to build reserves, as loan-loss provisions of \$14 billion exceeded net charge-offs of \$12.6 billion. More than half of all banks (57.8%) reported a quarterly increase in loan-loss reserves. Banks that itemize their loan-loss reserves (banks with assets greater than \$1 billion and representing 93% of total industry assets) reported higher reserves for credit card losses (up \$997.4 million, or 2.5%) and lower reserves for residential real estate losses (down \$556 million, or 4.4%). After declining for the past nine consecutive quarters, itemized reserves for losses on commercial loans reported quarterly growth of \$409 million (1.3%).



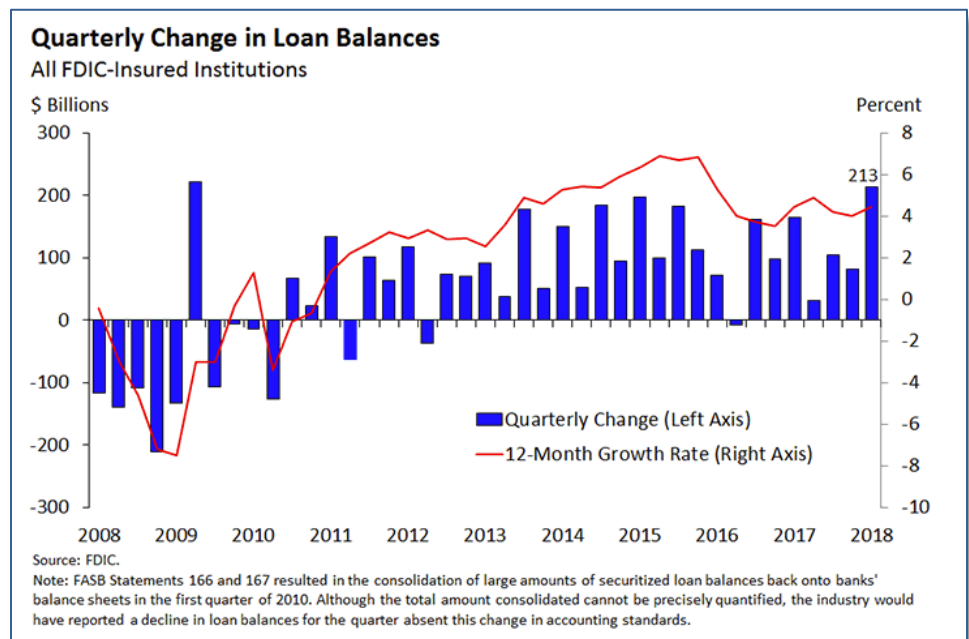
↑ Equity Capital Increases from the Third Quarter

Equity capital increased by \$25.3 billion (1.3%) during the fourth quarter.

Retained earnings rose by \$70.8 billion (10.3%) from a year ago. Declared dividends in the fourth quarter totaled \$52.7 billion, the highest level ever reported by the banking industry. At year-end 2018, 99.6% of all insured institutions, which account for 99.98% of total industry assets, met or exceeded the requirements for the well-capitalized category, as defined for Prompt Corrective Action purposes.

↑ Total Assets Increase 1.5 % During the Fourth Quarter

Total assets rose by \$270.4 billion (1.5%) during the fourth quarter. Cash and balances due from depository institutions declined by \$144.4 billion (7.9%) and total securities holdings grew by \$93 billion (2.6%). U.S. Treasury securities increased \$55.4 billion (11.2%) during the quarter, the largest quarterly dollar increase since fourth quarter 2014.



↑ Total Loan and Lease Balances Rise 4.4 % Over 12 Months

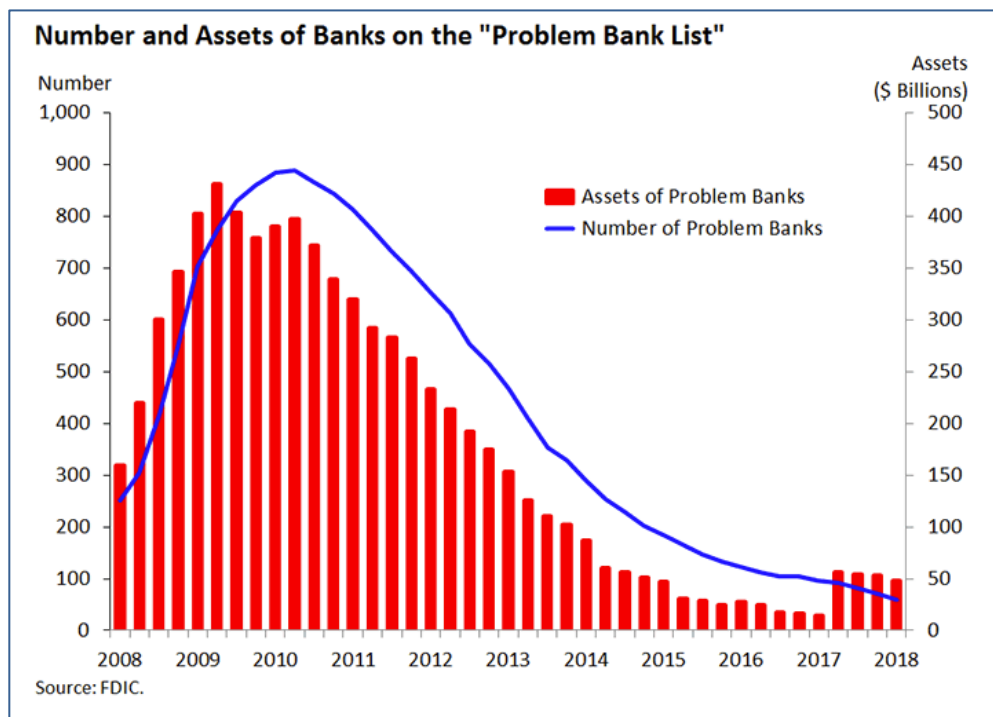
Total loan and lease balances were \$213 billion (2.1%) higher compared with the previous quarter. All major loan categories registered quarterly increases. Commercial and industrial loans increased by \$80.7 billion (3.9%), and consumer loans (including credit card balances) rose by \$52.2 billion (3.1%). During the 12 months ended December 31, total loan and lease balances rose by \$431.2 billion (4.4%), a slight increase from the 4% annual grow rate reported last quarter. All major loan categories reported year-over-year increases, led by commercial and industrial loans, which increased by \$156.2 billion (7.8%), and consumer loans (including credit card balances), which rose by \$64.9 billion (3.9%).

↑ Deposits Increase 2.2 % from the Previous Quarter

Total deposits increased by \$292.6 billion (2.2%) from the third quarter, the largest quarterly dollar increase since fourth quarter 2012. Interest-bearing deposits grew by \$296.5 billion (3.2%), while noninterest-bearing deposits fell by \$ 5.4 billion (0.2%). Reliance on nondeposit liabilities declined by \$47.5 billion (2.3%) from the previous quarter, as trade liabilities were reduced by \$23.1 billion (8.9%) and other liabilities fell by \$24.4 billion (6%).

↑ The Number of Banks on the “Problem Bank List” Declines to 60

The number of banks on the FDIC’s “Problem Bank List” declined from 71 to 60 at year-end 2018, the fewest since first quarter 2007. Total assets of problem banks fell from \$53.3 billion to \$48.5 billion. During the fourth quarter, two new charters were added, 70 institutions were absorbed by mergers, and there were no bank failures. For full-year 2018, eight new charters were added, 259 institutions were absorbed by mergers, and there were no bank failures.



SNAPSHOT STOCK PERFORMANCE

SOUTHWEST REGIONAL BANKS (MSECTOR415)

MARCH 2019

Name	Last Trade	52 Wk Range	PE	EPS	Mkt Cap	Div/Shr	Div Yld
ACNB Corporation	03/11 36.53	28.05 41.45	11.83	3.09	257.398M	0.92	2.49%
BancFirst Corporation	03/11 54.79	48.07 65.70	14.57	3.76	1.787B	1.20	2.20%
BOK Financial Corporation	03/11 86.21	69.96 107.00	13.00	6.63	6.229B	2.00	2.32%
Cass Information Sys, Inc.	03/11 50.17	47.74 62.08	24.72	2.03	728.812M	1.04	2.11%
Commerce Bancshares, Inc.	03/11 60.65	53.40 69.10	16.05	3.78	6.739B	1.04	1.73%
Cullen Frost Bankers, Inc.	03/11 101.45	81.87 121.66	14.68	6.91	6.391B	2.68	2.66%
Enterprise Fin Serv Corp	03/11 43.28	36.09 58.15	11.29	3.83	1.093B	0.56	1.30%
First Community Corp S C	03/11 20.00	17.93 26.25	13.79	1.45	152.67M	0.44	2.17%
First Financial Bankshares, Inc.	03/11 60.54	45.05 66.83	27.27	2.22	4.077B	0.84	1.40%
First Financial Northwest, Inc.	03/11 15.93	13.75 21.81	11.14	1.43	170.207M	0.32	2.12%
Great Southern Bancorp, Inc.	03/11 55.30	43.30 61.65	11.74	4.71	783.584M	1.28	2.35%
Guaranty Fed Bancshares, Inc.	03/11 22.91	20.11 27.39	13.97	1.64	102.258M	0.52	2.27%
Heartland Financial USA, Inc.	03/11 46.32	41.36 46.88	13.16	3.52	1.601B	0.64	1.40%
International Bancshares Corp	03/11 39.86	32.56 47.98	12.30	3.24	2.616B	0.84	2.12%
Landmark Bancorp, Inc.	03/11 24.59	21.00 28.08	10.29	2.39	107.51M	0.80	3.17%
Liberty Bancorp, Inc.	03/11 25.25	22.35 27.00	15.59	1.62	62.077M	0.27	1.07%
Mackinac Financial Corp	03/11 15.61	12.60 17.58	16.61	0.94	167.225M	0.48	3.02%
MidWest One Finl Group, Inc.	03/11 30.22	23.80 35.20	12.19	2.48	367.808M	0.81	2.71%
North Dallas Bank & Trust Co. TX	03/11 84.51	79.55 92.00	34.21	2.47	217.106M	1.00	1.18%
Prosperity Bancshares, Inc.	03/11 73.27	57.01 79.20	15.90	4.61	5.118B	1.64	2.27%
QCR Holdings, Inc.	03/11 34.78	30.15 49.60	12.16	2.86	546.679M	0.24	0.71%
Solera National Bancorp, Inc.	03/11 10.70	8.37 11.40	16.98	0.63	43.481M	N/A	N/A
Texas Capital Bancshares, Inc.	03/11 59.20	47.86 103.05	10.22	5.79	2.975B	N/A	N/A
Two Rivers Fin Group	03/11 32.00	31.00 35.51	13.97	2.29	71.508M	0.64	2.00%
UMB Financial Corporation	03/11 66.57	57.00 82.14	16.96	3.92	3.265B	1.20	1.81%
West Bancorp Incorporated	03/11 21.75	18.06 26.96	12.50	1.74	345.427M	0.80	3.70%

Source: Yahoo Finance (March 2019)

N/A – Indicates information was not available.

SNAPSHOT STOCK PERFORMANCE

SOUTHWEST REGIONAL BANKS (MSECTOR415)

MARCH 2018

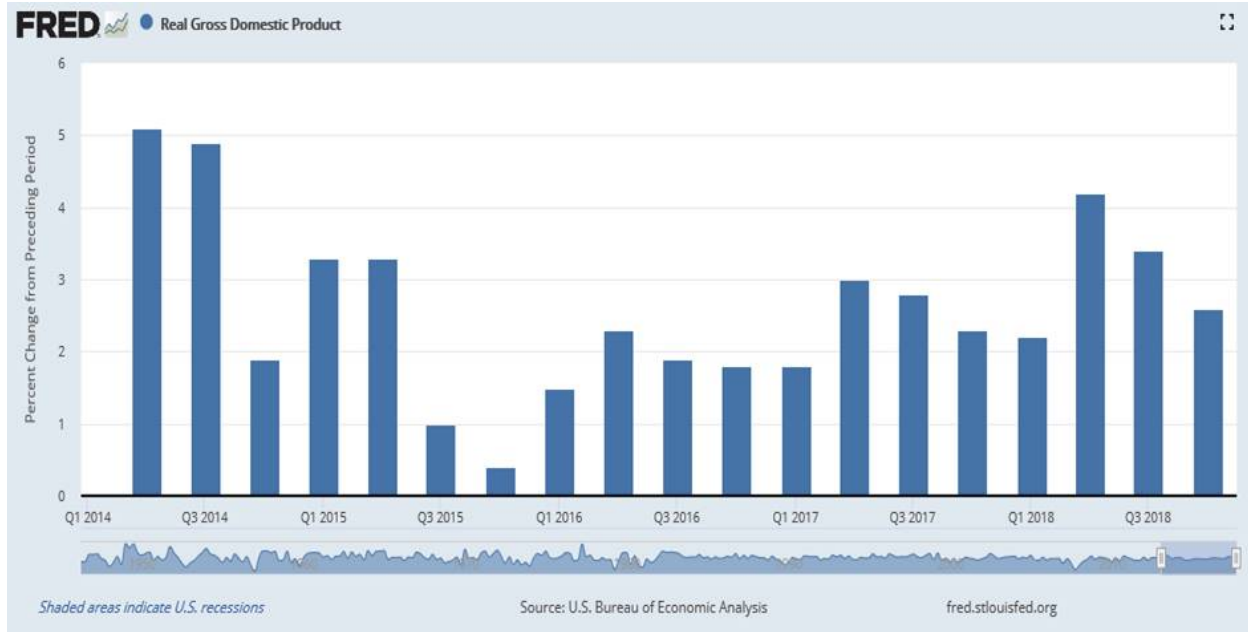
Name	Last Trade	52 Wk Range	PE	EPS	Mkt Cap	Div/Shr	Div Yld
ACNB Corporation	03/09 28.55	24.45 32.50	18.18	1.57	200.38M	0.20	2.80%
BancFirst Corporation	03/09 56.95	48.20 115.80	21.49	2.65	1.86B	0.21	1.44%
BOK Financial Corporation	03/09 99.72	73.44 99.50	19.49	5.11	6.53B	0.45	1.79%
Cass Information Sys, Inc.	03/09 62.30	54.37 69.86	31.00	2.01	765.46M	0.24	1.44%
CoBiz Incorporated	03/09 20.13	15.39 22.01	25.81	0.78	850.06M	0.06	1.07%
Commerce Bancshares, Inc.	03/09 60.79	51.90 60.82	21.03	2.89	6.49B	0.23	1.46%
Cullen Frost Bankers, Inc.	03/09 109.42	81.09 109.69	19.84	5.51	6.96B	0.57	2.09%
Enterprise Fin Serv Corp	03/09 49.40	36.65 49.67	23.86	2.07	1.14B	0.11	0.89%
First Community Corp S C	03/09 22.50	18.50 24.87	21.63	1.04	150.89M	0.10	1.64%
First Financial Bankshares, Inc.	03/09 48.90	36.85 48.85	27.02	1.81	3.30B	0.19	1.56%
First Financial Northwest, Inc.	03/09 16.68	13.13 20.32	19.55	0.85	178.64M	0.07	1.68%
Great Southern Bancorp, Inc.	03/09 51.80	47.25 58.45	14.43	3.59	730.89M	0.24	1.81%
Guaranty Fed Bancshares, Inc.	03/09 22.80	18.21 23.71	16.06	1.42	100.82M	0.12	1.84%
Heartland Financial USA, Inc.	03/09 56.00	42.1 56.40	21.13	2.65	1.74B	0.13	0.82%
International Bancshares Corp	03/09 41.40	32.50 42.45	17.54	2.36	2.74B	0.33	1.59%
Landmark Bancorp, Inc.	03/09 28.76	27.02 32.00	29.60	0.97	117.38M	0.20	2.68%
Liberty Bancorp, Inc.	03/09 23.80	20.05 24.50	39.02	0.61	85.69M	0.07	1.03%
Mackinac Financial Corp	03/09 16.30	13.16 16.80	14.30	1.14	99.58M	0.12	2.94%
MidWest One Finl Group, Inc.	03/09 33.60	30.56 38.00	21.68	1.55	411.10M	0.20	2.08%
North Dallas Bank & Trust Co. TX	03/09 80.25	70.50 80.20	36.16	2.22	206.04M	0.33	0.86%
Prosperity Bancshares, Inc.	03/09 78.24	55.84 79.05	19.99	3.92	5.47B	0.36	1.79%
QCR Holdings, Inc.	03/09 47.55	39.85 50.00	18.57	2.56	661.81M	0.05	0.44%
Solera National Bancorp, Inc.	03/09 8.75	7.40 8.75	NA	NA	23.74M	NA	NA
Texas Capital Bancshares, Inc.	03/09 94.20	69.65 102.90	25.24	3.73	4.67B	NA	NA
UMB Financial Corporation	03/09 77.03	62.37 80.04	20.98	3.67	3.85B	0.28	1.40%
West Bancorp Incorporated	03/09 26.20	20.60 28.00	18.58	1.41	424.85M	0.18	2.75%

Source: Yahoo Finance (March 2018)

N/A – Indicates information was not available.

NATIONAL ECONOMIC TRENDS

Real GDP



Consumer Price Index

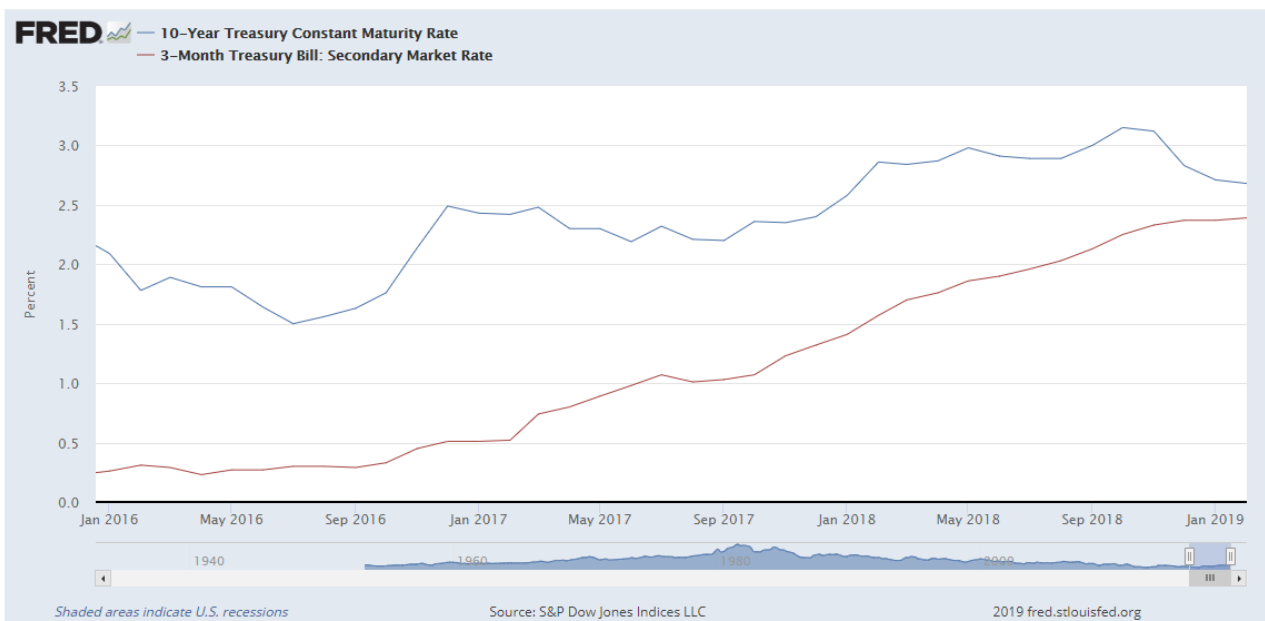


Source: Federal Reserve Bank of St. Louis, National Economic Trends, February 2019.

Unemployment Rate

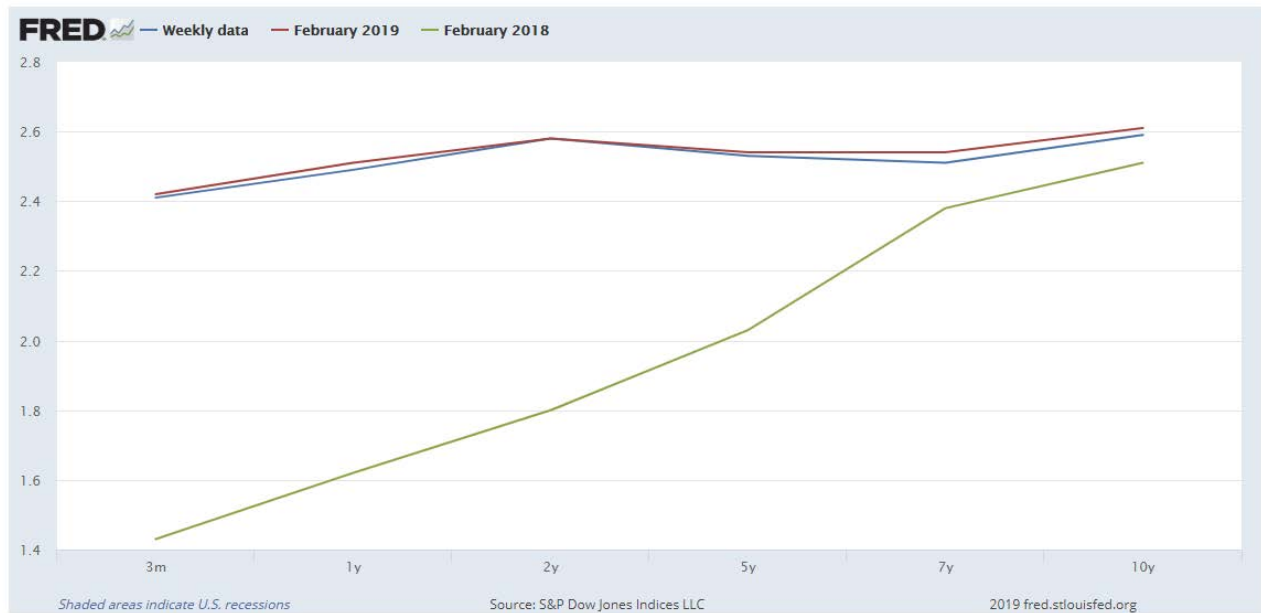


Interest Rates

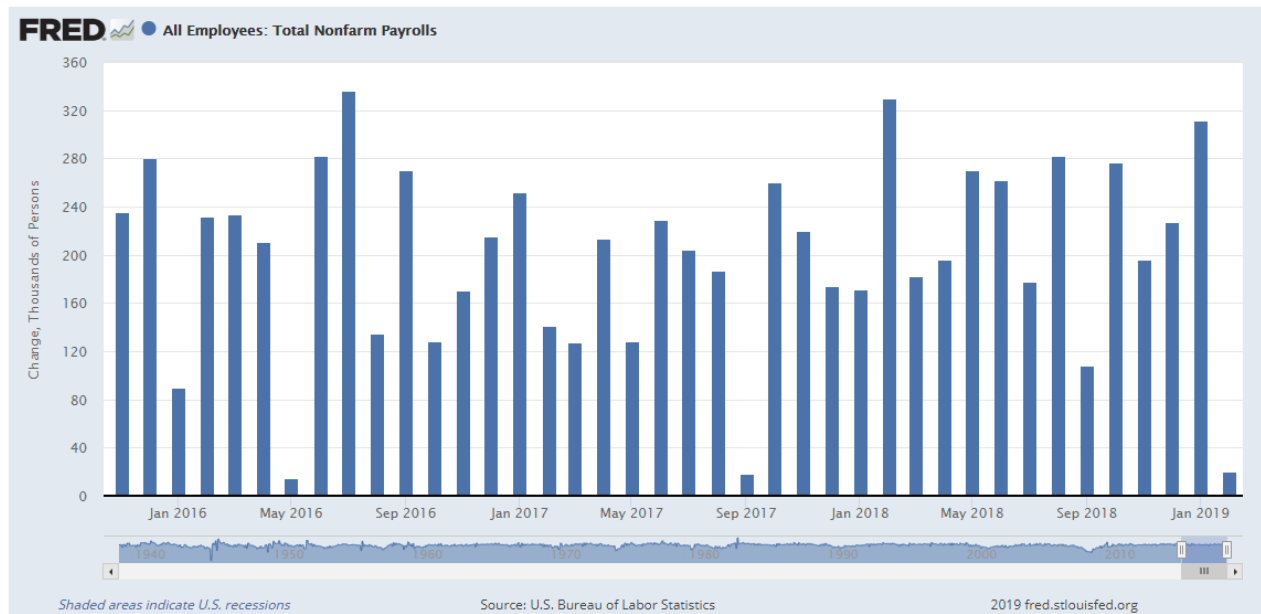


Source: Federal Reserve Bank of St. Louis, National Economic Trends, February 2019.

Treasury Yield Curve Percent



Change in Nonfarm Payrolls



Source: Federal Reserve Bank of St. Louis, National Economic Trends, February 2019.

ECONOMIC REPORTS AND FORECASTS: UNITED STATES

FEDERAL RESERVE BANK, DALLAS NATIONAL UPDATE

December 2018 - www.dallasfed.org

↑ U.S. Economy Finishes the Year Strong

The U.S. economy continued its expansion in the fourth quarter, fueled in part by strong consumption and rising wage growth. Inflation remained at or around the Federal Reserve's 2% target. Volatility in financial markets persisted, but its effects on the near-term outlook remain murky.

↕ Fourth-Quarter Growth Suggests Return to Normal Levels

Preliminary estimates suggest that output growth remains healthy but has slowed in the fourth quarter, following strong growth in the previous two quarters. Forecasts from the Survey of Professional Forecasters and the Atlanta and New York Federal Reserve Banks show fourth-quarter gross domestic product (GDP) growth of around 2.5%, a decline of nearly 1 percentage point from the third-quarter rate of 3.4% (third estimate). Weaker growth in the fourth quarter may be a result of the waning effects of the tax cuts enacted earlier this year and uncertainty surrounding current trade disputes.

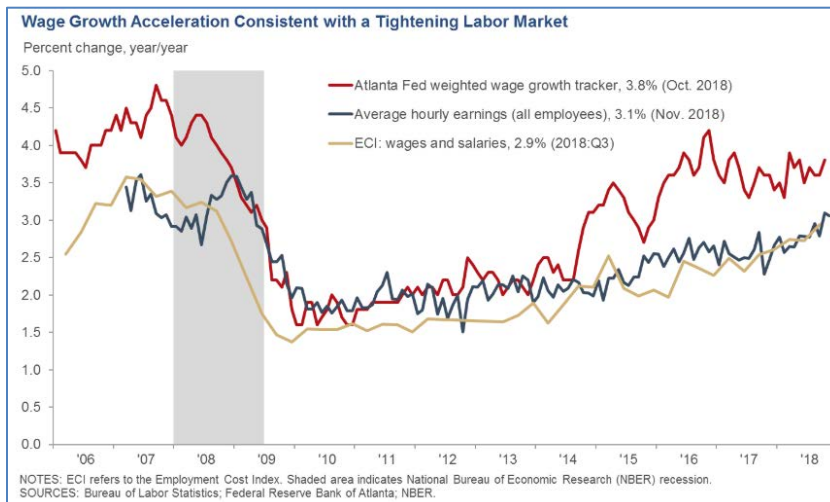
A decomposition of third-quarter GDP shows personal consumption expenditures (PCE) and inventory investment were strong positive contributors to output growth at 2.5 and 2.3 percentage points, respectively. Drags on output included net exports (exports minus imports) and residential investment.

↕ Labor Market Tightens, Wages Rise

Unemployment remained at 3.7% for the third straight month in November. Total nonfarm payrolls increased by 155,000 in November compared with October's 237,000 gain. The Job Openings and Labor Turnover Survey (JOLTS) provides data on labor market conditions two months prior to its release. Using JOLTS, labor market tightness can be estimated and is typically measured as the number of job openings per unemployed person. This value reached 1.18 in October, its highest level since the early 1970s. The

JOLTS "quits rate," which measures voluntary departures (typically due to workers switching jobs) as a fraction of total employment, was 2.3% in October, close to its highest rate on record since 2000. This elevated quits rate suggests workers are increasingly being poached, further pressuring wages.

Wage growth continued its upward trajectory in November. Growth in average hourly earnings was 3.05%, near its October increase of 3.1%. October was the first time since the Great Moderation period (1985-2007) that growth in average hourly wages exceeded 3%. The Atlanta

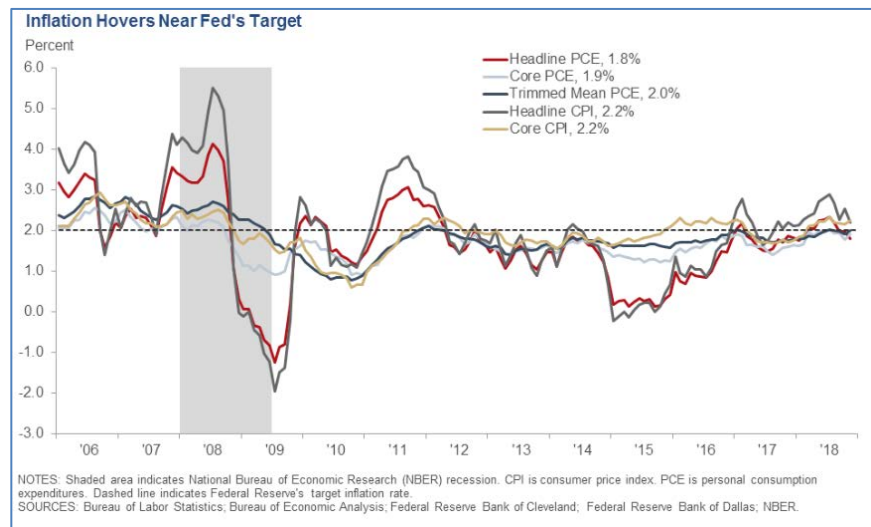


Fed Wage Tracker's three-month moving average and the Employment Cost Index, two other measures of wage growth, also saw slightly higher growth rates in their latest readings. Nominal wage growth is now outpacing inflation, indicating steady growth in real wages. After adjusting for inflation, the recent estimates of all three measures are about 1 percentage point above their 2008-13 averages.

↕ Inflation Remains Near Fed's Target

Inflation remained at or close to the Federal Reserve's 2% target in November. The headline Consumer Price Index (CPI) experienced a modest decline, dropping from 2.5% in October to 2.2% in November. Similarly, headline PCE dipped to 1.8% in November from its October level of 2.0%.

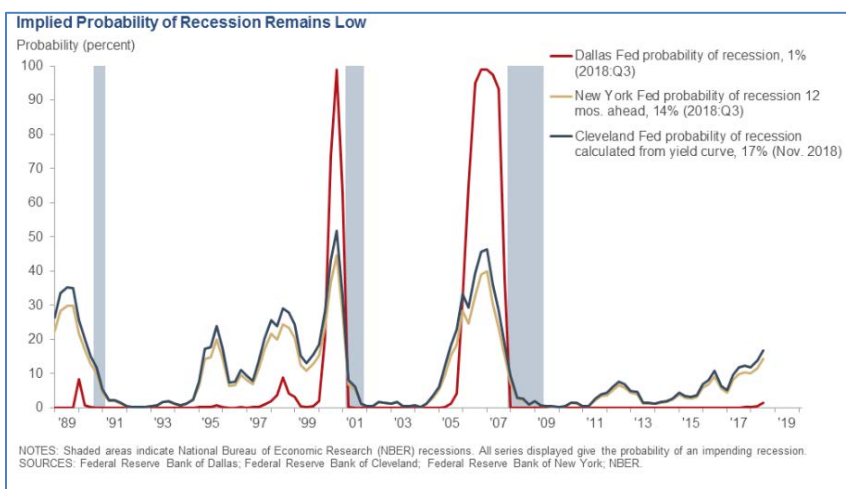
Excluding energy and food from inflation estimates, rates were little changed from October to November. Core CPI inched up by 0.1% to 2.2 in November, while core PCE rose to 1.9% over the same period. Long-term inflation expectations remain stable as well. The Survey of Professional Forecasters' five-year/five-year-forward median CPI expectation (expected average inflation over the five-year period beginning five years from now) remained at its third-quarter level of 2.2% in the fourth quarter.



↓ Financial Sector Experiences Higher Volatility

In recent weeks, investors' unease has been reflected in Treasury note yield spreads. As of Dec. 14, the average 10-year Treasury yield for the month stands at 2.9% — its lowest monthly average since August. Similarly, yields of several other maturities have declined at varying rates during the past four weeks, leading to partial inversions of the yield curve. For instance, on Dec. 10, the difference between the five-

year and three-year note yields turned negative. The 10-year/one-year and 10-year/two-year spreads have also seen steady declines since the beginning of the year and are currently hovering near 0.1%.



probability estimates, ranging from 1% to 17%, these values are still significantly below those observed prior to previous recessions. In addition, volatility in the financial sector has not yet spread to the real economy, though it does bear watching in the near-term.

U.S. ECONOMY AT A GLANCE

U.S. BUREAU OF LABOR STATISTICS

Data Series	Aug 2018	Sept 2018	Oct 2018	Nov 2018	Dec 2018	Jan 2019
Unemployment Rate ⁽¹⁾	3.9	3.7	3.8	3.7	3.9	4.0
Change in Payroll Employment ⁽²⁾	(P) 201	108	277	196	227	(P) 311
Average Hourly Earnings ⁽³⁾	(P) 27.16	27.30	27.35	27.43	27.53	(P) 27.55
Consumer Price Index ⁽⁴⁾	0.1	0.1	0.3	0.0	0.0	0.0
Producer Price Index ⁽⁵⁾	-0.1	0.1	(P) 0.5	(P) 0.1	(P) -0.1	(P) -0.1
U.S. Import Price Index ⁽⁶⁾	-0.4	0.1	0.5	(R) -1.7	(R) -1.0	(R) -0.5

Footnotes:

- (1) In percent, seasonally adjusted. Annual averages are available for Not Seasonally Adjusted Data.
 (2) Number of jobs, in thousands, seasonally adjusted.
 (3) Average hourly earnings for all employees on private nonfarm payrolls.
 (4) All items, U.S. city average, all urban consumers, 1982-84=100, 1-month percent change, seasonally adjusted.
 (5) Final Demand, one-month percent change, seasonally adjusted.
 (6) All imports, one-month percent change, not seasonally adjusted.
 (R) Revised.
 (P) Preliminary.

Data Series	4th Qtr 2017	1 st Qtr 2018	2nd Qtr 2018	3rd Qtr 2018	4th Qtr 2018
Employment Cost Index ⁽¹⁾	0.6	0.8	0.6	0.8	0.7
Productivity ⁽²⁾	(R) -0.4	(R) 0.6	(R) 2.8	(R) 1.8	1.9

Footnotes:

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

Data extracted on: March 11, 2019

THE FEDERAL RESERVE BOARD

THE BEIGE BOOK – JANUARY 16, 2019 EXCERPT

Overall Economic Activity

Economic activity increased in most of the U.S., with eight of twelve Federal Reserve Districts reporting modest to moderate growth. Nonauto retail sales grew modestly, as several Districts reported more holiday traffic compared with last year. Auto sales were flat on balance. The majority of Districts indicated that manufacturing expanded, but that growth had slowed, particularly in the auto and energy sectors. New home construction and existing home sales were little changed, with several Districts reporting that sales were limited by rising prices and low inventory. Commercial real estate activity was also little changed on balance. Most Districts reported modest to moderate growth in activity in the nonfinancial services sector, though a few Districts noted that growth there had slowed. The energy sector expanded at a slower pace, and lower energy prices contributed to a pullback in the industry's capital spending expectations. The agriculture sector struggled as prices generally remained low despite recent increases. Overall, lending volumes grew modestly, though a few Districts noted that growth had slowed. Outlooks generally remained positive, but many Districts reported that contacts had become less optimistic in response to increased financial market volatility, rising short-term interest rates, falling energy prices, and elevated trade and political uncertainty.

Highlight of Dallas Federal Reserve

While economic activity remained healthy, growth abated to a more modest pace. A broad-based deceleration was seen across manufacturing, services, retail, and energy. Hiring continued, and widespread labor shortages further elevated wages. Price pressures eased slightly. Outlooks were markedly less optimistic than the previous report.

ECONOMIC REPORTS AND FORECASTS: STATE OF TEXAS

FEDERAL RESERVE BANK, DALLAS

January 2019 - www.dallasfed.org

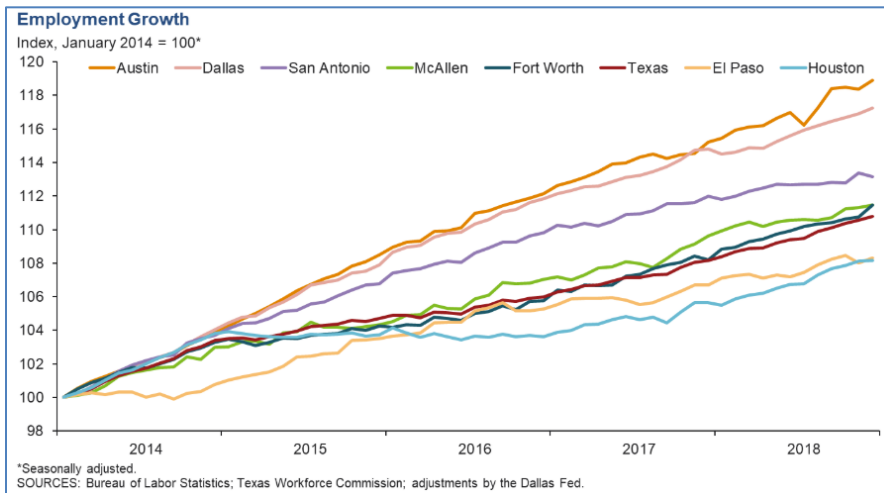
Texas economic indicators were mixed in December. The state finished 2018 with strong job growth and continued labor market tightness, but forward-looking indicators suggest that the state's economic outlook has softened. The leading index dipped for the third month, and the Dallas Fed's 2019 employment forecast shows slower growth than the state's long-run average. The Texas Business Outlook Surveys suggest that current output growth slowed, and firm sentiment about broader economic conditions and company outlooks deteriorated.

⇅ Labor Markets

Texas employment expanded an annualized 2.5% in December, bringing 2018 growth to 2.4%, or 298,219 jobs. The Dallas Fed's Texas Employment Forecast predicts 1.1% job growth in 2019 (December/December), with an 80% confidence band of -0.5% to 2.7%. The forecast growth rate is well below the state's long-run (January 1990-December 2018) growth rate of 2.1%. The Texas unemployment rate held steady for the third straight month at 3.7% in December, while the U.S. rate

ticked up to 3.9%. Both are well below their long-run averages, indicating continued labor market tightness.

All major metros except San Antonio added jobs in December, and employment expanded in all the metros in the fourth quarter. Austin had the fastest employment growth in 2018 at 3.2%, followed by Fort Worth (3.0%), Houston (2.4%) and Dallas (2.1%). San Antonio's 1.0% growth was the slowest among the major metros.



Solid growth in December was buoyed by a 20.1% expansion in oil and gas extraction employment, the fastest among the state's major sectors, followed by other services at 9.8% and education and health services at 7.9%. However, the information; trade, transportation and utilities; and professional and business services sectors shed jobs. Government employment was flat in 2018, but all other sectors added to payrolls last year, led by oil and gas extraction's 9.6% expansion.

⇅ Texas Leading Index

The Texas Leading Index, a composite of eight indicators that tend to change direction before the overall economy does, sheds light on the future of the state's economy. In December, the estimated value of the

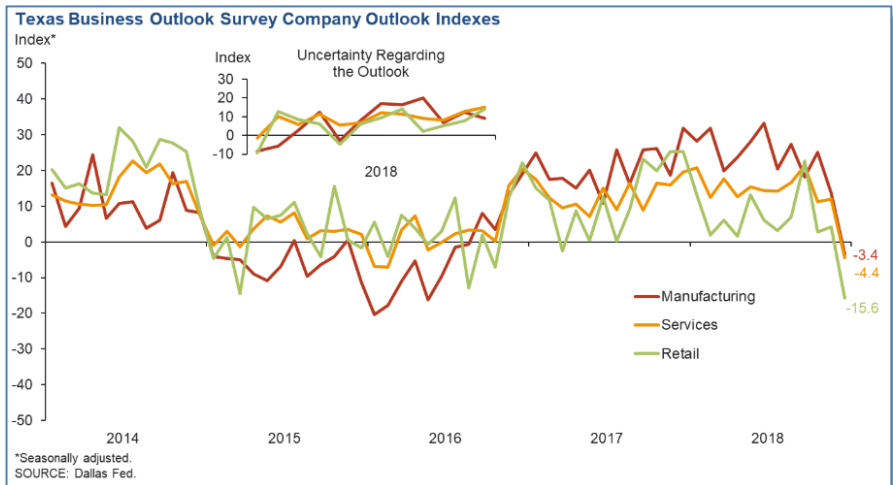
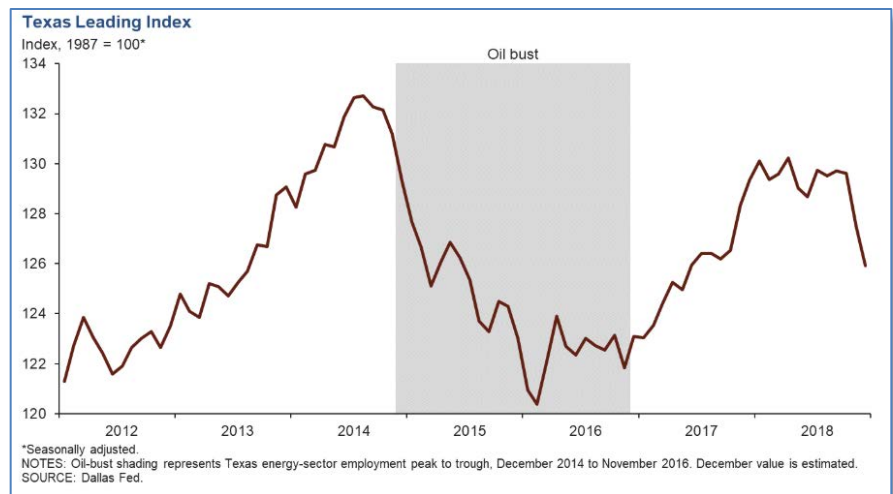
index dipped 1.2%, marking the third month of decline. The Texas stock index was the largest drag on the index in December, while the help-wanted index was the most significant positive contributor.

↓ Firms Report Deteriorating Business Condition

The FRB of Dallas' business outlook surveys pointed to worsening business conditions in December. The general business activity indexes in the manufacturing, services and retail surveys fell into negative territory, suggesting that business sentiment has weakened. The headline indexes of the three surveys remained positive but declined, suggesting deceleration in manufacturing production, service sector revenue, and retail sales growth.

↓ Firms' Outlooks Weaken

Firms across the three surveys also reported worsening company outlooks in December. All three company outlook indexes turned negative, with the more volatile retail index falling the most. The services and retail sector uncertainty indexes rose as a larger share of firms reported increased uncertainty regarding their company outlooks, while the manufacturing uncertainty index dipped but remained positive.

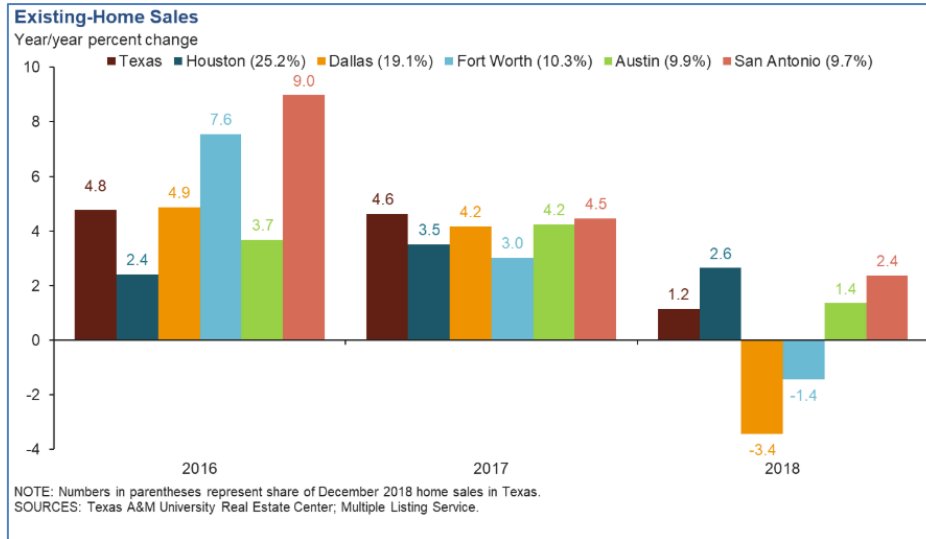


↕ Energy Sector Activity

Oil prices rose 1.6% to \$51.57 in the week ending Jan. 18, marking the third week of recovery after plummeting 39.8% from their October high. Natural gas prices rebounded to \$3.50 during the week, following five successive weeks of decline that reduced prices 35.6%. The rig count contracted by 11 in the week ending January 18 after remaining largely flat in recent months.

⇅ Housing

Texas' existing-home sales inched up 0.4% in December, but the five-month moving average edged down 0.2%. Existing-home sales were up 1.2% in 2018 compared with 2017. Houston, the state's largest market, recorded a 2.6% increase, followed by San Antonio's 2.4% and Austin's 1.4% growth. Dallas' existing-home sales were 3.4% lower in 2018 than in the previous year, and Fort Worth sales were down 1.4%.



TEXAS ECONOMIC STATISTICS

U.S. BUREAU OF LABOR STATISTICS

Data Series	Aug 2018	Sept 2018	Oct 2018	Nov 2018	Dec 2018	Jan 2019
Labor Force Data						
Civilian Labor Force ⁽¹⁾	⁽²⁾ 13,861.0	⁽²⁾ 13,888.9	⁽²⁾ 13,914.2	⁽²⁾ 13,921.6	⁽²⁾ 13,920.8	^(P) 13,956.3
Employment ⁽¹⁾	⁽²⁾ 13,344.1	⁽²⁾ 13,375.2	⁽²⁾ 13,400.9	⁽²⁾ 13,406.4	⁽²⁾ 13,404.4	^(P) 13,430.8
Unemployment ⁽¹⁾	⁽²⁾ 13,344.1	⁽²⁾ 13,375.2	⁽²⁾ 13,400.9	⁽²⁾ 13,406.4	⁽²⁾ 13,404.4	^(P) 13,430.8
Unemployment Rate ⁽³⁾	⁽²⁾ 3.7	⁽²⁾ 3.7	⁽²⁾ 3.7	⁽²⁾ 3.7	⁽²⁾ 3.7	^(P) 3.8
Nonfarm Wage and Salary Employment						
Total Nonfarm ⁽⁴⁾	12,552.6	12,560.0	12,600.3	12,614.7	12,633.9	^(P) 12,649.3
12-month% change	2.6	2.6	2.4	2.4	2.3	^(P) 2.4
Mining and Logging ⁽⁴⁾	249.5	252.0	254.6	254.8	256.5	^(P) 258.2
12-month% change	11.0	11.2	11.7	10.8	10.5	^(P) 10.6
Construction ⁽⁴⁾	743.5	743.6	744.9	748.0	753.6	^(P) 748.8
12-month% change	4.8	4.7	3.8	3.6	3.9	^(P) 3.4
Manufacturing ⁽⁴⁾	884.6	886.9	888.4	895.5	899.6	^(P) 897.6
12-month% change	3.3	3.5	3.3	3.9	4.1	^(P) 3.8
Trade, Transportation, and Utilities ⁽⁴⁾	2,488.3	2,495.0	2,499.3	2,511.2	2,509.7	^(P) 2,515.4
12-month% change	1.5	1.9	1.7	1.8	1.7	^(P) 2.1
Information ⁽⁴⁾	203.4	204.4	202.9	205.2	204.3	^(P) 204.5
12-month% change	0.4	1.2	-0.4	0.8	0.2	^(P) 0.3
Financial Activities ⁽⁴⁾	780.1	780.8	782.1	781.7	781.5	^(P) 784.3
12-month% change	2.2	1.8	1.7	1.7	1.5	^(P) 1.9
Professional & Business Services ⁽⁴⁾	1,746.2	1,746.7	1,751.6	1,748.1	1,745.4	^(P) 1,754.2
12-month% change	4.1	3.4	3.3	3.0	2.8	^(P) 2.8
Education & Health Services ⁽⁴⁾	1,702.8	1,704.7	1,709.2	1,710.7	1,714.8	^(P) 1,717.2
12-month% change	2.2	2.3	2.4	2.3	2.3	^(P) 2.3
Leisure & Hospitality ⁽⁴⁾	1,362.8	1,354.7	1,373.7	1,366.2	1,373.1	^(P) 1,369.7
12-month% change	2.8	2.9	3.4	2.6	2.8	^(P) 2.3
Other Services ⁽⁴⁾	433.4	435.9	437.2	437.4	438.4	^(P) 437.6
12-month% change	2.0	2.2	2.0	1.7	1.9	^(P) 1.8
Government ⁽⁴⁾	1,958.0	1,955.3	1,956.4	1,955.9	1,957.0	^(P) 1,961.8
12-month% change	1.1	1.0	0.8	0.7	0.8	^(P) 1.0
Footnotes ⁽¹⁾ Number of persons, in thousands, seasonally adjusted. ⁽²⁾ Reflects revised population controls, model reestimation, and new seasonal adjustment. ⁽³⁾ In percent, seasonally adjusted. ⁽⁴⁾ Number of jobs, in thousands, seasonally adjusted. ^(P) Preliminary.						

Data extracted on: March 11, 2019

FEDERAL RESERVE BANK

SENIOR LOAN OFFICER OPINION SURVEY

The January 2019 Senior Loan Officer Opinion Survey on Bank Lending Practices addressed changes in the standards and terms on, and demand for, bank loans to businesses and households over the past three months, which generally corresponds to the fourth quarter of 2018.

Regarding loans to businesses, respondents to the January survey indicated that, on balance, banks tightened standards for commercial real estate (CRE) loans, while standards and most terms on commercial and industrial (C&I) loans remained basically unchanged. Meanwhile, demand for loans to businesses reportedly weakened.

For loans to households, banks reported that their lending standards for most categories of consumer loans and residential real estate loans remained basically unchanged on balance. Credit cards were the one exception, with standards reportedly tightening over the fourth quarter. Meanwhile, banks reported weaker demand for all categories of loans to households.

In addition, the survey included a set of special questions inquiring about banks' expectations for lending policies and loan performance over 2019. Banks reported expecting to tighten standards for all categories of business loans as well as credit card loans and jumbo mortgages. Demand for most loan types is expected to weaken, on net, with the one exception being credit card loans, for which demand is expected to remain unchanged. Meanwhile, banks anticipate that loan performance will deteriorate for all surveyed categories.

BUSINESS LENDING

C&I Loans

Banks reported that standards for C&I loans to both large and middle-market firms and to small firms remained basically unchanged over the past three months. Most terms on such loans remained basically unchanged as well, although a moderate net share of banks reported increasing the premiums charged on riskier loans to large and middle-market firms and a modest net share of banks reported doing so for loans to small firms. Large banks, however, did report easing some key terms on loans to large and middle-market firms; moderate net shares of the largest banks reported increasing maximum credit lines, easing loan covenants, and narrowing loan rate spreads over costs of funds. Meanwhile, foreign banks reported tightening standards and most terms for C&I loans.

Nearly every bank that reported having eased standards or terms over the past three months attributed this change, in part, to increased competition from other banks or nonbank lenders. No other reason queried was cited as

important by a majority of banks. The reported reasons for tightening standards or terms were more varied. A less favorable or more uncertain economic outlook was the most cited reason for tightening, with reduced tolerance for risk and increased concerns about the effects of legislative changes, supervisory actions, or changes in accounting standards also being cited by more than half of the banks that reported tighter standards or terms.

Regarding the demand for C&I loans, a modest net share of domestic banks reported that demand for C&I loans from large and middle-market firms weakened, while a moderate net share of banks reported weakened demand from small firms. Meanwhile, a moderate net share of foreign banks reported weaker demand for C&I loans over the fourth quarter. A majority of the banks that reported weaker demand indicated that decreases in customers' needs to finance mergers and acquisitions as well as investment in plants and equipment

contributed to weaker demand, as did a shift in customers' borrowing toward other bank or nonbank sources.

CRE Lending

Moderate net fractions of banks reported tightening their standards for loans secured by multifamily residential properties and loans for construction and land development purposes, while a modest net share of banks reported

tightening standards for loans secured by nonfarm nonresidential properties. Meanwhile, a significant net fraction of banks reported weaker demand for construction and land development loans, and a modest net share reported weaker demand for multifamily loans. Demand for loans secured by nonfarm nonresidential properties was basically unchanged on net.

LENDING TO HOUSEHOLDS

Residential Real Estate Lending

On balance, banks reported that standards for residential real estate lending remained basically unchanged over the past three months. Standards were reported to be basically unchanged for all seven home purchase mortgage categories as well as for revolving home equity lines of credit (HELOCs). Meanwhile, significant net shares of banks reported weaker demand for all categories of residential mortgages, and a moderate net share of banks reported weaker demand for HELOCs.

Consumer Lending

A moderate net percentage of banks reported tightening standards on credit card loans over the past three months, while standards on auto and other consumer loans were reportedly little changed on net. In addition to tightening

standards on credit card loans, banks also reportedly tightened several terms on such lending. Modest net shares of banks reportedly increased the minimum required credit scores and widened loan rate spreads on credit card loans. While a modest net share of banks reported widening loan rate spreads on auto loans, banks reportedly kept most terms on auto lending and other consumer loans about unchanged.

Demand for auto, credit card, and other consumer loans reportedly was little changed on balance. A modest net share of banks reported increased willingness to make consumer installment loans.

SPECIAL QUESTION ON BANKS' OUTLOOK FOR 2019

A set of special questions asked banks about their expectations for lending standards, loan demand, and loan performance over 2019, assuming that economic activity progresses in line with consensus forecasts. On balance, banks reported expecting tighter standards, weaker demand, and worse loan performance, for most loan categories.

Regarding expectations for loans to businesses, moderate net fractions of banks reported that they expect to tighten standards on C&I loans to firms of all sizes, while significant net shares of banks expect to tighten standards for all three CRE loan categories.

Meanwhile, demand is expected to weaken for all business loans: Moderate net shares of banks reported expecting weaker demand for C&I loans to firms of all sizes, significant net shares of banks expect weaker demand for loans secured by multifamily properties or nonfarm nonresidential properties, and a major net share of banks expect weaker demand for construction and land development loans.

Additionally, banks reported expecting loan performance, as measured by charge-offs and delinquencies, to deteriorate, with either moderate or significant net shares of banks reporting expecting performance to deteriorate for the surveyed business loan categories.

The outlook for loans to households over the next year is broadly similar to the outlook for loans to businesses, although somewhat less uniform across loan categories. A moderate net share of banks reported expecting tighter standards for credit card loans, and a modest net share reported expecting tighter standards on nonconforming jumbo residential mortgage loans.

In contrast, standards for auto loans and GSE (government sponsored enterprise)-eligible mortgages are expected to remain basically unchanged on net. Meanwhile, either moderate or significant net shares of banks reported expecting weaker demand for these loans, with the exception of credit card loans, for which demand is expected to remain basically unchanged.

Loan performance is also reported as being expected to deteriorate for all categories of loans to households, with modest or moderate net shares of banks expecting performance to deteriorate for mortgages and consumer loans to prime borrowers, and significant net shares of banks expecting performance to deteriorate for consumer loans to nonprime borrowers.

Banks that reported expecting to tighten standards for any loan category were additionally asked to assess the importance of several potential reasons for the expected tightening. An expected deterioration in collateral values was the most widely cited reason for expecting to tighten standards. In addition, a majority of banks reported that an expected reduction in their risk tolerance and an expected deterioration in the quality of their loan portfolios contributed to the expected tightening of standards.

ACKNOWLEDGEMENTS AND RESOURCES

American Banker, New York, New York

Austin Business Journal, Austin, Texas

Baker Hughes, Houston, Texas

Board of Governors of the Federal Reserve System, Washington, D.C.

Builder Magazine, Washington, D.C.

Brookings Institute, Washington, D.C.

CNBC, Englewood Cliffs, New Jersey

Federal Deposit Insurance Corporation, Washington, D.C.

Federal Reserve Bank of Dallas, Dallas, Texas

Federal Reserve Bank of Saint Louis, Saint Louis, Missouri

Finance Commission of Texas, Austin, Texas

Hobby Center for the Study of Texas, Houston, Texas

Houston Chronicle, Houston, Texas

Houston Public Media, Houston, Texas

IBM, Armonk, New York

Lone Star Policy Institute, Dallas, Texas

Migrant Policy Institute, Washington, D.C.

National Drought Mitigation Center, Lincoln, Nebraska

Office of the Comptroller of the Currency, Washington, D.C.

Office of the Governor, Austin, Texas

Real Estate Center at Texas A&M University, College Station, Texas

San Antonio Express-News, San Antonio, Texas

Texas A&M AgriLife Extension, College Station, Texas

Texas Comptroller of Public Accounts, Austin, Texas

Texas Farm Bureau, Waco, Texas

Texas Department of Banking, Austin, Texas

Texas Department of Savings and Mortgage Lending, Austin, Texas

Texas Demographic Center, San Antonio, Texas

Texas General Land Office, Austin, Texas

Texas Workforce Commission, Austin, Texas

The Perryman Group, Waco, Texas

The Trade Partnership, Washington, D.C.

The Wall Street Journal, New York, New York

U.S. Bureau of Economic Analysis, Washington, D.C.

U.S. Bureau of Labor Statistics, Washington, D.C.

U.S. Census Bureau, Suitland, Maryland

U.S. Department of Agriculture, Washington, D.C.

U.S. Department of Housing and Urban Development, Washington, D.C.

Yahoo Finance, online

*Visit the Finance Commission of Texas [website](#) for previous
Condition of the Texas State Banking System Reports.*