



**SMALL BANK**

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Comptroller of the Currency  
Administrator of National Banks

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Washington, DC 20219

## **PUBLIC DISCLOSURE**

December 03, 2012

### **COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION**

The Hondo National Bank  
Charter Number 14351

1112 Eighteenth Street  
Hondo, TX 78861

Office of the Comptroller of the Currency

San Antonio South Field Office  
10001 Reunion Place, Suite 250  
San Antonio, TX 78216-4133

**NOTE:** This document is an evaluation of this 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. 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.

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

The Hondo National Bank's (HNB) lending performance reflects a satisfactory response to community credit needs in its assessment areas (AA). This conclusion is based on the following results from our review:

- The loan-to-deposit (LTD) ratio meets the standard for satisfactory performance.
- The bank originated a substantial majority of loans inside its AAs.
- Lending activities represent a reasonable penetration among individuals of different income levels and businesses of different sizes.
- Geographic distribution of loans represents a reasonable dispersion.

## **SCOPE OF EXAMINATION**

HNB was evaluated under the Small Bank examination procedures, which includes a lending test. The lending test evaluates the bank's record of meeting the credit needs of its AAs through its lending activities.

The lending test for HNB covers its performance from May 27, 2008 through September 30, 2012. HNB's primary loan products are commercial and residential real estate loans. To evaluate the bank's commercial and residential lending performance, we selected a sample of commercial and residential loans made from January 1, 2010 through December 31, 2011. The bank reports data under the requirements of the Home Mortgage Disclosure Act (HMDA). HMDA data from 2010 and 2011 were tested. The 2010 HMDA data were found to be unreliable. Therefore, HMDA data was not used to evaluate the bank's residential loan performance.

## **DESCRIPTION OF INSTITUTION**

HNB, an intrastate bank headquartered in Hondo, Texas, was chartered in 1936 and is wholly owned by Texas Heritage Bancshares. The bank's business strategy is to maintain community ties and provide state of the art banking services with friendly one-on-one service. HNB reported total assets of \$170 million and tier 1 capital of \$14 million at September 30, 2012. It has four offices: the main office located in Hondo and three branches located in Bandera, Uvalde, and Leakey, Texas. HNB provides full service loan and deposit products at all branches.

The main office and all three branches have a walk-in teller lobby, a drive-up motor bank, and an automated teller machine (ATM). All offices accept loan applications and all loans are closed in the office where the application originated. Additionally, customers can access their depository accounts through the internet, ATMs, and telephone bank. There have not been any significant changes to HNB's corporate structure, including merger or acquisition activities, since the last CRA examination that will impact this report.

As of September 30, 2012, HNB reported total loans of \$109 million and a net loans and leases to total assets ratio of 59.9 percent. The following chart provides a detailed summary of the loan portfolio at September 30, 2012.

Loan Portfolio Summary by Loan Product September 30, 2012		
Loan Category	Dollar Volume \$(000)	% of Outstanding Dollars
Commercial	40,780	37.47%
Residential	38,966	35.80%
Agricultural / Farm	18,123	16.65%
Consumer	9,931	9.13%
Other Loans	1,029	0.95%
Total	108,829	100%

There are no legal, financial, or other factors that impede HNB’s ability to help meet the credit needs in its AAs. The previous CRA examination, dated May 27, 2008, rated HNB “Satisfactory” under the small bank criteria.

## DESCRIPTION OF ASSESSMENT AREA(S)

HNB has two AAs which include the combined counties of Medina-Bandera and Uvalde-Real. Medina and Bandera County were combined because they are contiguous counties located in the San Antonio-New Braunfels metropolitan statistical area (MSA). Uvalde and Real County were combined because they are contiguous counties that are not located in any MSA. The defined AAs meet the requirements of the CRA regulation and no low- or moderate-income tracts are arbitrarily excluded.

### Medina–Bandera County Assessment Area

The Medina-Bandera County AA is comprised of the complete counties. Medina-Bandera County includes the towns of Hondo, Castroville, La Coste, Devine, Natalia, D’Hanis, Bandera, and Medina and is located in the San Antonio-New Braunfels MSA in South Texas. The county seats, Hondo and Bandera, are located approximately 40 miles west and 50 miles northwest of San Antonio respectively. This AA meets the requirements of the regulation and does not contain any low-or moderate-income (LMI) areas.

Demographic Information for the Medina-Bandera County AA					
	#	% Low	% Moderate	% Middle	% Upper
Geographies (Census Tracts)	10	0	0	100	0
Population by Geography	47,790	0	0	100	0
Owner-Occupied Housing by Geography	16,073	0	0	100	0
Businesses by Geography	5,796	0	0	100	0
Farms by Geography	461	0	0	100	0
Family Distribution by Income Level	15,417	21.53	19.68	22.19	36.60
Household Distribution by Income Level	19,950	18.50	14.02	17.53	49.95
Census Median Family Income (MFI)		\$42,271	Median Housing Value		\$73,742

HUD-Adjusted MFI: 2011	\$59,900	Families Below Poverty Level	13.70%
HUD- Adjusted MFI: 2010	\$57,800	Unemployment Rate	3.00%

The current local economy is characterized as good and stable. Economic activity is centered in agriculture, service and recreational industries, and retail and wholesale businesses. Average unemployment is low. Competition from other financial institutions is high. The bank’s competitors include eight local community banks, two finance companies, and two large bank branches.

We contacted a member of a local community organization who indicated that the community’s current economic condition is good. He indicated that there is demand for commercial loans. He feels that the main opportunity for financial institutions to aid in community development is by participating in guaranteed loan programs designed to improve business activities in rural communities.

**Uvalde-Real County Assessment Area**

The Uvalde-Real County AA is comprised of the complete counties and includes the towns of Uvalde, Sabinal, Camp Wood, and Leakey. The county seats, Uvalde and Leakey, are located approximately 85 and 100 miles west of San Antonio respectively. This AA meets the requirements of the regulation and does not arbitrarily exclude any LMI areas.

<b>Demographic Information for the Uvalde-Real County AA</b>					
	#	% Low	% Moderate	% Middle	% Upper
Geographies (Census Tracts)	6	0	16.67	83.33	0
Population by Geography	28,973	0	21.89	78.11	0
Owner-Occupied Housing by Geography	7,123	0	17.91	82.09	0
Businesses by Geography	2500	0	17.60	82.40	0
Farms by Geography	191	0	15.18	84.82	0
Family Distribution by Income Level	7,553	27.12	20.31	19.85	19.65
Household Distribution by Income Level	9,777	28.13	17.75	18.43	35.70
Census Median Family Income (MFI)		\$30,562	Median Housing Value		\$47,607
HUD-Adjusted MFI: 2011		\$48,600	Families Below Poverty Level		22.76%
HUD- Adjusted MFI: 2010		\$46,500	Unemployment Rate		3.55%

The current local economy is characterized as good and expanding due in part to the current oil and gas mining activity associated with the Eagle Ford shale formation. Economic activity in the area is relatively diverse with oil field related businesses, agriculture, service industries, and recreational and retail businesses being the primary economic activities. Average unemployment for the area is low. Competition from other financial institutions is high. The bank’s competitors include four local community banks, one regional bank branch, two branches of large financial institutions, and two finance companies.

We contacted a member of a local community organization who indicated that the community’s current economic condition is good due to the oil field activity in the area. She indicated that there is a shortfall in single and multi-family housing as a result of oil and gas exploration and

mining in the area. Based on this information she feels that there is an opportunity for financial institutions to aid in community development is by providing residential construction loans.

## CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

### LENDING TEST

HNB’s performance under the lending test is satisfactory considering the performance context and needs of its’ AAs. Borrower distribution was given more weight than the geographic distribution. This was due to the fact that a geographic distribution evaluation was not performed in one AA because the Medina-Bandera County AA contained only middle-income CTs.

#### Loan-to-Deposit Ratio

HNB’s net loan-to-deposit ratio is reasonable given the bank’s size, financial condition, and AA credit needs. The net loan-to-deposit ratio averaged 68.55 percent over the 18 quarters since the last CRA examination, with a low of 60.69 percent and a high of 78.27 percent.

The ratio compares favorably to the ratios of other community banks of similar sizes, locations, and product offerings. HNB ranks second among a total of five similarly situated banks serving its AA. The other four banks had an average net loan-to-deposit ratio of 63.71 percent, ranging from 47.48 percent to 73.37 percent.

#### Lending in Assessment Area

A substantial majority (82.50 percent) of the primary loan products originated within the AAs. The following table details the bank’s lending within the AAs by number and dollar amount of loans that originated during the evaluation period.

<b>Table 1 - Lending in the Assessment Areas</b>										
Loan Type	Number of Loans					Dollars of Loans (000s)				
	Inside		Outside		Total	Inside		Outside		Total
	#	%	#	%		\$	%	\$	%	
Commercial	15	75.00	5	25.00	20	2,543	88.95	316	11.05	2,859
Residential	18	90.00	2	10.00	20	1,797	87.20	264	12.80	2,061
Totals	33	82.50	7	17.50	40	4,340	88.21	580	11.79	4,920

Source: Loan sample

#### Lending to Borrowers of Different Incomes and to Businesses of Different Sizes

The distribution of loans reflects reasonable penetration among individuals of different income levels and businesses of different sizes, given the bank’s product offerings and local economic conditions.

Performance in the Medina-Bandera County AA

The borrower distribution of loans in the Medina-Bandera County AA is reasonable. Commercial loans were identified as credit needs in this AA.

*Commercial Loans*

The distribution of loans to businesses reflects excellent penetration among businesses of different sizes. Ninety percent of the bank’s loans to businesses originated and purchased during the loan sampling period were made to small businesses (defined as businesses with gross annual revenues of one million dollars or less). The following table shows the distribution of commercial loans among different sized businesses in the AA.

<b>Table 2A - Borrower Distribution of Loans to Businesses in Medina-Bandera County AA</b>				
Business Revenues (or Sales)	≤\$1,000,000	>\$1,000,000	Unavailable/ Unknown	Total
% of AA Businesses	70.51%	1.36%	28.12%	100%
% of Bank Loans in AA by #	90.00%	10.00%	0%	100%
% of Bank Loans in AA by \$	73.22%	26.78%	0%	100%

Source: Loan sample; Dunn and Bradstreet data.

*Residential Real Estate Loans*

The distribution of residential loans reflects reasonable penetration among borrowers of different income levels. HNB made 15.00 percent of its residential loans to low-income borrowers and 10.00 percent of its residential loans to moderate-income individuals during the evaluation period. The demographic data indicates that 21.53 percent of families in the AA are low-income and 19.68 percent of families in the AA are moderate-income. A mitigating factor in the penetration of low-income families is the fact that households below the poverty level represent 13.70 percent of the total households in the AA. Borrowers living below the poverty level could have a difficult time qualifying for residential loans. The following table shows the distribution of residential loans among borrowers of different income levels compared to the percent of families in each income category.

<b>Table 2 - Borrower Distribution of Residential Real Estate Loans in Medina-Bandera County AA</b>								
Borrower Income Level	Low		Moderate		Middle		Upper	
	% of AA Families	% of Number of Loans						
Residential	21.53	15.00	19.68	10.00	22.19	45.00	36.60	30.00

Source: Loan Sample; U.S. Census data

Performance in the Uvalde-Real County AA

The borrower distribution of loans in the Uvalde-Real County AA is reasonable. Residential real estate construction loans were identified as credit needs in this AA.

*Commercial Loans*

The distribution of loans to businesses reflects excellent penetration among businesses of different sizes. Ninety percent of the loans originated during the loan sampling period were made to small businesses. This is considered excellent compared to demographic data that show 66.76 percent of the area’s businesses are considered small businesses. The following table shows the distribution of commercial loans among different sized businesses.

<b>Table 2A - Borrower Distribution of Loans to Businesses in Uvalde-Real County AA</b>				
Business Revenues (or Sales)	≤\$1,000,000	>\$1,000,000	Unavailable/ Unknown	Total
% of AA Businesses	66.76%	2.04%	31.20%	100%
% of Bank Loans in AA by #	90.00%	10.00%	0%	100%
% of Bank Loans in AA by \$	90.23%	9.77%	0%	100%

*Source: Loan sample; Dunn and Bradstreet data.*

*Residential Real Estate Loans*

The distribution of residential loans reflects poor penetration among borrowers of different income levels. HNB made 10.00 percent of its residential loans to low-income borrowers and 10.00 percent of its residential loans to moderate-income individuals during the evaluation period. The demographic data indicates that 27.12 percent of families in the AA are low-income and 20.31 percent of families in the AA are moderate-income. A mitigating factor in the penetration of low-income families is the fact that households below the poverty level represent 22.76 percent of the total households in the AA. Borrowers living below the poverty level could have a difficult time qualifying for residential loans. Another mitigating factor in the penetration of low- and moderate-income families is the fact that HNB only has a four percent market share in Uvalde County. The following table shows the distribution of residential loans among borrowers of different income levels compared to the percent of families in each income category.

<b>Table 2 - Borrower Distribution of Residential Real Estate Loans in Uvalde-Real County AA</b>								
Borrower Income Level	Low		Moderate		Middle		Upper	
	% of AA Families	% of Number of Loans						
Residential	27.12	10.00	20.31	10.00	19.85	10.00	32.73	70.00

*Source: Loan Sample; U.S. Census data*

**Geographic Distribution of Loans**

The geographic distribution of loans reflects reasonable dispersion throughout the bank’s AA given identified credit needs. No significant lending gaps were found within the bank’s AAs.

Performance in the Medina-Bandera County AA

A geographic distribution evaluation was not conducted in this AA since the county only contains middle-income CTs.

Performance in the Uvalde-Real County AA

The bank’s geographic distribution of loans reflects reasonable dispersion throughout census tracts of different income levels. More weight was given to the commercial distribution because commercial loans are the bank’s primary loan product.

*Commercial Loans*

The bank’s geographic distribution of business loans reflects a reasonable dispersion throughout the census tracts of different income levels. Ten percent of the loans to businesses in this AA were made in the bank’s one moderate-income CT. This is considered reasonable compared to the demographic data.

<b>Table 3A - Geographic Distribution of Loans to Businesses in Uvalde-Real County AA</b>								
Census Tract Income Level	Low		Moderate		Middle		Upper	
Loan Type	% of AA Businesses	% of Number of Loans	% of AA Businesses	% of Number of Loans	% of AA Businesses	% of Number of Loans	% of AA Businesses	% of Number of Loans
Businesses	0.00	0.00	17.60	10.00	82.4	90.00	0.00	0.00

Source: Loan sample; Dunn and Bradstreet data.

*Residential Real Estate Loans*

The bank’s geographic distribution of home loans reflects poor dispersion throughout census tracts of different income levels. None of the bank’s residential loans were made in the bank’s one moderate-income CT located in the town of Uvalde. This is considered poor compared to the demographic data. This is due primarily to the location of the bank’s Uvalde branch and competition in the area. The bank’s Uvalde branch is located in a CT adjacent to the moderate-income tract toward the far eastern side of the moderate-income CT. Three other financial institutions are more centrally located and accessible to individuals in the moderate-income CT. HNB also only has a four percent market share in Uvalde County.

<b>Table 3 - Geographic Distribution of Residential Real Estate Loans in Uvalde-Real County AA</b>								
Census Tract Income Level	Low		Moderate		Middle		Upper	
Loan type	% of AA Owner Occupied Housing	% of Number of Loans	% of AA Owner Occupied Housing	% of Number of Loans	% of AA Owner Occupied Housing	% of Number of Loans	% of AA Owner Occupied Housing	% of Number of Loans
Residential	0.00	0.00	17.91	0.00	82.09	100.00	0.00	0.00

Source: Loan Sample; U.S. Census data.

**Responses to Complaints**

HNB has not received any CRA-related complaints during the evaluation period.

### **Fair Lending or Other Illegal Credit Practices Review**

Pursuant to 12 C.F.R. 25.28(c), or 12 C.F.R. 195.28(c), in determining a national bank's (bank) or Federal savings association's (FSA) CRA rating, respectively, the OCC considers evidence of discriminatory or other illegal credit practices in any geography by the bank or FSA, or in any assessment area by an affiliate whose loans have been considered as part of the bank's or FSA's lending performance.

We found no evidence of discriminatory or other illegal credit practices inconsistent with helping to meet community credit needs.