

PUBLIC DISCLOSURE

October 22, 2001

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

Falcon International Bank
RSSD #564557

5219 McPherson Road
Laredo, Texas 78041

Federal Reserve Bank of Dallas

2200 North Pearl Street
Dallas, Texas 75201

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.

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

The bank's performance under the CRA is rated Satisfactory based on its record of lending to borrowers of various income levels in its assessment area. Lending to businesses with annual revenues of one million dollars and less was significant. In addition, the dollar amounts of commercial loans reviewed were predominantly in amounts of \$100 thousand or less. Further, the sample distribution of loans to consumers who are classified as low- and moderate-income and those who reside in moderate-income geographies is considerable. Specifically, almost 93 percent of the commercial loans sampled were in amounts less than \$50 thousand. Bank management has demonstrated its commitment to meeting the needs of its community through the products offered as well as its participation in affordable housing loan programs targeted to low- and moderate-income borrowers.

DESCRIPTION OF INSTITUTION

As of June 30, 2001, Falcon International Bank, Laredo, Texas (Falcon) reported assets of \$177 million, with a net loan-to-deposit ratio of 84.66 percent. Falcon is owned by Falcon Bancshares, Inc. through its subsidiary bank holding company, Falcon Nevada, Reno, Nevada.

The main office, located at 5219 McPherson Road in Laredo, Texas, is a full service facility offering loan and deposit products. Real estate lending comprises approximately 72 percent of Falcon’s total portfolio, with consumer loans accounting for 19 percent of the bank’s total lending. The following table details the distribution of the bank’s loan portfolio as of the June 30, 2001, Consolidated Reports of Condition and Income (Call Report):

LOAN PORTFOLIO MIX	DOLLAR AMOUNT (IN THOUSANDS)	% OF LOANS
<u>Real Estate</u>		
Residential	36,979	26.98
Commercial	35,547	25.94
Construction/Land Development	18,495	13.49
Open-End Home Equity	3,079	2.25
Multifamily	3,561	2.60
Total Real Estate	<u>1,616</u>	<u>1.18</u>
	99,277	72.44
<u>Consumer</u>		
Open-End Credit	2,898	2.11
All Other	23,021	16.80
Total Consumer	25,919	18.91
Commercial/Industrial	7,505	5.48
Agricultural	85	0.06
State and Political	1,307	0.95
Other	2,963	2.16
Gross Loans	\$137,056	100.00 %

As the chart above illustrates, real estate lending dominates the bank’s loan portfolio, comprising 72 percent of the lending. Consumer lending represents the next largest percentage of loans, at almost 19 percent of the portfolio. The bank’s ability to meet various community credit needs has not been restricted by its capacity to lend, the capacity of other similarly-situated institutions to lend in the assessment area, demographic and economic factors present in the assessment area, or the lending opportunities available in the institution’s assessment area. Falcon International Bank’s CRA performance was evaluated by the Office of the Comptroller of the Currency on October 23, 1997, at

which time the bank received an overall rating of “satisfactory”.

DESCRIPTION OF THE ASSESSMENT AREA

Falcon has designated Laredo, TX MSA 4080, which includes Webb County, and the north central corridor of San Antonio in Bexar County, Texas, as its assessment areas (AA). The assessment area has changed since the previous compliance examination, because of the addition of a branch location, to include the section of Bexar County.

The bank’s main office is located in Laredo, Texas. Falcon ranked sixth of the seven FDIC-insured institutions in Webb County, in total deposits with \$124.8 million and holds 3.53 percent market share of deposits as of June 30, 2000. Laredo National Bank ranks first in share of deposits with 41 percent, followed by International Bank of Commerce and Wells Fargo Bank Texas, N.A. with 33 percent and eight percent, respectively. There were a total of 218 banking offices in Bexar County; however, Falcon’s branch was not opened until September, 2001, so no ranking in that portion of the assessment area is available. The bank identified International Bank of Commerce, Laredo National Bank, South Texas National Bank, Commerce Bank, NBC Bank, and Well Fargo Bank Texas, N.A. as its major competitors.

The following table details the bank’s five branch offices:

BRANCH/ NUMBER	ADDRESS	CENSUS TRACT	COUNTY	HOURS	TELEPHONE
Main 01 Drive-Thru	5219 McPherson Road Laredo, TX 78041	0016.00	Webb	M – F 9am to 5pm M – F 9am to 5pm Sat 9am to 1pm	956.723.2265
Downtown 02 Drive-Thru	801 Matamoros Street Laredo, TX 78040	0004.00	Webb	M – F 9am to 5pm M – F 8am to 6pm Sat 9am to 1pm	956.723.9855
East 03* Drive-Thru	204 Bob Bullock Loop Laredo, TX 78043	0018.02	Webb	M – F 9am to 5pm M – F 8am to 6pm Sat 9am to 1pm	956.723.2265
North 04* Drive-Thru	7718 McPherson Road Laredo, TX 78045	0016.00	Webb	M – F 9am to 5pm M – F 8am to 6pm Sat 9am to 1pm	956.723.2265
San Antonio 05* Drive-Thru	19230 Stone Oak Parkway San Antonio, TX 78258	1918.02	Bexar	M – F 9am to 5pm M – F 7am to 7pm Sat 8am to 12pm	210.402.6143

*New locations since 1997 exam

The United States Census Bureau divides metropolitan areas into statistical subdivisions called census tracts (CTs). Various information, including population, race, household composition, education, employment and income statistics, are available for each census tract. Demographic and economic information impact the bank's performance context, and are discussed below. Information was obtained from publicly available sources including the U.S. Department of Commerce's Bureau of the Census for 1990, the U.S. Department of Labor, the U.S. Department of Housing and Urban Development, and the Texas Workforce Commission.

DEMOGRAPHIC INFORMATION (1990)	LAREDO MSA 4080	BEXAR COUNTY
Population	133,239	209,086
Number of Families	29,735	56,972
Percent Low-Income Families	24.6	9.9
Percent Moderate-Income Families	16.7	11.2
Percent Middle-Income Families	16.5	17.1
Percent Upper-Income Families	42.2	61.7
Percent of Families Below Poverty Level	33.1	5.5
Number of Housing Units	37,197	92,975
Percent Owner-Occupied	56.2	47.5
Percent of Housing Rented	36.4	43.3
Median Housing Value	\$48,802	\$90,462

MSA 4080 – Laredo, TX

Demographic Characteristics

MSA 4080 consists of Webb County, located in south Texas along the Rio Grande River, the principal port of entry into Mexico. According to the 1990 census, the total population of the MSA is 133,239, representing an increase of 45 percent from 1990 to 2000 to an estimated population of 193,117. Approximately 91 percent of the population reside in the city of Laredo. Other cities in the MSA include Bruni, Mirando City and Oilton.

Income Characteristics

The 1990 median family income for MSA 4080 is \$19,527, compared to \$31,553 for the state. The 2000 HUD-adjusted median family income for Webb County is \$31,300. The assessment area contains 24 populated census tracts; none of the tracts are low-income. Of the tracts, 11 or 45.9 percent are moderate-income, eight or 33.3 percent are middle-income, and five or 20.8 percent are upper-income tracts. There are 29,735 families in the assessment area. The majority of families in the

AA, 42 percent, are classified as upper-income. Twenty-five percent of the families are low-income, 17 percent are moderate-income, and 16 percent are middle-income families. Approximately 33 percent of the low-income families are living below the poverty level, compared to 14 percent statewide. Approximately 40 percent of total families reside in moderate-income tracts. Middle-income tracts contain 28 percent of assessment area families, and 31 percent of families are in upper-income tracts. The following table illustrates the distribution of the population by census tract income level:

DISTRIBUTION OF POPULATION BY CENSUS TRACT INCOME LEVEL						
Census Tract Income Level	Total Tracts		Total Families		Total Population	
	#	%	#	%	#	%
Low income	0	0	0	0	0	0
Moderate income	11	45.9	11,993	40.3	57,324	43.0
Middle income	8	33.3	8,433	28.4	37,241	28.0
Upper income	5	20.8	9,309	31.3	38,674	29.0
TOTAL	24	100.0%	29,735	100.0%	133,239	100.0%

Housing Characteristics

There are 37,197 total housing units in the assessment area. Owner occupancy in the assessment area is at 56.2 percent. The state owner-occupancy percentage is 52.7 percent. Rental units comprise 36.4 percent of all housing units in the assessment area.

The 1990 median housing value is \$48,802 and median gross rent is \$314. Seventy-eight percent of assessment area housing units are single-family, ten percent are multi-family units housing five or more families, and 10 percent are mobile homes. Forty-one percent of the housing units are located in moderate-income, 27.8 percent in middle-income, and 31.2 percent in upper-income tracts. The distribution of the 20,902 owner-occupied units by tracts is 39.7 percent moderate, 29 percent middle, and 31.3 percent upper.

The median age of the assessment area housing stock is 25 years, with only 17.2 percent of units built prior to 1950. The oldest homes are located in moderate-income tracts, where the median age is 37 years, compared to 23, and 17 years in the middle- and upper-income tracts, respectively.

Labor, Employment and Economic Characteristics

The trade and services sectors rank first and second in terms of employment in the Laredo employment market. The area’s third largest employment sector is transportation, communication and public utilities.

The trade sector makes up 25 percent of nonagricultural employment in the area. Retail and wholesale trade constitute a large portion of employment as a result of trade with neighboring Mexico.

The service sector accounts for 21 percent of the area's nonagricultural employment. Health care is the largest industry in the services sector. Mercy Hospital of Laredo and Columbia Doctors Hospital are two major employers. Local government generates 18 percent of employment, while federal government contributes three percent and state government makes up two percent of the workforce. Education ranks among Laredo's top ten public employment sectors. Three educational facilities, United Independent School District (ISD), Laredo ISD and Texas A&M International University, are included among the area's top employers. Manufacturing provides only 2.6 percent of all nonagricultural MSA jobs. This percentage is lower than that of most Texas MSAs because of the influence of the maquiladoras in nearby Nuevo Laredo, Mexico.

Several businesses, including ConvergysCorp, Home Depot, Smithers Scientific and M.S. Carriers, either moved to Laredo or expanded existing operations to create more than 1500 jobs since 2000. In September 2000, the city of Laredo and Webb County received \$16.7 million in grants and loans to help bring water and sewage service to 787 households in 15 area colonias.

MSA 7240 – San Antonio, TX (North central corridor-portion of Bexar County)

Demographic Characteristics

San Antonio is the eighth largest city in the United States and one of the fastest growing metropolitan areas in the country. It is located in south central Texas along the I-35 corridor, the fastest growing region of the state. MSA 7240 consists of Bexar, Comal, Guadalupe and Wilson Counties. The bank selected 39 census tracts in Bexar County as its assessment area. According to the 1990 census, the total population of the assessment area is 209,086.

Income Characteristics

The 1990 median family income for the assessment area is \$44,112 compared to \$31,553 for the state.

The 2000 HUD-adjusted median family income for MSA 7240 is \$43,100. This portion of the assessment area contains 39 populated census tracts, none of which are low-income. Only two or 5.1 percent of the tracts are moderate-income, eight or 20.5 percent are middle-income, and 29 or 74.4 percent are upper-income tracts. There are 56,972 families in the assessment area. The majority of families in the assessment area, almost 62 percent, are classified as upper-income. Approximately 17 percent of the families are middle-income, 11 percent moderate-income and 10 are low-income. Approximately 5.5 percent of the moderate-income families are living below the poverty level, compared to 14 percent statewide. Approximately 3.3 percent of total families reside in moderate-

income tracts. Middle-income tracts contain 21.6 percent of assessment area families, and the remaining 75.1 percent are residing in upper-income tracts. The following table illustrates the distribution of the population by census tract income level:

DISTRIBUTION OF POPULATION BY CENSUS TRACT INCOME LEVEL						
Census Tract Income Level	Total Tracts		Total Families		Total Population	
	#	%	#	%	#	%
Low income	0	0	0	0	0	0
Moderate income	2	5.1	1,907	3.3	8,307	4.0
Middle income	8	20.5	12,291	21.6	49,350	23.6
Upper income	29	74.4	42,774	75.1	151,429	72.4
TOTAL	39	100.0%	56,972	100.0%	209,086	100.0%

Housing Characteristics

There are 92,975 total housing units in the assessment area. Almost 48 percent of the houses are owner-occupied. The state owner-occupancy percentage is 52.7 percent. Rental units comprise 43.3 percent of all housing units in the assessment area.

The 1990 median housing value is \$90,462 and median gross rent is \$431. Almost sixty-four percent of assessment area housing units are single-family, 35 percent are multi-family units housing five or more families, and approximately one percent are mobile homes. About 66 percent of assessment area housing units are located in upper-income, 29 percent in middle-income, and five percent in moderate-income tracts. The distribution of the 44,159 owner-occupied units by tract is 86 percent upper, 13 percent middle, and less than one percent moderate.

The median age of the assessment area housing stock is 30 years, with only 0.8 percent of units built prior to 1950. The oldest homes are located in upper-income tracts, where the median age is 30 years, compared to 27, and 17 years in the moderate and middle-income tracts, respectively.

Labor, Employment and Economic Characteristics

The services sector added the most jobs – 7,900 – to the San Antonio economy in 2000, and accounts for the largest share of San Antonio’s workforce, 32 percent. Trade follows closely with 25 percent of area employment. The trade sector added 4,600 jobs in 2000. Government is the third largest sector, accounting for 19 percent of area employment.

Health care makes up the largest portion of employment in the San Antonio area. USAA, a major insurance company serving military personnel all over the world, expanded by constructing a new headquarters. The military has a strong presence in the San Antonio area, with four Air Force bases (AFB) and Fort Sam Houston employing 67,896 people. A decline in government employment has occurred over the past year because of Kelly AFB's closing and layoffs at Brooks AFB. The government sector lost 1,300 jobs during 2000. Manufacturing added 800 jobs in 2000.

In Bexar County, nursery products and beef represent 59 percent and 15 percent, respectively of agricultural receipts according to the Texas Agricultural Extension Service. The Bexar Metropolitan Water District opened a \$30 million water treatment plant in southwest San Antonio in December 2000.

Industrial expansion has been occurring on the north and northwest portions of San Antonio. Retail expansion has occurred on the north and south sectors of the city. Single-family residential growth has been strong since 1993 and is projected to continue to be strong in the northwest area. Residential growth in the north central section is expected to be stronger in the future. The downtown area continues to serve the tourism industry with a mix of hotels and retail establishments.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

LOAN-TO-DEPOSIT RATIO

The bank’s loan-to-deposit ratio is excellent. As of June 30, 2001, the net loan-to-deposit ratio was 84.66 percent, compared to 68.77 percent as of the same date in 2000. The quarterly average ratio since the previous examination is 73.93 percent. UBPR data indicates national peer banks reported a 77.24 percent ratio as of June 30, 2001.

The following chart compares Falcon’s loan-to-deposit ratios with similarly situated financial institutions in Webb County. Bank management identified International Bank of Commerce, Laredo National Bank, South Texas National Bank, Commerce Bank, NBC Bank, and Wells Fargo branch locations, as some of their primary competitors. Most of the identified banks are not similar in size; however, the banks do have a strong presence in the community and are the bank’s most likely competitors. Commerce Bank, Laredo; South Texas National Bank, Laredo; and Laredo National Bank, Laredo, were selected due to their proximity to Falcon.

BANK	COUNTY	TOTAL ASSETS JUNE 30, 2001	LTD RATIO JUNE 30, 2001	QUARTERLY AVG. LTD RATIO
Falcon International Laredo, Texas	Webb	\$177,087	84.66%	73.93%
South Texas National Bank Laredo, Texas	Webb	\$327,343	48.01%	46.19%
Laredo National Bank Laredo, Texas	Webb	\$2,272,526	63.18%	52.56%
Commerce Bank Laredo, Texas	Webb	\$240,542	39.66%	38.65%

As the chart above illustrates, Falcon has a considerably higher loan-to-deposit ratio when compared with other local institutions. Although all of the banks are larger in asset size than Falcon, they have similar distributions in terms of the major loan products in their portfolios. A comparison of the ratios indicates that Falcon’s ratio exceeds the other local banks. The bank exceeds the requirements for satisfactory performance in this category.

LENDING IN ASSESSMENT AREA

Of the loans included in the sample, only two commercial loans and two motor vehicle loans were originated in the assessment area portion of the San Antonio MSA. Additionally, the San Antonio branch has been open only since September 2001. Therefore, the analysis of lending is conducted with a focus on the demographic data for the Laredo MSA.

The bank’s performance in this category is indicative of a good response to the credit needs of the assessment area (AA). The review of loans encompassed an initial sample of 34 commercial, 57 motor vehicle, and 32 residential loans originated during the period of June 1, 2000 and December 31, 2000.

Of the loans included in the sample, several loans were missing income and/or address data and were excluded from the analysis.

As the chart below illustrates, the percentage of all loan types originated inside the AA is 90 percent. Commercial loans were notable as 100 percent of them were inside the bank’s service area. Motor vehicle loans represented 88 percent of the number and 93 percent of the dollar amount of loans made in the bank’s AA. Eighty-three percent of the number and 84 percent of the dollar amount of residential loans were originated in the bank’s chosen market.

ANALYSIS OF LENDING IN THE ASSESSMENT AREA								
Loan Type	Inside Assessment Area				Outside Assessment Area			
	#	% of #	\$	% of \$	#	% of #	\$	% of \$
Commercial	29	100	1,051,433	100	0	0	0	0
Motor Vehicle	46	88	425,571	93	6	12	31,333	7
Residential	25	83	1,915,898	84	5	17	361,700	16
TOTAL*	100	90%	3,392,902	90.0%	11	10%	393,033	10.0%

*excludes 12 loans with addresses which could not be geocoded

LENDING TO BORROWERS OF DIFFERENT INCOMES AND TO BUSINESSES OF DIFFERENT SIZES

Falcon’s distribution of loans and its record of lending to low- and moderate-income borrowers in the AA is good and reflects an adequate penetration. The distribution of small business loans by gross annual revenue data and loan size indicate bank management is endeavoring to meet the credit needs of small businesses. As the chart below indicates, all loans in the sample were for amounts less than \$250 thousand. Approximately 93 percent of the loans originated were in amounts less than \$50 thousand. The majority of loans originated for small business purposes were made based on borrower income levels rather than gross annual revenues. Of those loans, one loan was made to a borrower classified as

moderate-income.

DISTRIBUTION OF COMMERCIAL LOANS BY GROSS ANNUAL REVENUES AND LOAN SIZE						
GROSS ANNUAL REVENUES (\$000s)	LOAN AMOUNT				TOTAL	
	LESS THAN \$50,000	\$50,000 - <\$100,000	\$100,000 - < \$250,000	\$250,000 AND UP		
Less than \$50	0	0	0	0	0	0%
\$50 – less than \$100	2	0	0	0	2	7.41%
\$100 and up	6	1	1	0	8	29.63%
Borrower Income	17	0	0	0	17	62.96%
Total*	25	1	1	0	27	100%

*excludes 2 loans without income information

The analysis indicates the bank is addressing a need often expressed by small business owners for small dollar loans. With an overwhelming majority of loans in amounts less than \$50 thousand, the bank is providing a loan product that many banks indicate will not meet the bank’s profitability profile.

The analysis of lending to borrowers of varying income levels was performed using HUD’s annually adjusted median family income for the Laredo MSA. The table below indicates the 2000 income level ranges based on median income of \$31,300:

LAREDO, TEXAS MSA 4080 – MEDIAN FAMILY INCOME \$31,300	
Income Level	2000
Low-income	\$0 - <\$15,650
Moderate-income	\$15,650 - <\$25,040
Middle-income	\$25,040 - < \$37,560
Upper-come	\$37,560 and up

The chart below details the distribution of the motor vehicle and residential loans sampled by income of the borrowers, with the percent of area families in each income bracket provided for comparison.

Because 33 percent of families in the AA are categorized as living below the poverty level, the ability to provide financing for low- and very low-income members of the community is challenging. The capability to provide mortgage loans, especially, is almost impossible, according to community contacts without subsidies of some sort. The community contacts interviewed during this assessment said the housing and land costs in the MSA are expensive and often preclude low-income people from becoming home owners. The bank’s ability to provide mortgage loan products targeted to borrowers who have been under-served in the community indicates a commitment to meeting an identified need.

DISTRIBUTION OF LOANS BY MEDIAN FAMILY INCOME LEVEL					
	LOW	MODERATE	MIDDLE	UPPER	TOTAL
Motor Vehicle					
Number of Loans	5	7	18	13	43
% of Number	12	16	42	30	100%
Dollar Volume	\$39,139	\$76,742	\$123,996	\$109,927	\$349,804
% of Dollar Volume	11	22	36	31	100%
1-4 Family Residential					
Number of Loans	0	2	4	16	22
% of Number	0	9	18	73	100%
Dollar Volume	\$0	\$36,100	\$283,033	\$1,340,765	\$1,659,898
% of Dollar Volume	0	2	17	81	100%
Percent of Families	24.6	16.7	16.5	42.2	100%

The distribution of motor vehicle and residential loans is acceptable and reflects an effort by bank management to reach all income levels of its assessment area. Of the motor vehicle loans originated, 11 percent and 16 percent of the number of loans were made to low- and moderate-income borrowers, respectively. Nine percent of the residential loans sampled were provided to moderate-income borrowers. Although the sample did not include any loans to low-income borrowers, bank management provided mortgage loan data indicating a substantial portion of its portfolio consists of affordable housing loans. The bank partners with a local affordable housing lender to ensure mortgage loans are available to members of the community whose income levels would not normally qualify for a home loan. Further, the bank not only provides financing for those affordable mortgages, but also provides down payment assistance, and members of bank staff participate in home ownership counseling seminars.

GEOGRAPHIC DISTRIBUTION OF LOANS

To analyze the bank's lending distribution among the income levels in the bank's AA, a review of the distribution of loans was conducted in relation to the census tract income levels. The bank's AA's do not have low-income tracts. In the Laredo AA, moderate-income tracts comprise almost 46 percent of the geographies, with 33 percent of the tracts middle-income and almost 21 percent upper-income. A majority of the families, slightly more than 40 percent, reside in moderate-income tracts, while 28 percent and 31 percent are in middle- and upper-income tracts, respectively. The chart below details the distribution of tracts, families, and total population in the bank's AA.

DISTRIBUTION OF POPULATION BY CENSUS TRACT INCOME LEVEL						
Census Tract Income Level	Total Tracts		Total Families		Total Population	
	#	%	#	%	#	%
Low income	0	0	0	0	0	0
Moderate income	11	45.9	11,993	40.3	57,324	43.0
Middle income	8	33.3	8,433	28.4	37,241	28.0
Upper income	5	20.8	9,309	31.3	38,674	29.0
TOTAL	24	100.0%	29,735	100.0%	133,239	100.0%

Overall, 27 percent of the loans reviewed were in moderate-income tracts, with 36 percent in middle-income tracts, and 37 percent in upper tracts, as indicated in the chart below. Small business loans accounted for the largest percentage of loans in moderate-income tracts, with 34 percent in those geographies. The bank's distribution overall and by individual products is acceptable and meets the standards for satisfactory performance in this category. The bank's lending in moderate-income tracts for the loan products reviewed is sufficient, given the composition of the AA.

DISTRIBUTION OF LENDING BY CENSUS TRACT INCOME LEVEL								
INCOME LEVEL	SMALL BUSINESS		MOTOR VEHICLE		RESIDENTIAL		TOTAL	
	#	%	#	%	#	%	#	%
Low	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Moderate	10	34	11	24	6	24	27	27
Middle	8	28	17	37	11	44	36	36
Upper	11	38	18	39	8	32	37	37
TOTAL	29	100%	46	100%	25	100%	100	100%

RESPONSE TO COMPLAINTS

The bank has not received any CRA-related complaints since the previous evaluation.

COMPLIANCE WITH ANTI-DISCRIMINATION LAWS (ECOA, FHA OR HMDA)

No violations of the substantive provisions of the anti-discrimination laws and regulations were identified during the concurrent Consumer Affairs Examination.