

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION PUBLIC DISCLOSURE

Texas Heritage Bank	500 Highway 79 West
_____ Name of Institution	_____ Street
Hutto	Williamson
_____ City	_____ County
Texas	78634
_____ State	_____ Zip Code
Sharon D. Ford	
_____ Examiner-in-Charge	

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CRA PERFORMANCE ASSESSMENT

GENERAL INFORMATION

The Community Reinvestment Act (CRA) requires each federal financial supervisory agency to use its authority when examining financial institutions subject to its supervision, to assess the institution's record of meeting the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound operation of the institution. Upon conclusion of such examination, the agency must prepare a written evaluation of the institution's record of meeting the credit needs of its community.

*This document is an evaluation of the Community Reinvestment Act (CRA) performance of **Texas Heritage Bank, Hutto, Texas**, prepared by **Federal Reserve Bank of Dallas, Dallas, Texas**, the institution's supervisory agency, as of January 26, 1998. The agency rates the CRA performance of an institution consistent with the provisions set forth in Appendix A to 12 CFR Part 228.*

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

Overall, the bank facilitates economic development and growth throughout the assessment area to borrowers of different income levels and businesses of different revenue sizes. The bank's quarterly loan-to-deposit ratio of 65.4% exceeded the average of its three primary competitors and seven similarly-situated banks by an exceptional 8 and 11 percentage points, respectively. Approximately 95% of the commercial and consumer loan sample were made inside the assessment area. Analysis of the loan sample revealed a satisfactory distribution of loans throughout the assessment area, as 56% of the consumer loans were made to low- and moderate-income individuals and 50% of the business loans were made to businesses with gross revenues of \$1 million or less.

DESCRIPTION OF INSTITUTION

Texas Heritage Bank, Hutto, Texas (Heritage), is an independent, retail bank that is a wholly-owned subsidiary of Heritage Bancorp, a one-bank holding company located in Hutto, Texas. Heritage's main office is located at 500 Highway 79 West, Hutto, Texas. The bank has a total of four branch locations, one in each of the following cities: Austin, Cedar Park, Georgetown, and Roundrock. The main office and the Cedar Park, Georgetown, and Roundrock branches are located in Williamson County, while the Austin branch is located in Travis County. The main office and the Austin, Cedar Park, and Roundrock branches are located in middle-income census tracts, while the Georgetown branch is located in a low-income census tract. All of the bank's locations offer a full line of loan and deposit products, banking services, and convenient banking hours. The main office and the Austin, Cedar Park, and Roundrock branches also provide drive-through facilities and ATMs.

As of September 30, 1997, the bank reported total assets of \$57 million. Net loans and leases represented 67.6% of total deposits. As indicated in the following chart, Heritage has a primary and increasing lending emphasis in real estate-related loans.

The asset distribution by loan type is as follows as of September 30, 1997:

LOAN TYPE	DOLLAR AMOUNT (THOUSANDS)	PERCENT OF TOTAL LOANS
Real Estate:		
Construction	\$4,983	13.83
Residential 1-4 Family	4,311	11.96
Commercial	8,328	23.11
Agricultural	2,880	7.99
Total Real Estate	20,502	56.89
Consumer:		
All other	7,599	21.09
Commercial and Industrial	7,535	20.91
Agricultural	251	0.70
Other	148	0.41
Total Loans	\$36,035	100.00%

Overall, the bank's ability to meet community credit needs has not been hampered by its capacity to lend, the capacity of other similarly-situated institutions to lend in the assessment area, demographic or economic factors present in the assessment area, or the lending opportunities available in the assessment area.

DESCRIPTION OF WILLIAMSON AND TRAVIS COUNTIES

The bank has identified its assessment area as Williamson and Travis Counties, which are part of the Austin-San Marcos Metropolitan Statistical Area (Austin-San Marcos MSA). These two counties are centrally located in the region of the state of Texas referred to as the "Texas Hill Country," which is known for its beautiful hills and lakes, scenic spring wildflowers, and vast recreational, vacation, and tourist destinations. The bank's main office is located in the community of Hutto, Texas, which lies in the southern portion of Williamson County and in the high-growth, northeast corridor of Austin, Texas.

This area has been experiencing a high rate of growth in recent years due to the growing prominence of the high-technology, semi-conductor, computer, and telecommunication industries. The passage of the North American Free Trade Agreement in 1993 in conjunction with the area's close proximity to Mexico and United States Interstate Highway 35, which runs from Mexico to Canada and travels through the Texas Hill Country, has also lead to increased manufacturing and distribution-related economic activity. President and Chief Executive Officer James Shields indicated that both Williamson and Travis Counties economies are being primarily driven by these growing industries and lack the level of diversification of other major metropolitan areas in the state such as Dallas or Houston. While the local economies of Cedar Park, Georgetown, and Roundrock are closely tied to the regional economy of the Austin-San Marcos MSA, these cities have been quickly transformed from being merely bedroom communities to cities having vibrant, diverse, and growing economies with greater depth and less economic interdependence. In consideration of the bank's asset size and the location of its offices, the majority of the bank's lending appears to be concentrated in the high growth, northeast corridor of Austin including these two counties.

According to President and Chief Executive Officer James Shields, bank management anticipated and planned for this high growth by establishing and expanding its relatively large branch network, loan administration and operation departments, and number of employees in this area shortly after the bank was acquired. He indicated that the Austin, Cedar Park, Georgetown, and Roundrock markets are experiencing strong loan demand, while the Hutto market has experienced slower growth as it lies outside the high-growth corridor and its economy is primarily agricultural in nature. The development of the proposed Texas Highway 131, along with continued growth to the northeast from Austin and Roundrock towards Hutto should spread the economic growth and development to this community in the near future.

Two community contacts interviewed in Cedar Park and Georgetown both indicated that the area was experiencing strong economic growth, particularly in the commercial and industrial and residential real estate markets and the high technology, telecommunications, electronics, manufacturing, and distribution industries. It was noted that Williamson County is the fastest growing county in the state of Texas, among the top three fastest growing counties in the country, and reported a 1.7% unemployment rate as of year-end 1997. The community contact in Georgetown noted that single- and multi-family affordable housing for low- and moderate-income individuals were needed due to the high cost of construction and minimum subdivision lot size restrictions of 6,000 square feet. It appears that this credit need is being recognized and somewhat addressed by the public and private sectors, as the number of apartments has doubled in the past three years and the minimum lot size restrictions are in the process of being lowered. The community contact in Cedar Park noted that commercial property financing was needed for retail/strip centers, office buildings, and warehouses due to strong demand and a tight supply for these types of buildings. Also, private sector financial participation in the proposed creation and development of a downtown district in Cedar Park would help spur additional economic development in the city.

Overall, it appears that there are numerous opportunities for the bank to participate in community development and other credit-related programs, particularly involving affordable housing and commercial property development and acquisition lending. It is anticipated that continued population growth will generate additional credit needs for affordable housing, small business, home improvement, and consumer loans in these two communities in the long-term.

Analysis of the Census data indicates that the population in Williamson and Travis Counties is generally more affluent and slightly younger in comparison to the state of Texas (state) metropolitan areas' population as a whole. The 1990 Census combined median family income (MFI) for the assessment area was \$36,466, in comparison to the state metropolitan MFI of \$31,553. Low- and moderate-income families represented 36.7% of the total population in Williamson and Travis Counties, in comparison to 39% for low- and moderate-

income families residing in metropolitan areas throughout the state. Of the total 36.7% figure, low-income families represented 19.8% and moderate-income families represented 16.9% of the total population in the assessment area. Further analysis of the low-income segment of the population living in the two counties found that 9.6% lived below the poverty level in relation to the 14.1% figure for state metropolitan areas. Approximately 40% of the population are aged 24 years or younger, 53% are aged 25-64 years, and 7% are aged 65 years or older for the two counties. Comparable figures for the state metropolitan areas were 39%, 51%, and 10%, respectively.

The Department of Housing and Urban Development (HUD) updates MFI on an annual-basis and reports the 1997 Austin-San Marcos MFI at \$48,600. For CRA purposes, borrower income information is based upon this figure. Refer to the Income Category chart in Lending to Borrowers of Different Incomes and to Businesses of Different Sizes section for specific definitions of income categories.

Of the 210 census tracts (CTs) comprising the bank's assessment area, they appeared to be fairly evenly distributed among the four income categories, as 20% were low-income CTs, 23% were moderate-income CTs, 31% were middle-income CTs, and 25% were upper-income CTs. However, analysis of the population distribution among the four income categories found that the majority resided in middle- and upper-income CTs, as 7% lived in low-income CTs, 26% lived in moderate-income CTs, 37% lived in middle-income CTs, and 30% lived in upper-income CTs. Based upon this information, one would anticipate a relatively lower level of lending in low- and moderate-income CTs and a higher level of lending in middle- and upper-income CTs.

Further analysis of the 1990 Census data reveals a strong housing market based upon a 11.6% vacancy rate, a median housing value of \$75,938, gross median monthly rent of \$419, and an affordability ratio of 37.8%, all of which exceed the Austin-San Marcos MSA and state metropolitan figures. Additionally, 43.2% of the homes are owner-occupied and 45.1% are rental properties, in comparison to the state metropolitan figures of 52.7% and 33.9%, respectively. Approximately 9.4% of the homes in the assessment area were built prior to 1950, in comparison to the state metropolitan area figure of 14.4%. While the local housing stock appears to be newer and generally in good condition, it appears that the need for affordable loans, in particular for low- and moderate-income individuals, noted by the community contact interviewed in Georgetown has been in existence since at least the early 1990's.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA:

Loan To Deposit Ratio

The institution's loan-to-deposit (LTD) ratio is considered satisfactory in light of its performance context, which includes the institution's capacity to lend in the assessment area, demographic and economic factors present in the assessment area, and the lending opportunities available in the institution's assessment area.

As of September 30, 1997, the bank's net loans represented 67.6% of total deposits, which fell slightly below the national peer level of 71.1%. Heritage's quarterly-average LTD ratio since the last examination of 65.4% was compared with seven banks operating within the assessment area in order to obtain a more meaningful comparison and more accurately assess the bank's performance. These seven banks were considered to be similarly-situated institutions based upon their similar asset sizes, loan portfolio mixes, loan growth patterns, management's contention that three of the banks were primary competitors of Heritage, and other factors. Heritage's quarterly-average LTD ratio of 65.4% exceeded the 57.8% average of its three primary competitors and the 54.5% average of the seven similarly-situated banks by 8 and 11 percentage points, respectively, which was considered outstanding

and exceeded the standards for satisfactory performance.

QUARTERLY-AVERAGE LOAN-TO-DEPOSIT RATIO FROM MARCH 31, 1997 THROUGH SEPTEMBER 30, 1997		
TEXAS HERITAGE BANK	PRIMARY COMPETITORS	SIMILARLY-SITUATED BANKS
65.4%	57.8%	54.5%

Lending in Assessment Area

A substantial majority of the 61 consumer motor vehicle loans and 54 commercial loans made during the six-month period from June 1 through November 30, 1997 were made inside the bank's assessment area. Overall, 95% on a number-basis and 96% on a dollar-basis were made inside Williamson and Travis Counties. Analysis by each product type and summary totals on both a number- and dollar-basis are presented on the following two charts:

LENDING IN/OUT OF ASSESSMENT AREA ANALYSIS ON NUMBER-BASIS		
LOAN TYPE	% OF LOANS IN	% OF LOANS OUT
Motor Vehicle Loans	95%	5%
Commercial Loans	94%	6%
Total Loans	95%	5%

LENDING IN/OUT OF ASSESSMENT AREA ANALYSIS ON DOLLAR-BASIS		
LOAN TYPE	% OF LOANS IN	% OF LOANS OUT
Motor Vehicle Loans	98%	2%
Commercial Loans	96%	4%
Total Loans	96%	4%

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

Overall, the bank's distribution of consumer motor vehicle loans by borrower income and commercial loans by business revenue data were considered to be reasonable and met the standards for satisfactory performance.

Review of the consumer motor vehicle loan sample consisted of analyzing borrower income as a percentage of the 1997 Austin-San Marcos MSA MFI of \$48,600. A breakdown by income range for each income category is detailed below:

1997 AUSTIN-SAN MARCOS MSA MEDIAN FAMILY INCOME - \$48,600		
INCOME CATEGORY	INCOME RANGE AS A PERCENT OF MEDIAN	UPPER LIMIT OF RANGE
Low-Income	0-50%	\$24,300
Moderate-Income	51-80%	\$38,880
Middle-Income	81-120%	\$58,320
Upper-Income	121% and Above	Over \$58,320

Further comparison of the motor vehicle loan distribution was made using the percentage breakdown by income category of the families living within the assessment area based upon 1990 Census data as shown on the following table:

INCOME CATEGORY	PERCENT OF FAMILIES IN ASSESSMENT AREA
Low-Income	19.8%
Moderate-Income	16.9%
Middle-Income	22.4%
Upper-Income	40.9%
Total	100.0%

Analysis of the motor vehicle loan sample among the various income categories found a reasonable distribution pattern, as 56% of the loans were made to low- and moderate-income individuals in comparison to the 55% figure noted at the last examination. This level of lending exceeded the 37% figure of low- and moderate-income families living within the assessment area.

MOTOR VEHICLE LOAN SAMPLE IN ASSESSMENT AREA BY INCOME LEVEL				
NUMBER OF LOANS		INCOME CATEGORY	DOLLAR AMOUNT OF LOANS	
NUMBER OF LOANS BY INCOME OF APPLICANT	PERCENT OF TOTAL LOANS		NUMBER OF LOANS BY INCOME OF APPLICANT (THOUSANDS)	PERCENT OF TOTAL LOANS
13	29	Low-Income	\$ 50	15
12	27	Moderate-Income	99	29
8	18	Middle-Income	63	19
12	26	Upper-Income	124	37
45	100%	Totals	\$336	100%

Analysis of the commercial loans among the various income categories also appeared satisfactory, as 50% of the commercial loans with revenue data were made to small businesses with gross annual revenues of \$1 million or less.

COMMERCIAL LOAN SAMPLE IN ASSESSMENT AREA BY INCOME LEVEL				
NUMBER OF LOANS		GROSS REVENUES (THOUSANDS)	DOLLAR AMOUNT OF LOANS	
NUMBER OF LOANS BY INCOME OF APPLICANT	PERCENT OF TOTAL LOANS		NUMBER OF LOANS BY INCOME OF APPLICANT (THOUSANDS)	PERCENT OF TOTAL LOANS
4	10	\$100 Or Less	\$ 40	2
5	13	\$101 to \$250	189	11
6	15	\$251 to \$500	341	20
2	5	\$501 to \$750	63	4
3	7	\$751 to \$1,000	215	12
20	50	Over \$1,000	900	51
40	100%	Totals	\$1,748	100%

Further analysis of the commercial loan sample by dollar amount found that the bank is making a

considerable amount of small dollar business loans. As shown on the following chart, 53% of the commercial loans made inside the bank's assessment area were for amounts of \$25,000 or less. This further substantiates management's willingness and efforts to help meet the community's credit needs, in particular for small dollar business loans.

COMMERCIAL LOANS IN ASSESSMENT AREA BY DOLLAR AMOUNT		
DOLLAR LEVEL CATEGORY	NUMBER	PERCENT OF TOTAL
\$10,000 Or Less	11	22
\$10,001 - \$25,000	16	31
\$25,001 - \$50,000	11	22
\$50,001 - \$100,000	12	23
Above \$100,000	1	2
Totals	51	100%

Geographic Distribution of Loans

Review of the motor vehicle and commercial loan sample consisted of analyzing the bank's geographical lending dispersion among the various CTs income categories in comparison to the distribution of CTs by income level and the distribution of the population residing in Williamson and Travis County.

The following table depicts the distribution of the 210 CTs comprising the bank's assessment area by income level, which appears to show some similarity in the number of CTs among the four income categories:

DISTRIBUTION OF CTs WITHIN ASSESSMENT AREA BY INCOME LEVEL		
INCOME CATEGORY	NUMBER	PERCENT OF TOTAL
Low-Income	42	20
Moderate-Income	49	23
Middle-Income	66	32
Upper-Income	53	25
Totals	210	100%

The distribution of the population by CT income category in the two counties, as shown below, appears to be slightly disproportionate, as only 7% of the population reside in low-income CTs while 37% reside in middle-income CTs and 30% reside in upper-income CTs.

POPULATION DISTRIBUTION WITHIN ASSESSMENT AREA BY CT INCOME LEVEL (% OF TOTAL)		
INCOME CATEGORY	NUMBER	PERCENT OF TOTAL
Low-Income	53,804	7
Moderate-Income	184,498	26
Middle-Income	262,565	37
Upper-Income	215,091	30
Totals	715,958	100%

The bank's geographical pattern of lending of the motor vehicle and commercial loans made inside the assessment area appeared to be reasonable, as 14% of the commercial loans and 10% of the motor vehicle loans were made in low- and moderate-income CTs. On an overall-basis, 12% of the loans were made in low- and moderate-income CTs, while 71% were made in middle-income CTs. Although this geographical lending pattern appears disproportionate, it is considered reasonable based upon the

following factors: the majority of CTs in the assessment area are middle- and upper-income CTs; the majority of the population reside in middle- and upper-income CTs; and, no apparent gaps were noted in the bank's lending dispersion throughout the assessment area.

LOAN SAMPLE IN ASSESSMENT AREA BY CT INCOME CATEGORY				
INCOME CATEGORY	COMMERCIAL LOANS		MOTOR VEHICLE LOANS	
	LOANS IN CT INCOME CATEGORY	PERCENT OF TOTAL LOANS BY LOAN TYPE	LOANS IN CT INCOME CATEGORY	PERCENT OF TOTAL LOANS BY LOAN TYPE
Low-Income	2	4	4	7
Moderate-Income	5	10	2	3
Middle-Income	37	73	40	69
Upper-Income	7	14	12	21
Totals	51	100%	58	100%

RESPONSE TO COMPLAINTS

The institution has not received any written complaints about its CRA performance since the last examination.

COMPLIANCE WITH ANTIDISCRIMINATION LAWS (ECOA, FHA, OR HMDA)

No violations involving illegal discrimination or discouragement were noted during the examination.