



SMALL BANK

Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

PUBLIC DISCLOSURE

May 5, 2008

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

Zapata National Bank
Charter Number: 14955

7th and Hidalgo
Zapata, TX 78076

Office of the Comptroller of the Currency

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

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.

Zapata National Bank's (ZNB) lending performance reflects a satisfactory response to community credit needs in its assessment area (AA). Factors that support the overall rating include:

- The average loan-to-deposit (LTD) ratio of 37 percent over the prior 23 quarters is reasonable given the bank's size, financial condition, market focus, competition, and lending opportunities in the AA.
- A substantial majority of our sample of loans, 93 percent of the number and 92 percent of the dollar volume, originated within the AA of the bank.
- 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

ZNB 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 AA through its lending activities.

Our examination scope covered the time period from September 30, 2002, the date of the prior Performance Evaluation, to May 5, 2008, the as of date for the current examination. We identified residential, commercial, and consumer loans to be the bank's primary loan products originated from September 30, 2002 through March 31, 2008. To evaluate ZNB's lending performance, we selected a sample of 60 loans originated during this time period. The sample consisted of 20 loans each for the 3 primary loan products identified.

DESCRIPTION OF INSTITUTION

ZNB is an intrastate bank headquartered in Zapata, Texas. ZNB was chartered in 1961 and is a wholly owned subsidiary of Zapata Bancshares, Inc., a one-bank holding company. As of March 31, 2008, ZNB had total assets of \$96 million and Tier One Leverage Capital of \$7.4 million. The bank's one office consists of a walk-in teller lobby, a drive-up motor bank, and an automated teller machine (ATM). There is also a remote ATM located a few miles north from the bank along the main highway in the AA. ZNB is a full-service bank and is the only independently owned community bank within the AA. There is one other bank in the AA; however, it is a branch of a larger state bank headquartered outside of the AA.

As of March 31, 2008, ZNB reported net loans of \$28 million and had a net loans and leases to total assets ratio of 29 percent. The loan portfolio composition is as follows:

| Loan Portfolio Summary by Loan Product March 31, 2008 | |
|--|---------------------------------|
| Loan Category | % of Outstanding Dollars |
| Residential | 48.30 |
| Commercial | 32.14 |
| Consumer | 18.77 |
| Agriculture/Farm | 0.44 |
| Other | 0.35 |
| Total | 100% |

Source: March 31, 2008 Consolidated Report of Condition.

The bank was rated “Satisfactory” at the last CRA examination dated September 30, 2002. No legal impediments or other factors hinder the ability of ZNB to provide credit needs in its AA. There have been no changes in the bank’s corporate structure.

DESCRIPTION OF ZAPATA COUNTY ASSESSMENT AREA

ZNB designated all of Zapata County as its AA. The AA is not in a metropolitan statistical area. The AA includes three census tracts with two tracts designated moderate-income, and one tract designated middle-income. The middle-income tract was identified as being distressed due to poverty and population loss. The percentage of households below the poverty level in Zapata County is 29.64 percent. The AA does not include any low-income census tracts. The AA meets the requirements of the regulation and does not arbitrarily exclude any low- or moderate-income geographies.

Zapata is located approximately 50 miles south of Laredo, Texas. Economic conditions are currently stable due in large part to increased natural gas production. The following table contains a summary of demographic information for this AA:

| Demographic Information for Zapata County | | | | | |
|--|----------|--------------|------------------------------------|-----------------|----------------|
| | # | % Low | % Moderate | % Middle | % Upper |
| Geographies (Census Tracts) | 3 | N/A | 66.67% | 33.33% | N/A |
| Population by Geography | 12,182 | N/A | 71.07% | 28.93% | N/A |
| Owner-Occupied Housing by Geography | 3,213 | N/A | 68.60% | 31.40% | N/A |
| Businesses by Geography | 528 | N/A | 28.41% | 71.59% | N/A |
| Farms by Geography | 7 | N/A | 0% | 100% | N/A |
| Family Distribution by Income Level | 3,194 | 33.28% | 19.73% | 18.75% | 28.24% |
| Household Distribution by Income Level | 3,927 | 32.85% | 17.19% | 18.00% | 31.96% |
| Census Median Family Income (MFI) | | \$36,380 | Median Housing Value | | \$37,403 |
| HUD – Adjusted MFI: 2007 | | \$43,100 | Households Below the Poverty Level | | 29.64% |
| HUD – Adjusted MFI: 2006 | | \$43,100 | Unemployment Rate | | 3.46% |
| HUD – Adjusted MFI: 2005 | | \$42,000 | | | |

Source: 2007 Business Geodemographic Data; 2000 U.S. Census Data.

ZNB’s local competition is limited to one other bank, which is a branch of a larger state bank, headquartered in Laredo, Texas.

This office conducted one community contact with a member of a local community organization in ZNB’s AA. The contact identified personal loans for consumers as the primary credit need in Zapata County. Affordable housing was also identified as a need for the AA. It was also noted that financial assistance for the elderly was needed in Zapata County.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

ZNB demonstrated satisfactory performance in meeting the credit needs of its AA. We focused our review on the primary lending products originated since the previous CRA examination: residential loans; consumer loans; and commercial loans. The sample of loans was selected to determine the extent of lending within the AA, the distribution of loans by borrower income level, and the geographic distribution of loans.

Loan-to-Deposit Ratio

ZNB’s quarterly average LTD ratio, 36.54 percent, is reasonable. While there are no other similarly situated banks in the AA, there is one similarly situated bank located about 50 miles northeast of Zapata in Hebbronville, Texas. ZNB’s LTD compares favorably to this bank. ZNB’s LTD ratio has fluctuated from a low of 30.37 percent at September 30, 2006, to a high of 43.49 percent at September 30, 2002. At March 31, 2008, the LTD ratio was 32.61 percent. ZNB is a large depositor for public deposits and these deposits are not considered lendable. The LTD ratio at March 31, 2008 would be about 47 percent if these deposits were netted out.

| Institution | Assets as of 3/31/08 (000s) | Average Quarterly LTD Ratio 9/30/02 - 3/31/08 |
|---|------------------------------------|--|
| <i>Zapata National Bank Zapata County, Zapata, Texas</i> | <i>\$96,264</i> | <i>36.54%</i> |
| First National Bank of Hebbronville Jim Hogg County, Hebbronville, Texas | \$109,348 | 21.64% |

Source: Quarterly Consolidated Report of Condition Information.

Lending in Assessment Area

ZNB exceeds the standards for satisfactory performance with a substantial majority of loans originating in its AA. We reviewed a sample of residential, consumer, and commercial loans that originated since the prior evaluation. The following table reflects the distribution of loans, by number and dollar volume, which originated in and out of the AA.

| Lending in Zapata County | | | | | | | | | | |
|---------------------------------|-----------------|--------------|----------|-------------|-----------|-------------------------|--------------|------------|-------------|--------------|
| Loan Type | Number of Loans | | | | | Dollars of Loans (000s) | | | | |
| | Inside | | Outside | | Total | Inside | | Outside | | Total |
| | # | % | # | % | | \$ | % | \$ | % | |
| Residential | 18 | 90.00 | 2 | 10.00 | 20 | 962 | 86.67 | 148 | 13.33 | 1,110 |
| Consumer | 19 | 95.00 | 1 | 5.00 | 20 | 196 | 96.55 | 7 | 3.45 | 203 |
| Commercial | 19 | 95.00 | 1 | 5.00 | 20 | 1,104 | 95.67 | 50 | 4.33 | 1,154 |
| Total Reviewed | 56 | 93.33 | 4 | 6.67 | 60 | 2,262 | 91.69 | 205 | 8.31 | 2,467 |

Source: Loan Sample.

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

Overall, ZNB meets the standards for satisfactory performance with reasonable distribution of loans to borrowers of different incomes and businesses of different sizes. We selected a sample of loans in the AA to evaluate performance for residential loans, consumer loans, and small business loans. The following narratives and tables document our findings.

Residential lending activity to moderate-income borrowers is reasonable for moderate-income families. As shown in the table below, 15 percent of the loans in the sample were originated to borrowers with moderate-income levels. This record of performance is comparable to the demographic data with respect to the number of moderate-income families of 19.73 percent. The table also reflects that 10 percent of the loans in the sample were to low-income borrowers, which is less than the number of low-income families in the AA of 33.28 percent. The low level of residential lending to low-income families can be generally attributed to the AA's high level of households with income that is below the poverty level (29.64%). To address the need for affordable housing in the AA, management indicated they make loans secured by mobile homes as long as the borrower meets their minimum credit standards. A review of the bank's loan portfolio (as of March 31, 2008) reflected that ZNB had 13 mobile home loans outstanding. These 13 loans ranged in size from \$4,000 to \$45,000. The following table reflects the bank's record of residential lending based on our sample of loans.

| Borrower Distribution of Residential Real Estate Loans by Income Level in Zapata County | | | | | | | | |
|--|------------------|----------------------|------------------|----------------------|------------------|----------------------|------------------|----------------------|
| Borrower Income Level | Low | | Moderate | | Middle | | Upper | |
| Loan Type | % of AA Families | % of Number of Loans | % of AA Families | % of Number of Loans | % of AA Families | % of Number of Loans | % of AA Families | % of Number of Loans |
| Residential | 33.28% | 10.00% | 19.73% | 15.00% | 18.75% | 30.00% | 28.24% | 45.00% |

Source: Loan Sample; 2000 U.S. Census Data.

Our analysis of consumer lending activity to borrowers with low- or moderate-income levels is reasonable. As shown in the following table, 35 percent of the number of loans in our sample were originated to borrowers with low-income levels while the demographic data showed about 33 percent of households are low-income. Twenty-

five percent of the number of loans in our sample were originated to borrowers with moderate-income levels while the demographic data showed about 17 percent of households are moderate-income.

| Borrower Distribution of Consumer Loans by Income Level in Zapata County | | | | | | | | |
|---|--------------------|----------------------|--------------------|----------------------|--------------------|----------------------|--------------------|----------------------|
| Borrower Income Level | Low | | Moderate | | Middle | | Upper | |
| | % of AA Households | % of Number of Loans | % of AA Households | % of Number of Loans | % of AA Households | % of Number of Loans | % of AA Households | % of Number of Loans |
| Consumer | 32.85% | 35.00% | 17.19% | 25.00% | 18.00% | 15.00% | 31.96% | 25.00% |

Source: Loan Sample; 2000 U.S. Census Data.

The distribution of loans to businesses exceeds the demographic data for businesses of different sizes. Ninety percent of the bank’s commercial loans originated during the loan sampling period were made to small businesses. Small businesses are businesses with gross annual revenues of one million dollars or less. About 40 percent of the businesses either did not report revenue data or it was unavailable. Our sample of commercial loans ranged in size from \$10,000 to \$200,000. The following table shows the distribution of commercial loans among different sized businesses in the AA.

| Borrower Distribution of Commercial Loans by Business Revenue in Zapata County | | | | |
|---|--------------|--------------|---------------------|-------|
| Business Revenues (or Sales) | ≤\$1,000,000 | >\$1,000,000 | Unavailable/Unknown | Total |
| % of AA Businesses | 56.63% | 3.03% | 40.34% | 100% |
| % of Bank Loans in AA by # | 90.00% | 10.00% | 0% | 100% |
| % of Bank Loans in AA by \$ | 87.54% | 12.46% | 0% | 100% |

Source: Loan sample; 2007 Business Geodemographic Data.

Geographic Distribution of Loans

Overall, the distribution of loans reflects a reasonable dispersion throughout the bank’s AA. As previously noted, there are two moderate-income census tracts and one middle-income census tract in the bank’s AA. Census bureau information indicates that 71 percent of the population in the AA lives in the moderate-income areas.

The geographic distribution of residential and consumer loans reflects a reasonable dispersion in the bank’s AA. The following tables show the geographic distribution of residential and consumer loans in the AA.

| Geographic Distribution of Residential Real Estate Loans in Zapata County | | | | | | | | |
|---|--------------------------------|----------------------|--------------------------------|----------------------|--------------------------------|----------------------|--------------------------------|----------------------|
| 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 | N/A | N/A | 68.60% | 65.00% | 31.40% | 35.00% | N/A | N/A |

Source: Loan Sample; 2000 U.S. Census Data.

| Geographic Distribution of Consumer Loans in Zapata County | | | | | | | | |
|--|--------------------|----------------------|--------------------|----------------------|--------------------|----------------------|--------------------|----------------------|
| Census Tract Income Level | Low | | Moderate | | Middle | | Upper | |
| Loan Type | % of AA Households | % of Number of Loans | % of AA Households | % of Number of Loans | % of AA Households | % of Number of Loans | % of AA Households | % of Number of Loans |
| Consumer | N/A | N/A | 68.58% | 65.00% | 31.42% | 35.00% | N/A | N/A |

Source: Loan Sample; 2000 U.S. Census Data.

The geographic distribution of commercial loans reflects an excellent dispersion in the bank’s AA. Ninety-five percent of the bank’s business loans originated during the loan sampling period were made to businesses in the moderate-income census tracts. The following table shows the geographic distribution of business loans in the AA.

| Geographic Distribution of Commercial Loans in Zapata County | | | | | | | | |
|--|--------------------|----------------------|--------------------|----------------------|--------------------|----------------------|--------------------|----------------------|
| 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 |
| Commercial | N/A | N/A | 28.41% | 95.00% | 71.59% | 5.00% | N/A | N/A |

Source: Loan Sample; 2007 Business Geodemographic Data.

Responses to Complaints

ZNB has not received any consumer complaints related to its CRA performance during this evaluation period.

Fair Lending or Other Illegal Credit Practices Review

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