



PUBLIC DISCLOSURE

June 18, 2013

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

The First National Bank of Hughes Springs
Charter Number 6922

505 E. First Street
Hughes Springs, TX 75656

Office of the Comptroller of the Currency

1800 NW Loop 281
Suite 306
Longview, TX 75604-2516

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

First National Bank of Hughes Springs (FNB) has a satisfactory record of meeting community credit needs. This rating is based on the following:

- The bank's loan-to-deposit ratio is reasonable based on its size and complexity.
- A majority of the institution's lending is located within the assessment areas.
- The distribution of loans to borrowers of different income levels is excellent throughout the assessment areas.
- The geographic distribution of loans reflects a reasonable dispersion throughout the assessment areas.

SCOPE OF EXAMINATION

This Performance Evaluation (PE) is an assessment of The First National Bank of Hughes Springs' ability to meet the credit needs of the communities in which it operates. The bank was evaluated under the Small Bank performance criteria. The bank's primary loan products in the Hughes Springs Assessment Area (AA) include residential real estate mortgages and commercial loans. The primary loan product for the Liberty City AA is consumer loans. Loans originating in the Winona AA were not included in the scope of our review as the lending volume in that AA was not sufficient to perform a meaningful analysis. Conclusions regarding the bank's lending performance were based on 22 residential real estate loans, 25 commercial loans, and 33 consumer loans originated during 2010 and 2011 compared to 2000 U.S. Census Data. Lending activity in 2012 and year-to-date 2013 is not significantly different from 2010 and 2011. Bank management agreed with this data analysis.

DESCRIPTION OF INSTITUTION

The First National Bank of Hughes Springs is a \$196 million bank with its main office located at 505 East First Street, Hughes Springs, Texas. The bank is wholly owned by Chalybeate Springs Corporation, a one-bank holding company. The bank has 10 full service branches and one drive-thru branch. The bank operates 10 automatic teller machines (ATMs) located at the various branches. A majority of the bank's offices are located in the non-metropolitan counties of Morris, Cass, Harrison, and Marion Counties. The bank also has a branch located in Gregg County, which is in the Longview Metropolitan Statistical Area (MSA). They also operate a branch in Smith County, which is located in the Tyler MSA. Two of the branches located in Bowie County, Texas were not included in the examination. These branches were purchased in 2012 and there has not been sufficient time to determine the effectiveness of meeting needs in this area.

The bank is a full service institution and its business strategy is to provide a variety of traditional deposit and loan products and financial services to consumers and commercial businesses. As of March 31, 2013, net loans represented 60 percent of total assets. The following chart reflects the distribution of the bank's loan portfolio by type:

Loan Category	\$ (000)	%
Commercial Real Estate Loans	\$43,183	36.50
Commercial Loans	\$32,393	27.38
Residential Real Estate Loans	\$25,165	21.27
Consumer Loans	\$11,618	9.82
Agriculture Loans	\$3,466	2.93
Other Loans	\$2,485	2.10
Total	\$118,310	100.00

There are no legal, financial or other factors impeding the bank's ability to meet the community credit needs in its assessment area. The bank's CRA performance was previously evaluated as of January 14, 2008, with an overall level of performance rated as "Satisfactory."

DESCRIPTION OF ASSESSMENT AREA(S)

First National Bank has designated three separate assessment areas as follows:

Hughes Springs Assessment Area

The Hughes Springs AA consists of Morris, Cass, and Marion Counties, in their entirety, and one adjacent census tract in Harrison County. There are six full service branches, one drive-thru branch, and six ATMs located within the assessment area. The assessment area consists of fourteen middle-income census tracts and one moderate-income tract. There are no low-income census tracts located in the assessment area. The following table reflects the demographics of the assessment area:

Demographic and Economic Characteristics of Hughes Springs Assessment Area	
Population	
Number of Families	17,361
Number of Households	24,302
Geographies	
Number of Census Tracts/BNA	15
% Low-Income Census Tracts/BNA	0.00%
% Moderate-Income Census Tracts/BNA	6.67%
% Middle-Income Census Tracts/BNA	93.33%
% Upper-Income Census Tracts/BNA	0.00%
<i>Median Family Income (MFI)</i>	
2011 MFI for AA	\$36,380
2011 HUD-Adjusted MFI	\$48,600
Economic Indicators	
Unemployment Rate	3.43%
2010 Median Housing Value	\$47,251
% of Households Below Poverty Level	18.88%

Source: U.S. Census Data

Competition is typical of institutions located in rural markets with small branches of other community institutions located throughout the assessment area. Additionally, several of the local competitors are headquartered within the assessment area. The bank is retail oriented with a focus on 1-4 family residential mortgages and business loans. The local economy is stable. Major employers in the area include Lone Star Steel, International Paper Company, and the Daingerfield-Lone Star Independent School District.

Our review included contacting a representative of a local government organization located in the assessment area. The contact noted that the assessment area is largely rural with several smaller communities. While this contact did not identify a primary credit need, they did indicate that the local financial institutions offer products that meet the community's credit needs.

Liberty City Assessment Area

The Liberty City assessment area is located in Gregg County, Texas and is part of the Longview, Texas MSA. Liberty City is a rural area west of Longview, Texas and situated between the larger cities of Kilgore, TX and Gladewater, Texas. There is one branch and one ATM in the assessment area. The assessment area consists of two middle-income census tracts and one moderate-income census tract.

Demographic and Economic Characteristics of Liberty City Assessment Area	
Population	
Number of Families	5,063
Number of Households	7,010
Geographies	
Number of Census Tracts/BNA	3
% Low-Income Census Tracts/BNA	0.00%
% Moderate-Income Census Tracts/BNA	33.33%
% Middle-Income Census Tracts/BNA	66.67%
% Upper-Income Census Tracts/BNA	0.00%
<i>Median Family Income (MFI)</i>	
2010 MFI for AA	\$40,970
2012 HUD-Adjusted MFI	\$55,600
Economic Indicators	
Unemployment Rate	5.10%
2010 Median Housing Value	\$53,841
% of Households Below Poverty Level	16.96%

Source: U.S. Census Data

Competition is typical of institutions located in rural markets with small branches of other community institutions located throughout the assessment area. Additionally, several of the local competitors are headquartered within the bank's assessment area. The bank is retail oriented with a focus on consumer loans. The local economy is stable. Major employers in Liberty City include the Sabine Independent School District as well as other smaller retail service providers. Other major employers from nearby towns of Gladewater, Texas and Kilgore, Texas include Texas Die Casting and General Dynamics.

Our review included contacting a representative of a local realty business in the assessment area. This contact identified residential and consumer lending as the primary credit need with limited opportunity for community development. The contact did indicate that the local financial institutions offer a variety of products that meet the community's credit needs.

Winona Assessment Area

The Winona assessment area is located in Smith County, Texas and is part of the Tyler, Texas MSA. Winona is a rural community located north of Tyler, Texas. There is one branch and one ATM in the assessment area. The assessment area includes a single middle-income census tract in the Tyler, Texas MSA. Due to limited lending activity in this branch, there is insufficient data to perform a full lending analysis of this assessment area.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

Loan-to-Deposit Ratio

The loan-to-deposit ratio of FNB is reasonable based on the bank's size, financial condition and the credit needs of the combined assessment areas. The bank's quarterly average loan-to-deposit ratio was calculated to be 63.26 percent since the prior CRA examination in January 2008. The average loan-to-deposit ratio of banks in and around the assessment area, for the same period, was 68.15 percent.

Institution	Assets (000s) (as of 12/31/12)	Average LTD Ratio
First National Bank of Hughes Springs	\$195,642	63.26
Texas Heritage National Bank Daingerfield, Texas	\$106,325	88.28
Texana Bank N.A. Linden, Texas	\$154,089	84.61
Citizens State Bank Tyler, Texas	\$259,513	79.14
American State Bank Arp, Texas	\$238,085	73.65
Citizens Bank Kilgore, Texas	\$354,695	66.10
Gladewater National Bank Gladewater, Texas	\$48,606	66.20
Lindale State Bank Lindale, Texas	\$114,488	65.35
Kilgore National Bank Kilgore, Texas	\$90,593	61.94
Morris County National Bank of Naples, Texas	\$88,390	57.52
First State Bank Hallsville, Texas	\$34,598	38.75

Lending in Assessment Areas

A majority of the bank's lending activity is located inside the assessment area. We reviewed a total of 60 loans in the assessment area, 20 consumer loans, 20 residential real estate loans, and 20 commercial loans. The consumer loans are representative of the Liberty City Assessment Area. The residential and commercial loans are representative for the Hughes Springs Assessment Area. By number of origination, 76 percent of the loans and by volume of origination, 48 percent of the loans originated within the assessment area. The breakdown by loan category is detailed in the following table.

Lending in the combined Assessment Area										
Loan Type	Number of Loans					Dollars of Loans				
	Inside		Outside		Total	Inside		Outside		Total
	#	%	#	%		\$	%	\$	%	
Consumer	13	65.00	7	35.00	20	130	52.77	117	47.23	247
Residential Real Estate	18	90.00	2	10.00	20	1,096	77.65	316	22.35	1,412
Commercial Loans	15	75.00	5	25.00	20	1,307	35.85	2,338	64.15	3,645
Totals	46	76.67	14	23.33	60	2,533	47.76	2,771	52.24	5,304

Source: Loan sample

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

The distribution of loans to borrowers of different income levels represents an excellent penetration throughout the bank's assessment areas.

Hughes Springs Assessment Area

The distribution of loans to borrowers of different income levels represents an excellent penetration throughout the Hughes Springs assessment area.

Residential Real Estate Loans

The distribution of residential real estate loans by borrower income level is excellent. The distribution of residential lending to low income families exceeds the percentage of assessment area families. The distribution of loans to moderate-income families is near the percentage of assessment area families. The median cost of housing in the assessment area is \$47 thousand. A low-income family earns less than \$24 thousand based on the HUD updated 2011 median family income with 18.88 percent of families in the assessment area living below the poverty level. Moderate-income families earn between \$24 thousand and \$39 thousand.

Borrower Distribution of Residential Real Estate Loans in Hughes Springs Assessment Area								
Borrower Income Level	Low		Moderate		Middle		Upper	
Loan Type	% of AA Families	% of # of Loans	% of AA Families	% of # of Loans	% of AA Families	% of # of Loans	% of AA Families	% of # of Loans
Residential Real Estate	22.41	25.00	18.71	15.00	20.79	20.00	38.09	40.00

Source: Loan sample, U.S. Census data.

Commercial Loans

The bank's distribution of loans to small businesses is excellent. The percentage of loans to businesses with revenues of \$1 million or less exceeds the percentage of assessment area businesses with revenues of \$1 million or less. However, 28 percent of businesses in the area did not report income.

Borrower Distribution of Loans to Businesses in Hughes Springs Assessment Area				
Business Revenues (or Sales)	≤\$1,000,000	>\$1,000,000	Unknown	Total
% of AA Businesses	70.73	1.67	27.60	100%
% of Bank Loans in AA by #	95.00	5.00	0.00	100%
% of Bank Loans in AA by \$	79.50	20.50	0.00	100%

Source: Loan sample, Dun and Bradstreet data.

Liberty City Assessment Area

The distribution of loans to borrowers of different income levels represents an excellent penetration throughout the Liberty City assessment area

Consumer Loans

The distribution of consumer loans to borrowers of different incomes is excellent. The distribution of loans to low income borrowers exceeds the demographic comparator. Similarly, the distribution of loans to moderate-income borrowers exceeds the demographic comparator.

Borrower Distribution of Consumer Loans in Gregg MSA Assessment Area								
Borrower Income Level	Low		Moderate		Middle		Upper	
	% of AA Households	% of # of Loans	% of AA Households	% of # of Loans	% of AA Households	% of # of Loans	% of AA Households	% of # of Loans
Consumer Loans	26.58	42.32	15.90	26.92	19.93	15.38	37.59	15.38

Geographic Distribution of Loans

The geographic distribution of loans reflects a reasonable dispersion of loans throughout the bank's assessment areas. The 2000 U.S. Census data shows two moderate-income tracts within the bank's assessment areas, one in the Hughes Springs assessment area, and one in the Liberty City assessment area. However, in 2010 and 2011 the Federal Financial Institution Examination Council (FFIEC) identified six middle-income tracts in Morris and Marion Counties as either distressed or underserved. These census tracts are located in the Hughes Springs assessment area and the level of lending in these census tracts was included in the analysis of geographic distribution of loans throughout the assessment areas.

Hughes Springs Assessment Area

The geographic distribution of loans reflects a reasonable dispersion of loans throughout the Hughes Springs assessment area.

Residential Real Estate Loans

The geographic distribution of residential loans is reasonable. The assessment area has no low-income tracts, one moderate-income tract, and fourteen middle-income tracts. The percentage of number of loans to the moderate-income tract is near the percentage of owner-occupied housing located in the moderate-income tract. Additionally, seven of the loans from the sample were made to residents located in middle-income tracts that were either distressed or underserved during the review period.

Geographic Distribution of Residential Real Estate Loans in Hughes Springs Assessment Area								
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 Real Estate	0.00	0.00	6.04	5.00	93.96	95.00	0.00	0.00

Source: Loan sample, U.S. Census data.

Commercial Loans

The geographic distribution of loans to businesses is reasonable. There are no low-income tracts and only one moderate-income tract within the assessment area. There were no loans in the sample to businesses located in the moderate-income tract. However, less than 3 percent of businesses in the assessment area are located in the moderate-income tract. The low level of businesses located in the moderate income-tract provides few opportunities for commercial lending. Additionally, two of the loans from the sample were made to businesses located in

middle-income tracts that were either distressed or underserved during the review period.

Geographic Distribution of Loans to Businesses in the Hughes Springs Assessment Area								
Census Tract Income Level	Low		Moderate		Middle		Upper	
	% of AA	% of # of Loans	% of AA	% of # of Loans	% of AA	% of # of Loans	% of AA	% of # of Loans
Businesses	0.00	0.00	2.67	0.00	97.33	100.00	0.00	0.00

Source: Loan sample, Dun and Bradstreet data.

Liberty City Assessment Area

The geographic distribution of loans reflects a very poor dispersion of loans throughout the Liberty City assessment area.

Consumer Loans

The geographic distribution of loans to consumers is very poor. Mitigating factors considered during our review include the location of the moderate-income tract relative to the branch, physical barriers such as Interstate-20, and a significant level of competition within the assessment area. The moderate-income census tract is located in Kilgore, Texas, a larger community than the branch location. Residents of the moderate-income census tract would have to travel along state highways and cross Interstate – 20 to reach the branch in Liberty City, making it inconvenient for consumers to conduct business in Liberty City. Competition is significant with several community banks located within close proximity of the census tract in Kilgore. In addition, 64 percent of the residents in the census tract are either low-income or below the poverty level thus reducing the availability of applicants who could potentially qualify for a loan.

Geographic Distribution of Loans to Consumers in the Liberty City Assessment Area								
Census Tract Income Level	Low		Moderate		Middle		Upper	
	% of AA	% of # of Loans	% of AA	% of # of Loans	% of AA	% of # of Loans	% of AA	% of # of Loans
Businesses	0.00	0.00	22.52	4.35	77.48	95.65	0.00	0.00

Source: Loan sample, U.S. Census Data

Responses to Complaints

FNB has not received any complaints or public comments regarding CRA performance during this 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.