



SMALL BANK

Comptroller of the Currency
Administrator of National Banks

PUBLIC DISCLOSURE

February 10, 2003

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

**The Karnes County National Bank of Karnes City
Charter Number 5614**

**301 E. Calvert Avenue
Karnes City, TX 78118**

**Comptroller of the Currency
San Antonio South Field Office
10101 Reunion Place Blvd., Suite 402
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.

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INSTITUTION'S CRA RATING

This institution is rated Satisfactory.

Karnes County National Bank's lending performance reflects a satisfactory response to community credit needs. Factors in our assessment include:

- The bank's loan-to-deposit ratio is good and compares favorably to similarly situated financial institutions.
- A substantial majority of loans, representing 88% of the number and 84% of the dollar volume are within the bank's assessment area (AA).
- The distribution of borrowers reflects a reasonable penetration among businesses and farms of different sizes, and individuals of different income levels.
- The geographic distribution of loans is excellent.
- There are no consumer complaints with respect to the bank's CRA performance during this evaluation period.

DESCRIPTION OF INSTITUTION

Karnes County National Bank (KCNB) is an independently owned community bank (no holding company) with assets of \$53.1 million as of December 31, 2002. The main office is located in Karnes City, Karnes County, Texas, with ATMs in Karnes City, Texas and Kenedy, Texas. There are no branches. KCNB's loan portfolio is composed primarily of commercial and consumer (includes residential loans) loan products. Competition in Karnes County is strong with two other community banks, three branches of a regional bank, and two credit unions.

Net loans of \$22.7 million represent 43 percent of KCNB's total assets. A summary of the loan portfolio follows:

Loan Portfolio Composition		
As of December 31, 2002		
Loan Category	\$ (000)	%
Commercial	11,366	49.2
Consumer	4,532	19.6
Residential	4,503	19.5
Agriculture	2,691	11.7
Total	23,092	100

There are no legal or financial circumstances that impede the bank's ability to help meet the credit needs in its AA. KCNB's previous CRA rating, dated July 13, 1998, was "satisfactory." The bank does not have any affiliate relationships and there have been no changes in its corporate structure since the last review.

DESCRIPTION OF THE KARNES COUNTY ASSESSMENT AREA

KCNB has designated Karnes County, Texas as its AA. Karnes County consists of four Block Number Areas (BNAs) with a 1990 Census total population of 12,455. The AA has three moderate-income BNAs and one middle-income BNA. The AA meets the requirements of the regulation and does not arbitrarily exclude any low- or moderate-income geographies.

DEMOGRAPHIC AND ECONOMIC CHARACTERISTICS OF AA	
<i>Population</i>	
Number of Families	3,284
Number of Households	4,331
<i>Geographies</i>	
Number of Census Tracts/BNA	4
% Low-Income Census Tracts/BNA	0.00%
% Moderate-Income Census Tracts/BNA	75.00%
% Middle-Income Census Tracts/BNA	25.00%
% Upper-Income Census Tracts/BNA	0.00%
<i>Median Family Income (MFI)</i>	
1990 MFI for AA	\$24,585
2002 HUD-Adjusted MFI	\$36,100
<i>Economic Indicators</i>	
Unemployment Rate-AA	4.80%
Unemployment Rate-State	6.30%
Unemployment Rate-National	5.90%
1990 Median Housing Value	\$29,172
% Households Below Poverty Level	33.43%
% Owner Occupied Housing	63.10%

The population of the AA was 12,455 based on 1990 census data. The AA population experienced moderate growth and was 15,446 based on 2000 census data. People committed to institutions account for a large percentage of that growth.

Economic conditions are stable, although the community as a whole is poor, with 33 percent below the poverty level. Of the families living in the AA, 35 percent are low-income, 17 percent are moderate-income, 14 percent are middle-income, and 34 percent are upper-income. Major employers of the AA include correctional facilities, school districts, agriculture, retail, and manufacturing.

We conducted one community contact during this review. The contact was a government

official of Karnes County who thought KCNB was doing a good job of providing basic banking services and promoting community development. The contact did not know of any specific credit needs in the community.

SAMPLING INFORMATION

Our review focused on KCNB's major product lines: business and farm loans, 1-4 family residential loans, and consumer loans. We sampled 20 loans from each product line. For the *Lending to Borrowers of Different Incomes and to Businesses of Different Sizes* and the *Geographic Distribution of Loans* analyses, we excluded loans that were made outside of the AA. All loans sampled were originated between January 1, 1999 and December 31, 2002, and were selected randomly.

CONCLUSIONS ABOUT PERFORMANCE CRITERIA

Management has demonstrated “satisfactory” performance in meeting the credit needs of the AA.

Loan-to-Deposit Ratio

KCNB's loan-to-deposit (LTD) ratio meets the standards for satisfactory performance. During this review period, the ratio ranged from 41.20 to 55.32 percent with a quarterly average ratio of 46.34 percent. Quarterly averages reflect KCNB's LTD ratio to be slightly higher than local competition. The following chart compares KCNB's ratio to that of its peers, other independent community banks in Karnes County.

Institution	Assets (\$000) as of 12/31/02	LTD ratio as of 12/31/02	Average LTD Ratio
Karnes County National Bank	53,980	50.06	46.34
Falls City National Bank	95,305	45.62	40.43
First-Nichols National Bank	38,714	40.21	35.14

Lending in Assessment Area

KCNB's lending in the AA meets the standards for satisfactory performance. A substantial majority of the bank's lending activity is within its AA. As illustrated in the following table, 88 percent of the number and 84 percent of the dollar amount of sample loans were made in the AA. The following table reflects the bank's lending in and out of the AA by type of loan sampled.

Lending In and Out of the Assessment Area								
LOAN TYPE	IN ASSESSMENT AREA				OUT OF ASSESSMENT AREA			
	#	%	\$ (000s)	%	#	%	\$ (000s)	%
1-4 Family Residential	19	95	721	80	1	5	178	20
Consumer Credit	18	90	175	84	2	10	34	16
Commercial/Agriculture	16	80	703	88	4	20	95	12
Total Reviewed	53	88	1,599	84	7	12	307	16

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

KCNB meets the standards for satisfactory performance in this category. The distribution of loans reflects a reasonable penetration among individuals of different income levels and businesses and farms of different sizes given the demographics of the AA.

Of the 20 business loans sampled, 17 (85 percent) were to small businesses and farms. Additionally, 13 of these loans were to businesses and farms with revenues of less than \$100,000. The following table illustrates the lending distribution to businesses and farms located within the bank's AA. As the table reflects, the percent of both number and dollar of loans granted to small businesses and farms is slightly below the percentage of small businesses and farms in the AA. The ratios are indicative of a reasonable level of performance regarding loans to small businesses and small farms.

BORROWER DISTRIBUTION OF LOANS TO BUSINESSES AND FARMS		
Business Revenues	≤\$1,000,000	>\$1,000,000
% of AA Businesses	95	5
% of Bank Loans in AA #	85	15
% of Bank Loans in AA \$	76	33

The sample of consumer loans reflects that the bank has a good record of consumer loan originations to low- and moderate-income borrowers. Seventy percent of consumer loans sampled (by number) were made to low and moderate-income individuals.

CONSUMER								
Borrower Income Level	LOW		MODERATE		MIDDLE		UPPER	
% of AA Households	34		16		15		35	
LOANS BY YEAR	% of Number	% of Amount	% of Number	% of Amount	% of Number	% of Amount	% of Number	% of Amount
1999	5	10	0	0	0	0	0	0
2000	5	4	0	0	0	0	0	0
2001	5	2	5	3	5	16	5	10
2002	30	13	20	14	10	12	10	16
Total	45	29	25	17	15	28	15	26

The following table indicates the income distribution of the loans in our residential sample and

shows that the bank has made residential loans to low-income families but at a proportionally lower level compared to the percentage of low-income families in the AA. The reason for this is that there is not much demand for new housing. The population has increased in the past 10 years by the approximate increase in institutionalized individuals. There were no loans to moderate-income families in our sample. However, two of the four loans to middle-income families were to families with incomes that exceeded the moderate-income level by only \$1,200.

RESIDENTIAL REAL ESTATE								
Borrower Income Level	LOW		MODERATE		MIDDLE		UPPER	
% of AA Families	35		17		14		34	
LOANS BY YEAR	% of Number	% of Amount	% of Number	% of Amount	% of Number	% of Amount	% of Number	% of Amount
1999	0	0	0	0	5	3	25	25
2000	5	2	0	0	0	0	20	17
2001	0	0	0	0	10	7	10	9
2002	5	2	0	0	5	10	15	25
Total	10	4	0	0	20	20	70	76

Geographic Distribution of Loans

KCNB's geographic distribution of loans throughout the AA is excellent and exceeds the standards for satisfactory performance. The bank's location is in one of the three moderate-income BNAs. The one middle-income BNA is located on the fringes of the AA. Of the 60 residential, consumer, and business/farm loans, only one farm loan was in the middle-income BNA as shown in the tables below.

BUSINESSES AND FARMS								
Census Tract Income Level	LOW		MODERATE		MIDDLE		UPPER	
% of AA Bus. & Farms	0		81		19		0	
LOANS BY YEAR	% of Number	% of Amount	% of Number	% of Amount	% of Number	% of Amount	% of Number	% of Amount
1999			15	11	0	0		
2000			15	13	0	0		
2001			25	46	0	0		
2002			40	29	5	1		
Totals	NA	NA	95	99	5	1	NA	NA

CONSUMER								
Census Tract Income Level	LOW		MODERATE		MIDDLE		UPPER	
%of AA Households	0		84		16		0	
LOANS BY YEAR	% of Number	% of Amount	% of Number	% of Amount	% of Number	% of Amount	% of Number	% of Amount
1999			5	10	0	0		
2000			5	4	0	0		
2001			20	30	0	0		
2002			70	56	0	0		
NA	NA	NA	100	100	0	0	NA	NA

RESIDENTIAL REAL ESTATE								
Census Tract Income Level	LOW		MODERATE		MIDDLE		UPPER	
%of AA Owner Occupied	0		82		18		0	
LOANS BY YEAR	% of Number	% of Amount	% of Number	% of Amount	% of Number	% of Amount	% of Number	% of Amount
1999			30	28	0	0		
2000			20	20	0	0		
2001			25	16	0	0		
2002			25	36	0	0		
Totals	NA	NA	100	100	0	0	NA	NA

Responses to Complaints

There have been no CRA-related consumer complaints received since the previous evaluation.

Fair Lending Review

An analysis of four years public comments and consumer complaint information was performed according to the OCC's risk-based fair lending approach. Based on its analysis of the information, the OCC decided that a comprehensive fair lending examination would not need to be conducted in connection with the CRA evaluation this year. The latest comprehensive fair lending exam was performed in 1998.