



SMALL BANK

Comptroller of the Currency
Administrator of National Banks

PUBLIC DISCLOSURE

February 03, 2003

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

**Carlsbad National Bank
Charter Number 12569**

**202 West Stevens Street
Carlsbad, New Mexico 88220**

**Comptroller of the Currency
ADC- Arizona & New Mexico
9633 South 48th Street Suite 265
Phoenix, Arizona 85044**

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.

Carlsbad National Bank's (CNB) lending performance in relation to its assessment area (AA) credit needs is Satisfactory. The bank has demonstrated its ability to meet the credit needs of the AA through reasonable performance in lending to small businesses and low- and moderate-income individuals. The following information further describes the bank's performance under the Community Reinvestment Act (CRA):

- The bank's loan-to-deposit ratio is reasonable and meets the standard for Satisfactory.
- The bank makes a substantial majority of its loans within the AA and exceeds the standard for Satisfactory.
- The bank's distribution of loans to individuals of different income levels and businesses of different sizes is reasonable and meets the standard for Satisfactory.

DESCRIPTION OF INSTITUTION

CNB is a community bank located in southern Eddy County in Carlsbad, New Mexico. As of December 31, 2002, the bank had \$174 million in average assets and net total loans of \$74 million, or 42 percent of total assets. CNB operates a main office, two branches and four automated teller machines (ATMs) all within the city limits of Carlsbad. The bank has neither opened nor closed any branch offices or ATMs during the evaluation period.

Carlsbad Bankcorporation, a one-bank holding company located in Carlsbad, New Mexico, owns 100 percent of the bank. There are no other subsidiaries or affiliates.

The bank's primary lending focus is residential real estate and business lending. In terms of dollars, residential real estate loans represent 42 percent and commercial loans represent 34 percent of the bank's total loan portfolio as of December 31, 2002.

There are no financial or legal impediments that hinder the bank's ability to help meet the credit needs of its assessment area. The previous CRA examination dated May 31, 1997, resulted in a satisfactory rating.

DESCRIPTION OF SOUTHERN EDDY COUNTY

CNB has designated the southern half of Eddy County, New Mexico as its assessment area (AA). This consists of eight contiguous block numbering areas (BNA), and includes the towns of Carlsbad, and Loving, all located in southeastern New Mexico. There are 2 upper income and 6 middle-income tracts. There are no low- or moderate-income (LMI) tracts. The AA meets the legal requirements of the regulation and does not arbitrarily exclude LMI geographies.

The table outlines some of the pertinent demographic and economic information for the AA.

| DEMOGRAPHIC AND ECONOMIC CHARACTERISTICS OF AA | |
|--|----------|
| <u>Population</u> | |
| Number of individuals | 33,739 |
| <u>Median Family Income (MFI) and % of families by income levels</u> | |
| 2002 HUD-adjusted statewide non-MSA MFI | \$33,700 |
| Low-income families | 17% |
| Moderate-income families | 14% |
| Middle-income families | 20% |
| Upper-income families | 49% |
| <u>Housing</u> | |
| Number of housing units | 13,909 |
| Percent Owner Occupied | 64% |
| 1990 Median Housing Value | \$48,233 |
| <u>Economic Indicators</u> | |
| Unemployment Rate (as of 12/31/01) | 5.1% |
| % of Households Below Poverty Level | 18.51% |

Source: U.S. Census Bureau, and Bureau of Labor Statistics

The economy of the AA was historically based on oil and gas (O&G) development and production, potash mining, and tourism (Carlsbad Caverns). Current major employers include Westinghouse (which manages the Waste Isolation Pilot Plant - WIPP), two potash mines, the schools, and medical center. Over the last five-years, unemployment for Eddy County has remained steady with the exception of 1999 when it jumped to 8.1 percent. This was when four potash mines closed and the O&G industry hit a slump, both events resulted in large local lay-offs. WIPP, a low-level radioactive waste storage facility located southeast of the city, has contributed greatly to the recent growth of Carlsbad. It received its first shipment in 1999, but did not experience significant hiring until 2001. Two new call centers also opened during this period. However, in 2001 the events of September 11 also caused a considerable slowdown in the local tourist traffic that has not yet completely rebounded. The unemployment statistics have returned to their normal levels, largely due to WIPP and the new call centers.

Competition for financial services is strong. In addition to CNB, there are three other banks, including a branch of a nation-wide company, three credit unions, and six non-bank financial institutions (three brokerage firms and three mortgage companies).

To gather more current information on the nature of the community and potential lending opportunities in the AA, we contacted one community leader in a government office during this examination. The contact reported no unmet credit needs in the community. He said that the major long-term issue facing Carlsbad is the impact on the local economy when the WIPP project is completed.

CONCLUSIONS ABOUT PERFORMANCE CRITERIA

The evaluation of the bank's lending performance is based upon the review of loans samples. For the purpose of this review, we determined the bank's primary products are home refinance loans, and business loans. These loans comprised 29% and 32%, respectively, of the dollar amount of the loans originated since the May 31, 1997 examination through December 31, 2002, (also known as the "evaluation period").

After identifying primary products, we took a random sample of 20 loans from each primary product, for a total of 40 loans. The Lending in Assessment Area sample is taken from loans originated during the evaluation period. The Lending to Borrowers of Different Income and Businesses of Different Sizes sample is taken from loans originated in the AA during 2001 and 2002. The Loan-to-Deposit ratio is not based on samples. It is based on the average of 21 quarterly ratios during the evaluation period.

The bank's CRA performance in meeting the credit needs of the community is satisfactory as supported by the following.

Loan-to-Deposit Ratio

The CNB loan-to-deposit ratio of 55 percent is reasonable given the bank's size, financial condition, and assessment area credit needs. To better understand the bank's performance, we compared this ratio to the one other similarly situated bank in the AA. There are four banks in the AA, but two of the banks have a substantial majority of their deposits outside the AA and only one or two branches inside the AA. The remaining similarly sized bank in the AA has 10 branches compared to CNB's three. While CNB's ratio appears on the low side, compared to the other bank's loan-to-deposit ratio of 79 percent, the CNB ratio would be greatly improved if the bank added back originated loans sold in the secondary market. For the evaluation period, the bank sold over \$45 million of its 1-4 family residential loans to the secondary market. This is in addition to real estate loans originated and kept in the bank's portfolio, which totaled \$32 million at December 31, 2002.

Lending in Assessment Area

A substantial majority of the sampled loans originated inside the AA. This exceeds the standard for satisfactory performance. The conclusion is based on an analysis of the original dollar amount and number of a sample of 40 loans. We selected 20 of each of the bank's two primary loan products: home refinance and business loans. The loans sampled were made during the evaluation period of May 31, 1997 through December 31, 2002. Our analysis determined that 98 percent of the number and 99 percent of the dollar amount of the loans in the sample were made within the bank's AA.

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

The distribution of loans reflects a reasonable penetration among individuals of different income levels and businesses of different sizes, given the demographics of the AA.

For different income levels of individuals, we sampled 20 home refinance loans originated in 2001 and 2002. We then compared the bank's lending distribution to the demographics of the AA. Our focus for the analysis was the bank's level of lending to low- and moderate-income borrowers. By number of loans, the bank's performance nearly matches the demographics of low-income individuals in the area, and substantially exceeds the demographics of moderate-income individuals in the area. By dollar amount of loans, the bank's performance appears to be substantially below the demographics of low-income individuals in the area, but nearly matches the demographics of moderate-income individuals in the area. The following table shows the details. The substantially lower dollar amount to low-income borrowers can be explained by customers in this category qualifying for smaller loan amounts, and by the 18 percent of households in the AA below the poverty level who would probably not qualify.

| Lending Distribution Based on Income Level of Refinanced Residential Real Estate Borrowers January 2001 through December 2002 Loan Originations | | | |
|---|--|---|--|
| Borrower Income Level | Bank Lending Distribution by Number of Loans | Bank Lending Distribution by Dollar Amount of Loans | Percentage of Families in each Income Category (Census Information) |
| Low | 15 | 4 | 17% |
| Moderate | 25 | 13 | 14% |
| Middle | 10 | 5 | 20% |
| Upper | 50 | 78 | 49% |
| Totals | 100% | 100% | 100% |

For businesses of different sizes, we sampled 20 business loans originated in 2001 and 2002. We then compared the bank's lending distribution to the business demographics of the AA. Our focus for the analysis was the bank's level of lending to businesses with revenues of less than \$1 million. By number of loans, the bank's performance nearly matches the demographics of the area. By dollar amount of loans, the bank's performance appears to be significantly below the demographics. This number is skewed by one large loan in the sample to a business with revenues greater than \$1 million. We also consider this ratio reasonable, as larger businesses generally have larger borrowing needs. The following table shows the details of the borrower distribution analysis for business loans by gross annual revenue size.

| Distribution of Commercial Loans by Gross Annual Revenue Years 2001-2002 | | | | | |
|---|------------|--------|------------------------|------------------|---------------------------|
| Revenue Size | # of loans | % of # | \$'(000's) of Loans | % of \$'(000) | % of businesses in AA* |
| Under \$1 million | 15 | 75% | 975 | 26% | 80% |
| Over \$1 million | 5 | 25% | 2,813 | 74% | 5% |
| Total Loans: | 20 | 100% | 3,788 | 100% | 85%** |

*Source: 2002 Dun & Bradstreet

**Does not total 100% because nearly 15% of businesses in assessment area did not report their revenues.

Geographic Distribution of Loans

We did not perform an analysis of the bank's geographic distribution of loans. The AA includes only moderate and upper income block numbering areas and such an analysis would not be meaningful.

Qualified Investments and CD Services

We received a list of investments the bank wanted us to consider. Many of the investments on the list did not meet regulatory requirements for "community development" under the CRA, though they did benefit the community. Of the investments on the list, we were only able to qualify one, a donation of \$10 thousand to the Carlsbad Department of Development. The donation was to attract a calling center to the community to help alleviate unemployment due to layoffs in the mining, and oil and gas industries. The call center helped to retrain these individuals, and benefited about 200 people. This investment qualifies under the CRA because it promotes economic development by supporting permanent job creation for persons who are low- or moderate-income.

Responses to Complaints

CNB has not received any complaints about its performance in helping to meet AA credit needs during this evaluation period.

Fair Lending Review

An analysis of 1997-2003 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.