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Financial Industry Trends

FEDERAL RESERVE BANK OF DALLAS

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Financial institutions in this part of the country benefited from a vigorous regional economy in 1995. Construction activity, energy and high-tech production, exports and, in Louisiana, the gaming industry contributed to the favorable economic climate and created ample business opportunities for financial services providers.

The Eleventh Federal Reserve District comprises southern Louisiana, northern New Mexico and Texas. Financial Industry Trends provides an overview of the activities of the domestic and foreign financial institutions in all three states, based on data collected for the entire state by the various federal regulatory agencies that oversee the financial industry.

In this issue of Trends, we see that financial institutions moved quickly to meet the demand for their products and services, further propelling loan growth along the upward trend that began in 1992. In particular, real estate and business lending have recovered, after having plummeted during the last banking downturn.

With loans growing far faster than deposits, our attention turned to funding issues in 1995. While small banks were able to reduce federal funds sold and attract deposits, large banks made greater use of managed liabilities as a funding source. Managed liabilities consist of federal funds purchased, securities sold under agreements to repurchase and other borrowed money (including Federal Home Loan Bank advances). Some funding also was provided by a larger equity base, as capital ratios approached historic highs. Given the overall health of the banking industry, the higher loan-to-deposit ratios did not seem to be cause for much concern.

Steady loan growth, continued profits and high capital levels also characterized the region's credit unions and thrift institutions. The year's biggest surprise came from foreign banks, whose Texas-based agencies and representative offices reported huge gains in commercial loans that stemmed from large corporations' increased demand for financing.

Should you have any questions or comments, feel free to reach me at P.O. Box 655906, Dallas, Texas 75265-5906, or via e-mail at Bob.Hankins@dal.frb.org.

Robert D. Hankins
Senior Vice President
GROWING PROSPECTS

Healthy Southwest Economy Provides Fertile Ground for Bank Loans

Banks in Louisiana, New Mexico and Texas enjoyed a prosperous year in 1995 as strong loan growth and a stable net interest margin kept earnings at a high level. Asset quality appeared largely uncompromised, and capital remained high relative to past levels. Lending outpaced deposit growth, but the region's banks were able to maintain a comfortable liquidity position.

At year-end 1995, the three states were home to 1,188 banks that held combined total assets of $262.7 billion. The number of banks declined from 1,250 at year-end 1994. No banks were closed due to failure in 1995. A net addition of 201 branch locations during the year brought the total number of branch offices to 4,091.

For 1995, aggregate net income was $3 billion, exceeding the $2.7 billion reported for 1994. The return on average assets was 1.23 percent for 1995. By state, the returns on average assets were 1.39 percent in Louisiana, 1.36 percent in New Mexico and 1.19 percent in Texas. In comparison, the aggregate return for banks in the rest of the United States was 1.20 percent. In the three-state region, only 25 banks were unprofitable in 1995, and 67 percent of the banks reported higher net income than in 1994.

The improved earnings resulted from a continued increase in noninterest income and the
containment of overhead expense—helped by a reduction in deposit insurance premiums—which offset a small increase in provisions for loan losses. In addition, gains on securities contributed $14.5 million to net income for 1995, whereas securities losses of $117 million hampered earnings in 1994.

The net interest margin for banks in Louisiana, New Mexico and Texas remained fairly stable in 1995 and 1994, while loan growth continued at a rapid clip. Net interest margin was 4.4 percent for 1995 and 4.44 percent for 1994. Total loans grew at a median rate of 10.7 percent at banks in Louisiana, 8.7 percent at New Mexico's banks and 9.5 percent at banks in Texas. For the rest of the United States, median loan growth equaled 8.7 percent during 1995, and the net interest margin declined slightly, to 4.22 percent from 4.31 percent in 1994.

In the three District states, loan volume increased $18.4 billion, with real estate and business loans posting the biggest gains. Real estate loans were up $11 billion, with about 60 percent of this growth in the one- to four-family residential category. Most of the increase in real estate loans resulted from the transfer of loans into the region from affiliated organizations in other parts of the country. Commercial and industrial loans were up $5 billion, and consumer loans rose $2.7 billion. Agricultural loans showed an increase of $125 million.

Problem asset levels continued to recede relative to total assets. Only 0.81 percent of total loans and leases were noncurrent\(^1\) at year-end 1995, down from 0.83 percent a year earlier. Total troubled assets\(^2\) were 0.57 percent of gross assets, down from 0.63 percent, and remained lower than the troubled asset ratio of 0.86 percent for the rest of the United States.

Although overall asset quality indicators remained satisfactory for banks in the three-state region, net loan losses increased in 1995, reversing a six-year decline. Net loan losses rose to $321 million, or 0.24 percent of average loans, from $181 million, or 0.16 percent of average loans, in 1994. This increase was the result of higher net charge-offs of business and consumer loans, which both surpassed their 1994 levels by $72 million. Most of the 1995 charge-offs can be attributed to a few large banks that were involved in acquisitions.

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\(^1\)Noncurrent loans and leases are those that are 90 days past due or that are contractually past due but are considered as being current through the use of an extension of time arrangement or a modification of the contractual terms.

\(^2\)Total troubled assets include nonaccrual loans and leases, loans and leases 90 days past due and still accruing interest, and other loans and leases that management classifies as being impaired.

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**Figure:** Banking Offices in Louisiana, New Mexico and Texas

**Table:** Major Profitability Components for Insured Commercial Banks in Eleventh District States
In contrast, the real estate loan portfolio yielded small net recoveries in both 1995 and 1994 for banks in Louisiana, New Mexico and Texas. In the rest of the United States, net loan losses continued to decline, falling to 0.52 percent of average loans for 1995, down slightly from 0.54 percent for 1994.

Banks in Louisiana, New Mexico and Texas allowed their reserves for loan losses to decline slightly relative to noncurrent loans. The coverage ratio was 188 percent at year-end 1995, down from 202 percent at year-end 1994. The reserve account equaled 1.53 percent of total loans, down from 1.68 percent at year-end 1994. Outside the three District states, the reserve for loan losses was 2.06 percent of total loans and covered 174 percent of noncurrent loans at year-end 1995.

Sustained and robust loan growth in the region, coupled with a more gradual increase in deposits, has contributed to a tightening of liquidity. During 1995, total deposits increased by $3.9 billion in the three District states, while total loans grew by $18.4 billion. This imbalance caused the region's loan-to-deposit ratio to rise to 71 percent from 63 percent at the end of 1994.

The three states' largest banks drove the rising loan-to-deposit ratio. These banks made greater use of federal funds purchased and other borrowed money, while smaller banks managed to attract sufficient deposits or reduce federal funds sold. At year-end 1995, the loan-to-deposit ratio for banks with assets of $1 billion or more rose to 86 percent, up from 73 percent at the end of 1994. Banks with under $1 billion in assets had a loan-to-deposit ratio of just 53 percent at year-end 1995, up only slightly from 51 percent a year earlier. For banks in the rest of the country, the loan-to-deposit ratio was 85 percent at year-end 1995, having increased from 82 percent at year-end 1994.

Some funding was provided by a rising capital base, which was high relative to histor-
ical levels. For banks in Louisiana, New Mexico and Texas, equity capital grew by $2.2 billion in 1995—reaching 8.2 percent of total assets—even after a large dividend payout. Common stock dividends of $2 billion and preferred stock dividends of $1.6 million represented 64.4 percent of net income. For banks in the rest of the country, equity capital was 8 percent of total assets, up from 7.67 percent at year-end 1994, and the dividend payout ratio was 63.82 percent.

—Karen Couch

1 Noncurrent loans and leases are those past-due 90 days or more plus those on nonaccrual status.

2 Troubled assets comprise noncurrent loans and leases plus other real estate owned.
THE OVERALL CONDITION of bank holding companies (BHCs) in Louisiana, New Mexico and Texas remained good in 1995, based on a review of consolidated earnings, asset quality and capital levels, and parent company debt-to-equity ratios.

The three states contained 608 top-tier BHCs, but generally only those with total consolidated assets of $150 million or more were required to report consolidated financial data. Those reports formed the basis of this analysis.
In Louisiana, there were 19 such BHCs, with a combined $23.3 billion in total consolidated assets. Net income of $304.5 million yielded a return on average assets of 1.44 percent. For 1995, reductions in overhead expense and securities losses helped offset a higher provision expense. Total assets have held stable in the 1990s for Louisiana BHCs, but equity capital has nearly doubled—from $1.2 billion, or 5.14 percent of total assets in 1990, to $2.3 billion, or 9.96 percent of total assets at year-end 1995. The large increase in equity capital resulted primarily from retained earnings. Further enhancing capital accounts in 1995 were net unrealized gains on available-for-sale securities of $55.4 million. In contrast, at year-end 1994, Louisiana BHCs reported net unrealized losses of $153.6 million. With a comfortable capital cushion and solid earnings performance, Louisiana BHCs substantially increased their common stock dividend payout for 1995. Common stock dividends totaled $98 million, or 32.17 percent of net income, a hefty increase from $72 million, or 21.33 percent of net income, in 1994.

New Mexico had 11 BHCs; their combined assets were $3.2 billion. New Mexico BHCs reported net income of $39.3 million, for a return on average assets of 1.26 percent. Lower overhead expenses in 1995 resulted in an improvement over 1994’s earnings performance. Retained earnings and small net unrealized gains on available-for-sale securities caused equity capital to rise. At year-end 1995, equity capital was $276.8 million, or 8.74 percent of total assets. Common stock dividends were $8.9 million. The common stock dividend payout ratio remained basically unchanged from 1994 at 23.21 percent of net income.

Texas had 91 BHCs with a combined $39.1 billion in assets. Their net income of $460.9 million represented a return on average assets of 1.26 percent. Texas BHCs relied on higher net interest income and higher noninterest
Bank Holding Companies with Total Consolidated Assets of More Than $1 Billion

<table>
<thead>
<tr>
<th>Company</th>
<th>Location</th>
<th>Total assets</th>
<th>Return on average assets (percent)</th>
<th>Equity capital to total assets (percent)</th>
<th>Asset growth rate (percent)</th>
</tr>
</thead>
<tbody>
<tr>
<td>First Commerce Corp.</td>
<td>New Orleans, La.</td>
<td>$8,542,829</td>
<td>1.04</td>
<td>8.58</td>
<td>25.59</td>
</tr>
<tr>
<td>Hibernia Corp.</td>
<td>New Orleans, La.</td>
<td>7,196,169</td>
<td>1.82</td>
<td>9.97</td>
<td>13.58</td>
</tr>
<tr>
<td>Cullen/Frost Bankers, Inc.</td>
<td>San Antonio, Texas</td>
<td>4,181,093</td>
<td>1.17</td>
<td>8.17</td>
<td>9.08</td>
</tr>
<tr>
<td>Whitney Holding Corp.</td>
<td>New Orleans, La.</td>
<td>3,154,147</td>
<td>1.36</td>
<td>10.70</td>
<td>8.20</td>
</tr>
<tr>
<td>International Bancshares Corp.</td>
<td>Laredo, Texas</td>
<td>2,935,613</td>
<td>1.40</td>
<td>8.37</td>
<td>10.39</td>
</tr>
<tr>
<td>Victoria Bankshares, Inc.</td>
<td>Victoria, Texas</td>
<td>1,972,685</td>
<td>.82</td>
<td>9.65</td>
<td>13.01</td>
</tr>
<tr>
<td>Laredo National Bancshares, Inc.</td>
<td>Laredo, Texas</td>
<td>1,629,485</td>
<td>1.09</td>
<td>8.49</td>
<td>-1.84</td>
</tr>
<tr>
<td>First Financial Bankshares, Inc.</td>
<td>Abilene, Texas</td>
<td>1,062,334</td>
<td>1.62</td>
<td>10.82</td>
<td>4.91</td>
</tr>
</tbody>
</table>

Bank Holding Company Income Stream Components as a Percentage of Average Assets

<table>
<thead>
<tr>
<th>Component</th>
<th>Louisiana 12/31/94</th>
<th>Louisiana 12/31/95</th>
<th>Louisiana Basis-point change</th>
<th>New Mexico 12/31/94</th>
<th>New Mexico 12/31/95</th>
<th>New Mexico Basis-point change</th>
<th>Texas 12/31/94</th>
<th>Texas 12/31/95</th>
<th>Texas Basis-point change</th>
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</thead>
<tbody>
<tr>
<td>Interest income</td>
<td>7.09</td>
<td>7.84</td>
<td>75</td>
<td>7.18</td>
<td>8.02</td>
<td>84</td>
<td>6.52</td>
<td>7.36</td>
<td>84</td>
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<tr>
<td>Interest expense</td>
<td>2.49</td>
<td>3.16</td>
<td>67</td>
<td>2.54</td>
<td>3.23</td>
<td>69</td>
<td>2.33</td>
<td>3.05</td>
<td>72</td>
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<tr>
<td>Net interest income</td>
<td>4.60</td>
<td>4.68</td>
<td>8</td>
<td>4.65</td>
<td>4.79</td>
<td>14</td>
<td>4.19</td>
<td>4.32</td>
<td>13</td>
</tr>
<tr>
<td>Noninterest income</td>
<td>1.61</td>
<td>1.55</td>
<td>-6</td>
<td>.91</td>
<td>.83</td>
<td>-8</td>
<td>1.38</td>
<td>1.46</td>
<td>8</td>
</tr>
<tr>
<td>Provision expense</td>
<td>-26</td>
<td>.11</td>
<td>37</td>
<td>.08</td>
<td>.11</td>
<td>3</td>
<td>.07</td>
<td>.15</td>
<td>8</td>
</tr>
<tr>
<td>Overhead expense</td>
<td>4.28</td>
<td>4.08</td>
<td>-20</td>
<td>3.78</td>
<td>3.39</td>
<td>-39</td>
<td>3.68</td>
<td>3.69</td>
<td>1</td>
</tr>
<tr>
<td>Securities gains (losses)</td>
<td>-20</td>
<td>-.04</td>
<td>16</td>
<td>-.07</td>
<td>-.01</td>
<td>6</td>
<td>-.02</td>
<td>0</td>
<td>2</td>
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<tr>
<td>Other tax-equivalent adjustments</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Pretax net operating income</td>
<td>1.99</td>
<td>2.00</td>
<td>1</td>
<td>1.60</td>
<td>2.04</td>
<td>44</td>
<td>1.81</td>
<td>1.94</td>
<td>13</td>
</tr>
<tr>
<td>Applicable income taxes</td>
<td>.57</td>
<td>.56</td>
<td>-1</td>
<td>.54</td>
<td>.73</td>
<td>19</td>
<td>.62</td>
<td>.68</td>
<td>6</td>
</tr>
<tr>
<td>Minority interest</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>.03</td>
<td>.04</td>
<td>1</td>
<td>.01</td>
<td>.01</td>
<td>0</td>
</tr>
<tr>
<td>Extraordinary items, net</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>-.02</td>
<td>-2</td>
<td>0</td>
<td>0</td>
<td>0</td>
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<tr>
<td>Return on average assets</td>
<td>1.43</td>
<td>1.44</td>
<td>1</td>
<td>1.02</td>
<td>1.26</td>
<td>24</td>
<td>1.19</td>
<td>1.26</td>
<td>7</td>
</tr>
<tr>
<td>Number of bank holding companies</td>
<td>21</td>
<td>19</td>
<td>12</td>
<td>11</td>
<td>83</td>
<td>91</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
income in 1995, as earnings edged up over their 1994 level. Equity capital of $3.4 billion equaled 8.67 percent of total assets. Net unrealized gains on available-for-sale securities added $46.7 million to capital accounts, whereas a year earlier, net unrealized losses of $125.8 million had a negative impact on capital. Common stock dividends were $74.6 million and equaled 16.19 percent of net income, which was roughly even with the 1994 level.

BHCs in all three states reported satisfactory asset quality. Nonaccrual loans and real estate acquired in satisfaction of debts previously contracted equaled less than 1 percent of total loans plus real estate acquired for debts previously contracted for BHCs in Louisiana and New Mexico. For Texas BHCs, this figure dropped 28 basis points to 1.03 percent. However, net loan losses rose in all three states. Louisiana BHCs, which had net recoveries for 1994, had net charge-offs of 0.22 percent of average loans for 1995. For New Mexico's BHCs, net charge-offs were 0.13 percent of average loans, up from 0.01 percent for 1994. And in Texas, net charge-offs were 0.21 percent of average loans, up from 0.14 percent the previous year.

At the parent-company-only level, debt-to-equity ratios remained low for BHCs of all sizes. Debt-to-equity ratios were 4.32 percent for large BHCs in Louisiana, 7.71 percent in New Mexico and 3.11 percent in Texas. For small BHCs—those with consolidated assets of less than $150 million—debt-to-equity ratios were 3.31 percent in Louisiana, 14 percent in New Mexico and 8.82 percent in Texas.

BHCs in the three states held 698 bank subsidiaries, which represented 38 percent of banking industry assets in the region. In comparison, BHCs located out of state controlled
88 bank subsidiaries, which represented 52 percent of the banking assets in Louisiana, New Mexico and Texas. The 402 independent banks within the three states held the remaining 10 percent of industry assets.

The growing presence of out-of-state banking organizations in Louisiana, New Mexico and Texas is consistent with the general trend for the United States as a whole. In 1990, more than 50 percent of the banking assets in 12 states and the District of Columbia were held by out-of-state BHCs. By year-end 1995, out-of-state banking organizations controlled the majority of the banking assets in 23 states and the District of Columbia.

— Olga N. Zograf
Karen Couch
Foreign Agency Market Share of Commercial Loans in Texas

* Foreign agency market share is 24.8 percent when commercial loans booked at the agencies' offshore branches are included.
1995 was a record-breaking year for foreign banks operating in Texas. Lending activity reached new heights, despite a reduction in the number of foreign banks operating in the state. And if the levels of unfunded loan commitments are any indication, foreign banks will capture more commercial loan market share in the future.

Foreign banks that want a U.S. presence are permitted to establish branches, agencies, representative offices, Edge Act or agreement corporations, or subsidiaries. In the three Eleventh District states, foreign banks have established a presence through agencies and representative offices located in Dallas and Houston. Agencies are permitted to lend funds and maintain credit balances incidental to their commercial banking activities, but Texas law prohibits them from accepting deposits and offering fiduciary services. Representative offices are marketing offices, which act as liaisons between the parent company and corporate borrowers. These offices do not book loans or deposits but generally administer the loan portfolio their marketing activities have generated.
<table>
<thead>
<tr>
<th>Bank name</th>
<th>Home country</th>
<th>Year commenced business in Texas</th>
</tr>
</thead>
<tbody>
<tr>
<td>Arab Banking Corp., B.S.C.</td>
<td>Bahrain</td>
<td>1964</td>
</tr>
<tr>
<td>Bank of Montreal</td>
<td>Canada</td>
<td>1967</td>
</tr>
<tr>
<td>The Bank of Nova Scotia</td>
<td>Canada</td>
<td>1985</td>
</tr>
<tr>
<td>Canadian Imperial Bank of Commerce</td>
<td>Canada</td>
<td>1985</td>
</tr>
<tr>
<td>National Bank of Canada</td>
<td>Canada</td>
<td>1985</td>
</tr>
<tr>
<td>The Toronto-Dominion Bank</td>
<td>Canada</td>
<td>1989</td>
</tr>
<tr>
<td>Banque Francaise du Commerce Exterieur</td>
<td>France</td>
<td>1979</td>
</tr>
<tr>
<td>Banque Nationale de Paris</td>
<td>France</td>
<td>1991</td>
</tr>
<tr>
<td>Banque Paribas</td>
<td>France</td>
<td>1986</td>
</tr>
<tr>
<td>Caisse Nationale de Credit Agricole</td>
<td>France</td>
<td>1996</td>
</tr>
<tr>
<td>Credit Lyonnais</td>
<td>France</td>
<td>1977</td>
</tr>
<tr>
<td>Societe Generale</td>
<td>France</td>
<td>1986</td>
</tr>
<tr>
<td>Hongkong and Shanghai Banking Corp., Ltd.</td>
<td>Hong Kong</td>
<td>1986</td>
</tr>
<tr>
<td>Banca di Roma S.P.A.</td>
<td>Italy</td>
<td>1989</td>
</tr>
<tr>
<td>The Bank of Tokyo–Mitsubishi, Ltd.</td>
<td>Japan</td>
<td>1985</td>
</tr>
<tr>
<td>The Dai-ichi Kangyo Bank, Ltd.</td>
<td>Japan</td>
<td>1976</td>
</tr>
<tr>
<td>The Fuji Bank, Ltd.</td>
<td>Japan</td>
<td>1985</td>
</tr>
<tr>
<td>The Industrial Bank of Japan, Ltd.</td>
<td>Japan</td>
<td>1979</td>
</tr>
<tr>
<td>The Long-Term Credit Bank of Japan, Ltd.</td>
<td>Japan</td>
<td>1984</td>
</tr>
<tr>
<td>The Sakura Bank, Ltd.</td>
<td>Japan</td>
<td>1991</td>
</tr>
<tr>
<td>The Sanwa Bank, Ltd.</td>
<td>Japan</td>
<td>1977</td>
</tr>
<tr>
<td>The Sumitomo Bank, Ltd.</td>
<td>Japan</td>
<td>1986</td>
</tr>
<tr>
<td>Banco Nacional de México</td>
<td>Mexico</td>
<td>1987</td>
</tr>
<tr>
<td>ABN AMRO Bank N.V., Inc.</td>
<td>Netherlands</td>
<td>1986</td>
</tr>
<tr>
<td>MeesPierson, N.V.</td>
<td>Netherlands</td>
<td>1994</td>
</tr>
<tr>
<td>Rabobank Nederland</td>
<td>Netherlands</td>
<td>1987</td>
</tr>
<tr>
<td>Den norske Bank, AS</td>
<td>Norway</td>
<td>1979</td>
</tr>
<tr>
<td>Riyad Bank</td>
<td>Saudi Arabia</td>
<td>1990</td>
</tr>
<tr>
<td>Credit Suisse</td>
<td>Switzerland</td>
<td>1977</td>
</tr>
<tr>
<td>Union Bank of Switzerland</td>
<td>Switzerland</td>
<td>1986</td>
</tr>
<tr>
<td>The International Commercial Bank of China</td>
<td>Taiwan</td>
<td>1980</td>
</tr>
<tr>
<td>Bank of Scotland</td>
<td>United Kingdom</td>
<td>1975</td>
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<tr>
<td>National Westminster Bank</td>
<td>United Kingdom</td>
<td>1977</td>
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</table>

Thirty-three foreign banks from 13 countries have operations in Texas. Initially, foreign banks came to Texas to take advantage of the energy industry, but they quickly began diversifying into other areas once they were in the state. Now, foreign banks tend to target companies in the Southwest with annual revenues of more than $200 million. Japanese banks have the largest presence in Texas, with French banks trailing closely. At year-end 1995, seven
Japanese agencies held 45 percent of total assets of foreign agencies in Texas. Three French banks held 32 percent of total assets.

Since year-end 1994, the number of foreign banks operating in the state has fallen. Three foreign banks ceased operations in Texas altogether. Credito de Italiano of Italy closed its Houston representative office in September 1995, and Standard Chartered Bank of Great Britain closed its Houston agency in December 1995. Both organizations currently have operations in other parts of the United States. Daiwa Bank of Japan was forced to terminate all U.S. operations in February 1996 because of a cover-up involving securities losses. The assets of Daiwa's U.S. operations were subsequently purchased by Sumitomo Bank of Japan, and Sumitomo reopened Daiwa's Texas operations as representative offices. Finally, the April 1996 merger of two Japanese powerhouses, the Bank of Tokyo and Mitsubishi Bank, resulted in the closure of the Bank of Tokyo's Houston representative office. The new organization, the Bank of Tokyo-Mitsubishi Ltd., now operates an agency in Houston and a representative office in Dallas. The state had one new entrant in 1995—Caisse Nationale de Credit Agricole of France opened a representative office in Houston. After these changes, Texas is home to 17 foreign agencies and 26 representative offices, all in either Houston or Dallas.

Despite the contraction in the number of foreign banks operating in the state, the agencies have been pumping up their balance sheets for the past two years. Total assets at Texas' foreign agencies reached a peak of $10.5 billion at year-end. Additionally, some foreign banks have offshore branches (primarily in the Cayman Islands) that are managed by agencies located in Texas. At year-end 1995, the offshore branches associated with the state's agencies reported total assets of $14.5 billion, bringing the total assets held by foreign banks in Texas to $25 billion.¹

Asset growth at foreign agencies in Texas was spurred by commercial loan growth, a reflection of foreign agencies' wholesale nature. Commercial loans accounted for 91 percent of total assets at agencies in the state, versus 25 percent at foreign branches and agencies elsewhere in the United States. The aggregate total of outstanding commercial loans at the state's agencies reached $9.5 billion.
at year-end, for an increase of almost 33 percent over year-end 1994. Commercial loan growth at Texas foreign agencies considerably outpaced the 15-percent loan growth at foreign branches and agencies elsewhere in the United States. According to the Federal Reserve’s January 1996 Senior Loan Officer Opinion Survey on Bank Lending Practices, foreign branches and agencies indicated large corporations’ need for merger and acquisition financing is driving the increased demand.

In 1995, foreign agencies operating in Texas held 21 percent of the state’s commercial loan market. When adjusted for commercial loans booked at the offshore branches, year-end 1995 market share was almost 25 percent. These market share figures, however, are based on a very narrow definition: the percentage of commercial loans held by foreign agencies relative to all commercial loans in Texas. Two important factors can distort the market share figures. First, when looking at the market share of Texas’ foreign agencies, it is important to remember that the agencies are active participants in loan syndications and may be booking loans that did not originate in the region. Second, loans may be originated by foreign agencies or representative offices in Texas but booked at related branches or agencies in other parts of the country.

In general, foreign agencies do not directly compete with most of the state’s banks. Foreign agencies and representative offices tend to limit their customer base to large corporations, whereas the majority of commercial banks in Texas are more likely to lend to small business and retail customers.

The remarkable increase in lending over the past year has not been detrimental to the agencies’ asset quality. In fact, asset quality at the state’s foreign agencies improved in 1995, with total noncurrent loans accounting for 0.23 percent of total loans, down from 0.69 percent at year-end 1994.

Many foreign banks operating in the United States are also active in offering contingent liabilities, such as lines of credit and standby letters of credit, and trading in the derivatives markets. These products enable foreign branches and agencies to offer services that produce fee income and have no effect on the banks’ legal lending limits. Foreign branches and agencies operating in the United States operate on
the consolidated equity of their parent banks.

In Texas, foreign agencies tend to limit off-balance-sheet activities to loan commitments and standby letters of credit. Most derivatives activities are consolidated at offices elsewhere in the United States. The consolidated unfunded loan commitments reported at year-end 1995 totaled $15 billion, which equaled 145 percent of total assets. Over the year, loan commitments increased almost 30 percent, a possible indication of future growth. While the state’s agencies have been active in issuing standby letters of credit in the past, in 1995 standby letters of credit decreased 23 percent.

Because foreign agencies operating in Texas are prohibited by state law from accepting deposits, funding is mostly provided through borrowings from related offices located elsewhere in the United States. At year-end 1995, borrowings from related U.S. offices totaled almost $10 billion, which equaled 94 percent of total assets. Funding at offshore offices managed by the state’s agencies tends to be more diverse, coming from both related and nonrelated offices in the United States and the banks’ home countries.

Foreign banks operating in Texas have proved themselves an essential source of funding and international services for large corporations and multinational firms in the Southwest. By taking advantage of the economic growth in the region and increased merger and acquisition activity last year, foreign banks in Texas experienced their highest rate of asset growth since 1991.

—Susan Tetley

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1 Foreign banks often establish nonbanking entities in the United States, such as securities dealers, foreign exchange houses and nonbank credit-extending subsidiaries. A number of these organizations operate in Texas, but information on their activities and size is extremely limited. Available data as of year-end 1995 on nonbanking organizations owned by foreign banks in Texas revealed that these organizations held assets totaling almost $9 billion. When the assets held at these nonbanking offices are included in the calculation, total assets held by foreign banks operating in Texas reached $34 billion at year-end 1995.

2 Noncurrent loans are the sum of loans at least 90 days past due plus those on nonaccrual status.
Credit Unions in Eleventh District states continued to focus on improving their loan portfolios in 1995, mostly by targeting automobile loans. To fund loan growth, regional credit unions raised deposit rates, attracting share certificates in particular. Higher funding costs, however, lowered regional credit union profitability.

A total of 1,191 federally insured credit unions, ranging in size from $15,000 to $1.8 billion in total assets, were operating in the three-state region as of year-end 1995. These credit unions accounted for a $28 billion segment of the regional financial marketplace, with most of the largest
credit unions located in Texas. Nationwide, there were 11,680 credit unions holding $307 billion in assets as of year-end 1995.

Membership at credit unions in Louisiana, New Mexico and Texas was 6.6 million at the end of 1995, up 4.2 percent over the 1994 year-end level. Unlike commercial banks and thrifts, federally insured credit unions are nonprofit institutions whose membership is limited by the common bond restrictions of the 1934 Federal Credit Union Act. In 1993 and 1994, the National Credit Union Administration broadened its interpretation of the common bond restriction, resulting in a large increase in the membership base of credit unions. During 1995, the customer base of regional credit unions increased to 18.7 million potential members, up 0.5 percent over the year-end 1994 level and 13.7 percent over the year-end 1993 level. The increases in both current and potential membership left the ratio of current to potential members at about 35 percent for credit unions in the three Eleventh District states.

Double-digit loan growth rates over the past four years led to a slight increase in delinquent loans and loan defaults last year at credit unions in the Eleventh District states. Delinquent loans increased to 1.01 percent of total loans as of year-end 1995, and loan defaults increased to 0.36 percent of average loans. Total troubled assets, which include delinquent loans and repossessed real estate, increased to $191 million, or 0.67 percent of assets, as of year-end 1995. At Louisiana credit unions, troubled assets accounted for 1.04 percent of assets, compared with 0.45 percent and 0.63 percent for credit unions in New Mexico and Texas, respectively.

Loan portfolios at credit unions in this region and elsewhere in the United States have been expanding at a fairly fast pace, with growth rates approaching or exceeding 10 percent. Recent loan growth among regional credit unions has been concentrated in auto loans, which expanded $1.7 billion, or 24 percent, during 1994 and an additional $1.3 billion, or 15 percent, during 1995. Auto loans increased to 56 percent of regional credit union loans as of year-end 1995, while real estate, unsecured and other loans each declined as a proportion of total loans. Although auto loans also increased at credit unions nationwide, they accounted for only 38 percent of loans at credit unions located outside the Eleventh District states. These credit unions devote a greater proportion of their loan portfolios to real estate loans than do credit unions located in this region—34 percent versus 16 percent as of December 31, 1995.
After increasing slightly in the first half of 1995, regional credit union investments fell to $8.7 billion, $439 million lower than at year-end 1994. While, investments in U.S. agency securities, mutual funds and corporate credit unions together increased $326 million, this increase was offset by a $765 million decline in holdings of U.S. government obligations and other investments.

To fund asset growth, credit unions attempted to attract more savings by raising deposit rates. Deposits, or shares as credit unions refer to them, increased $1.6 billion, or 7 percent, during 1995. Regional credit unions were particularly successful in attracting share certificates, which are similar to bank certificates of deposits. These accounts increased $1.7 billion, or 50 percent, as the average rate paid by regional credit unions for these funds increased from 4.4 percent in 1994 to 5.3 percent in 1995.

Higher deposit rates led to a higher cost of funds for regional credit unions, hampering overall earnings performance. For the three District states combined, the return on assets declined to 0.94 percent for 1995 from 1.06 for 1994. The returns for credit unions in Louisiana and New Mexico remained roughly even with their 1994 values, while the profitability of Texas credit unions declined.

Louisiana credit unions continued to outperform credit unions in the remainder of this region as well as those located elsewhere in the United States, earning net income after cost of funds and net statutory reserve transfers of $45 million during 1995, for a return on assets of 1.35 percent. With net income of $21 million and a return on assets of 1.03 percent, New Mexico credit unions also turned in a strong performance. Texas credit unions earned net income of $195 million for a 0.87-percent return on assets.
Capital levels among credit unions in Louisiana, New Mexico and Texas continued to increase through 1995. Earnings retention increased the equity capital ratio for credit unions in these three states as a group to 10.1 percent as of year-end 1995, compared with 9.4 percent at year-end 1994. At 12.1 percent, the capital ratio for Louisiana credit unions exceeded that of credit unions in the other Eleventh District states and those located elsewhere in the United States. Capital ratios for credit unions in New Mexico and Texas were around 9.8 percent at year-end 1995, compared with 10.3 percent for credit unions located outside the region.

—Kelly Klemme
THRIFTS IN LOUISIANA, NEW MEXICO AND TEXAS reported increases in assets, loans and deposits during 1995, even as thrifts continued to decline in number. Increases in mortgage loans and consumer loans fueled overall asset growth and contributed to a strong earnings performance.

As of year-end 1995, 89 thrifts holding $57.4 billion in total assets were operating in the three Eleventh District states, compared with 100 thrifts holding $54.9 billion in assets at year-end 1994. Four savings and loans converted to state savings banks during 1995, and seven other institutions were either acquired or converted to branches. Nationwide, there were 1,433 thrifts holding assets of $753.3 billion as
Thrift Industry Profitability

Return on assets, percent

Louisiana
New Mexico
Texas
Rest of the United States


NOTE: The return on assets is the ratio of net income after tax to average assets.

During 1995, thrifts in the three Eleventh District states were more profitable than thrifts located elsewhere in the United States. Louisiana thrifts earned net income of $37 million in 1995 for a return on assets of 0.98 percent, New Mexico thrifts earned net income of $14 million for a return of 1.17 percent, and Texas thrifts earned net income of $569 million for a return of 1.10 percent. Thrifts outside the three Eleventh District states earned a return on assets of 0.69 percent during 1995.

Higher noninterest income and lower noninterest expense helped boost the regional thrift industry's profitability during 1995. Together, thrifts in Louisiana, New Mexico and Texas earned an annualized return on assets of 1.10 percent during 1995, compared with 0.90 percent for 1994. Noninterest income increased to an annualized 0.95 percent of average assets in 1995, 32 basis points higher than in 1994. Regional thrifts more than recovered their 1994 losses on the sale of both assets held for sale and available-for-sale securities, contributing 17 basis points to the improvement in noninterest income. In addition, overhead expenses fell to 2.06 percent of average assets in 1995, 17 basis points lower than in 1994.

Together, these improvements boosted profitability 49 basis points and were more than enough to offset a decline in net interest income, reduced gains on the sale of repossessed assets and other assets held for investment, and an increase in provision expense. As a percentage of average assets, the spread between interest income and interest expense narrowed to 2.49 percent during 1995 from 2.59 percent in 1994 as increases in interest expense exceeded increases in interest income. And provision expense grew to 0.22 percent of average assets during 1995 from 0.12 percent in 1994. Most of the region's thrifts—97 percent—were profitable during 1995, up from 94 percent during 1994.

Asset quality indicators among regional thrifts remained good through 1995. Noncurrent loans and repossessed real estate at Texas thrifts declined to $558 million, or 1.02 percent of assets, as of year-end 1995. Among thrifts in New Mexico, troubled assets equaled $12 million, or 0.90 percent of assets. And Louisiana
thrifts reported the lowest concentration of troubled assets among the three District states at $18 million, or 0.46 percent of assets. Among private-sector thrifts located elsewhere in the United States, the troubled asset ratio equaled 1.23 percent as of year-end 1995.

Regional thrift industry loan volume has been increasing steadily since the third quarter of 1994. During 1995, loans outstanding increased $4 billion, or 11.6 percent. Mortgage loan originations exceeded loan sales and boosted regional thrifts' mortgage loan holdings by $2.9 billion to a total of $32.4 billion. Most of the increase in mortgage loans can be attributed to growth in adjustable rate loans secured by one- to four-family residences. Consumer loans were up $1 billion, and commercial loans, after falling $126 million in 1994, increased $207 million during 1995.

Regional thrifts continued to shift their asset mix from securities to loans in 1995 and used deposits and other liabilities to help fund loan growth. Regional thrifts' securities portfolios declined by $2.3 billion during 1995. Deposits increased $1.3 billion, and other liabilities, which include subordinated debt and other security issues, increased $550 million.

A growing equity base also has provided funding. As of year-end 1995, the ratio of equity capital to assets among regional thrifts equaled 7.3 percent, up from 6.8 percent at year-end 1994. Moreover, all thrifts in Louisiana, New Mexico and Texas were considered at least "adequately capitalized" based on risk-based capital guidelines.

—Kelly Klemme
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