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Houston Business

A Perspective on the Houston Economy

Mergers and Federal Rescues Forged Largest Texas Banks

Old newspaper files and clippings tell the story of banking problems in the 1980s. It is hard to imagine a more difficult banking environment.

Most of the large banks and bank holding companies in Houston and Texas returned to profitability over the past two years, effectively turning the page on the 1980s. In 1982, the largest Texas banks were rated among the soundest and fastest-growing in the nation. The well-known story of their swift fall from grace, outlined in Table 1, forced a wave of interstate mergers and regulatory rescues.

Old newspaper files and clippings tell the story of banking problems in the 1980s. It is hard to imagine a more difficult banking environment: high real interest rates, a one–two blow from oil prices and then real estate, archaic unit banking laws and deregulation of savings and loan associations that created a free-wheeling competitor.

Although solid profits over the past couple of years make this article a history lesson for most Texas banking survivors, the story assumes new relevance as bank problems continue in other parts of the nation. Clippings tell the story as reported in the *Houston Post* (HP), the *Wall Street Journal* (WSJ) and the *New York Times* (NYT).

> It is now becoming clear that energy lending is the banking industry's biggest debacle since the Depression. . . .On October 7, for instance, InterFirst Corp. of Dallas stunned banking circles by announcing the largest quarterly loss in U.S. banking history. It blamed bad energy loans.
>
> —*WSJ*, November 14, 1983

> [InterFirst] concentrated on loans to small and medium-sized service companies, which

drill wells and make various equipment. When energy prices began falling in 1982, these companies' revenues virtually disappeared....Real estate is [now] particularly important to InterFirst because it offered lending opportunities even after energy loans went bad.

—*WSJ*, August 6, 1985

[Texas Commerce] said net income would decline 35 percent....The news stunned the financial markets and caused not only Texas Commerce's stock to fall, but also the stocks of the other banking companies that are heavy lenders to the energy industry. Texas Commerce and J.P. Morgan & Company in New York....are the only two bank holding companies in the United States with the highest triple-A bond rating from Standard & Poor's.

—*NYT*, March 19, 1985

Federal banking authorities, concerned about the ability of banks in the oil patch to survive the collapse of oil prices, are preparing contingency rescue plans....At the same time, regulators are asking Congress to liberalize a current emergency acquisition law to permit out-of-state institutions to acquire bank holding companies.

—*WSJ*, April 3, 1986

InterFirst bankers have been slowly working their way out of one of the nation's biggest energy loan debacles....InterFirst's top officials believe that the worst is behind it....But the uncertain future may hold dangers for Texas....The oil price free fall may not be over, and the Texas real estate market, the other big source of InterFirst's loan headaches, is reeling.

—*WSJ*, April 30, 1986

And with 17.8% of total loans to the oil industry, First City has a greater exposure than any other major Texas bank holding company to fallout spreading across Texas from the four-year-old slump in energy prices....There are also concerns about the company's $3.49 billion real estate portfolio, which so far hasn't been a source of large loan losses....First City's real estate portfolio could be vulnerable to some shocks.

—*WSJ*, July 7, 1986

The First National Bank & Trust Co. of Oklahoma City was closed yesterday by federal regulators, marking the second-largest commercial bank failure in the U.S....[O]ther Southwest banks are under pressure to keep deposits...But the overall situation isn't yet grave....[One bank analyst] says, "There isn't another problem out there of this size."

—*WSJ*, July 15, 1986

With an energy portfolio about half the size of its two biggest Houston competitors, Allied is less imperiled by the collapse of oil prices....Allied's $2.2 billion real estate portfolio—with heavy exposure in the depressed Dallas and Houston markets—is its biggest headache. Real estate loans recently surpassed energy loans as the major source of problem credits.

—*WSJ*, July 21, 1986

[O]nly 10% of [Republic's] loan portfolio is in energy, one of the smallest percentages among Texas banks....Market analysts expect RepublicBank to be marginally profitable in 1986, but that could change if oil prices remain low and if Texas real estate values deteriorate sharply.

—*WSJ*, July 21, 1986

Stock prices of nearly all major Texas bank holding companies spurted yesterday in active trading, as the Texas Senate approved a sweeping interstate banking measure designed to allow out-of-state institutions to acquire Texas banks and thrifts.

—*WSJ*, August 21, 1986

Texas Commerce Bancshares Inc. said Monday it has agreed to a $1.19 billion proposed merger with Chemical New York Corp., the first of what analysts say could be a march of other big and medium-sized banks to the altar...[TCB's] nonperforming assets are concentrated mainly in real estate rather than energy.

—*HP*, December 16, 1986

The acquisition this week of the oil capital's biggest bank...is symbolic of the radical reversal in the fortunes of a once-swaggering region whose economy has also lost its independence....For years, Texas Commerce and other Houston banks tended to back promising local entrepreneurs from the start of their careers, building close business relationships that lasted for decades.

—*WSJ*, December 17, 1986

When RepublicBank and InterFirst....announced their merger this week, Wall Street booed....But here in Dallas, city leaders rallied around the deal....Business leaders here point out that a RepublicBank–InterFirst combination would give the city a heavy weight financial

Table 1
Largest Bank Holding Companies in Texas in the Early 1980s

***Allied Bancshares Inc.*—Acquired by First Interstate Bancorp, Los Angeles, in January 1988 without federal assistance.**

***Cullen/Frost Bankers Inc.*—Operating profitably without federal assistance.**

***First City Bancorporation of Texas*—Received $1 billion infusion from Federal Deposit Insurance Corp. (FDIC) in September 1987; reorganized under management of outside group that raised $500 million in new capital.**

***InterFirst Corporation*—Federally assisted takeover by NCNB Corp. in July 1988; assisted by FDIC with a $1 billion cash infusion in March 1988; had merged with RepublicBank in March 1987 to become First RepublicBank Corp.**

***Mercantile Texas Corp.*—Federally assisted takeover of most banks by Banc One, Corp., Columbus, Ohio, in June 1989; taken over by FDIC in March 1989; merged with Southwest Bancshares Inc. in October 1984 to form MCorp.**

***RepublicBank Corporation*—See InterFirst Corporation above. Merged with InterFirst in March 1987 to become First RepublicBank Corp.**

***Southwest Bancshares Inc.*—See Mercantile Texas Corp. Merged with Mercantile Texas in October 1984 to form MCorp.**

***Texas Commerce Bancshares*—Acquired by Chemical Banking Corp, New York, in May 1987 without federal assistance.**

institution....The biggest worry...is that continued weakness in the Texas economy will produce a fresh wave of loan write-downs in 1987 from commercial real estate problems.

—*NYT*, December 20, 1986

Texas Commerce Bancshares, Inc. has chosen a charter through which it will liquidate $300 million of assets....Texas Commerce and Chemical...propose to identify the loan-liquidation operation as the National Loan Bank....National Loan's sole function will be to warehouse and liquidate...nonperforming and potentially nonperforming loans and related assets.

—*HP*, March 28, 1987

Allied becomes the second major bank holding company to agree to be acquired by an out-of-state organization....[T]he value of Allied's merger with First Interstate will depend on Allied's performance in the next five years. The merger also includes creation of a special bank to liquidate Allied's problem assets.

—*HP*, May 22, 1987

The Federal Deposit Insurance Corporation Wednesday announced a $1 billion bailout package to keep Houston's First City Bancorporation of Texas—burdened with bad energy and real estate loans—from closing its doors...[T]he FDIC has lined up a team of private investors...to pour in $500 million new capital and take over the bank, leaving current shareholders owning less than 3 percent.

—*HP*, September 10, 1987

Federal bank regulators announced today that they would inject $1 billion cash into the subsidiary of the First RepublicBank Corporation of Dallas in an effort to stop a huge outflow of deposits and a widespread loss of confidence....The action...was described as a temporary measure taken until a permanent solution was found.

—*NYT*, March 18, 1988

NCNB Corp., North Carolina banking's biggest winner, is betting the bank on First RepublicBank of Dallas—Texas banking's biggest loser...NCNB, based in Charlotte, N.C., thus becomes the newest out-of-stater to seize a share of the spoils of the devastated Texas banking industry.

—*WSJ*, August 1, 1988

First RepublicBank's road to ruin was charted just 19 months ago when the two Dallas banking rivals...teamed up to fend off the possibility of InterFirst being acquired by an out-of-state bank....[O]nly two of Texas top 10 banking companies have survived without a government rescue or a takeover from a better capitalized company: MCorp...based in Dallas, and San Antonio's Cullen/Frost Bankers Inc. While Cullen/Frost appears out of danger, MCorp...is struggling to raise capital without federal aid.

—*WSJ*, August 1, 1988

Banc One Corp., in a stunning entry into the Texas market, won the bidding war for MCorp's failed banks....The FDIC will pay as much as $2 billion to insulate Banc One from Bridge Bank's portfolio of soured loans....The FDIC will fill in the bank's negative net worth and then capitalize it with a $500 million injection of equity, which will eventually be acquired by Banc One.

—*WSJ*, June 29, 1989

Southwestern banks continued their modest recovery in the first quarter....Indeed, compared with some New England banks, which have taken massive charges against real-estate loans in recent months, Southwestern banks are almost beginning to look solid.

—*WSJ*, April 6, 1990

The Houston economy continues to mark time, waiting for some stimulus from a national expansion. Oil and gas exploration continued to deteriorate at the end of 1991, and 1992 has started with further weakness. Although there are few other negative indications in Houston, growth remains extremely slow. The strong forward momentum that brought Houston out of the 1980s recession has been stopped in its tracks since last January. Once a national recovery resumes, Houston should match or modestly exceed the national performance. The local economy is already on the mend from many of the problems now slowing the national recovery, including the credit crunch, real estate deflation and even fat-trimming by large companies.

RETAIL SALES

With holiday retail sales, most retailers finished 1991 even with or slightly ahead of 1990. After two weekends of rain, one respondent reported that only a "monster final weekend" pulled out a decent shopping season. Sales and promotions were much in evidence throughout the holidays, however, indicating that continued concern over the pace of sales led to a willingness to sacrifice profits for volume. Inventories were described as being in good shape coming into January, with problems possible only in a few apparel lines. Several small retailers indicated they were pleasantly surprised when books were closed in January to find the year as a whole worked out better than 1990 and better than they expected.

Auto and truck sales finished 1991 on an upbeat note, with a 2-percent gain compared with the previous December. For the year as a whole, sales were down 5 percent.

OIL AND GAS EXPLORATION

The domestic rig count appeared to stabilize on a seasonally adjusted basis during the late fall but in both December and January was in decline once more. Another warm winter in the Northeast corridor, important to natural gas sales for winter heating, pushed natural gas futures for February delivery down to levels near $1.20 per thousand cubic feet and to even lower levels by spring. Some drillers and oil service companies, hoping for a revival of exploration with a cold winter and higher gas prices, may be forced into another round of cutbacks. Respondents expected a weak start for domestic exploration in the first half of 1992 but then a pickup in the second half. Worldwide exploration may be up slightly in late 1992, as U.S. companies continue to move their efforts overseas.

PETROCHEMICALS

Ethylene was temporarily in short supply in December but returned to market in January as plant maintenance ended at some plants, and a new plant came on line. The price is down, but so is the price of feedstock. Margins were expected to narrow throughout January. The first quarter is expected to remain weak due to a big build-up of inventories of downstream derivative products by manufacturers.

WOOD PRODUCTS

Slow and steady improvement was seen in most lines of lumber and wood products. Seasonal slowness was observed in both bleachboard and corrugated products, but prices were holding steady or improving in these lines. Lumber and other building products also continued to improve slowly, with pricing in decent shape and likely to jump sharply with any real improvement in the building market.

REAL ESTATE

Like the economy, Houston real estate markets are also marking time. New single-family housing in Houston finished 1991 slightly ahead of the sales total for 1990, and multifamily housing finished slightly behind. Starts lagged new home sales for much of the year, leaving very thin inventories of new, completed homes on the ground. Resales of existing homes were up strongly at year-end, however, with a steady flow of entry-level buyers and far fewer move-up buyers in recent months. Prices of existing homes lagged inflation by a small margin. Apartment occupancy remained high, with rents flat over the past six months.

Occupancy rates and rents for local office space finished 1991 slightly up from 1990, but much slower leasing at year-end was blamed on the national recession. Both the downtown office market and the Galleria area are seeing big blocks of Class A office space becoming available in the wake of the layoff announcements made last fall.

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