

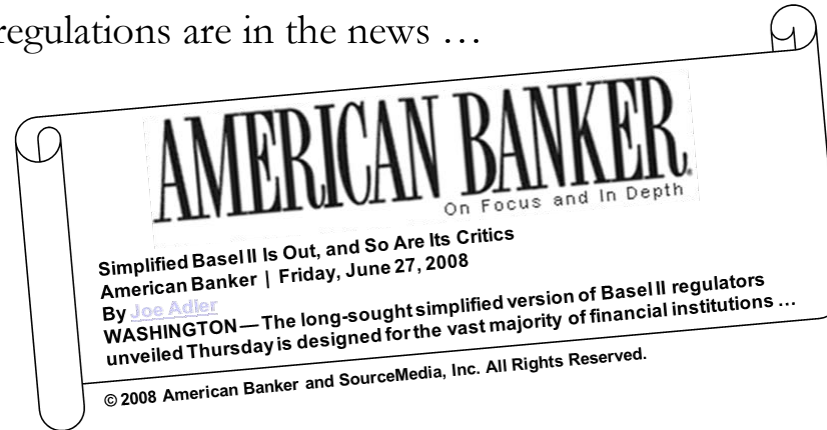
The Impact of Standardized Basel II on Texas Banks

Prepared for Texas Bankers Association



Executive Summary

- Basel II bank capital regulations are in the news ...

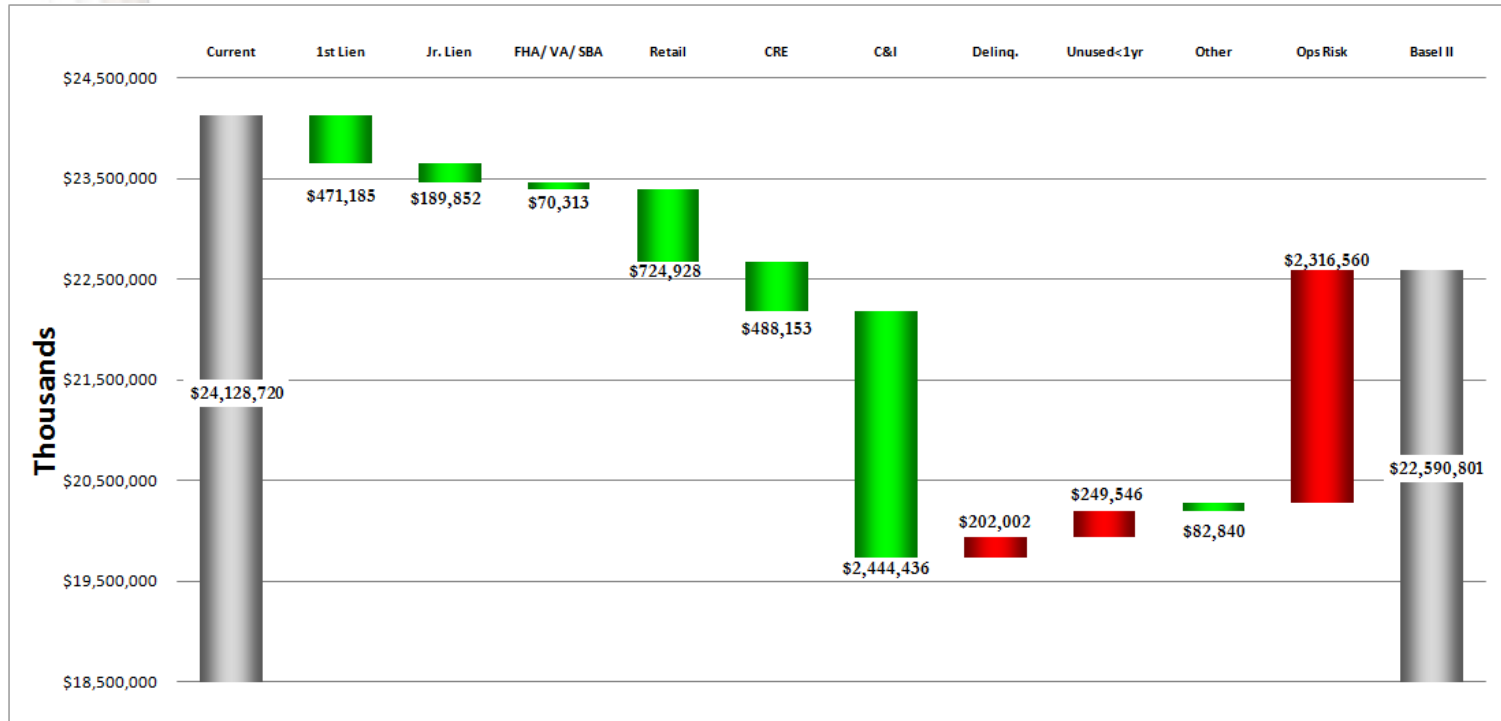


- We estimate that Standardized Basel II compliance will improve the regulatory capital ratios of 70.7% of 593 Texas banks and thrifts
 - Aggregate potential capital savings for all 593 banks of \$1,538 million
 - The median Texas bank would save \$0.7 million or 3.3% of their existing Tier 1 capital requirement
- Implementation is not without its challenges
 - Pillar II reporting can be complex and costly
 - Compliance requires demonstrated capital management capabilities
- Are your members aware of and prepared for these changes?
 - Second Pillar Consulting is uniquely positioned to help banks comply with Pillar II and obtain the capital relief they deserve

Texas Banks can save up to \$1,538 million in required capital under Standardized Basel II and improve risk management

Capital savings estimate and asset category contribution

Regulatory Capital Requirement

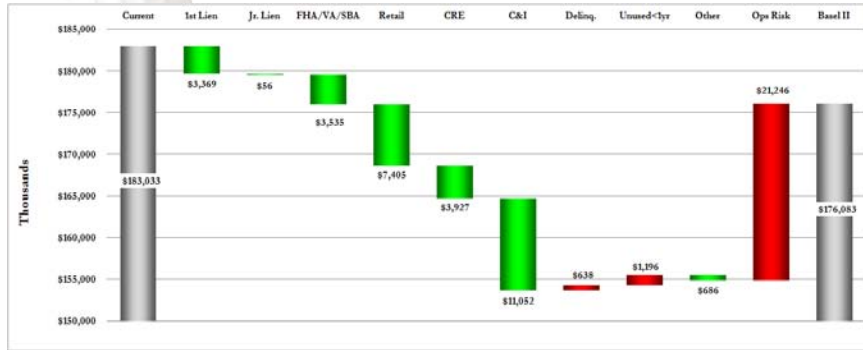


Source: 2008Q3 Call Reports; SPC estimates

For Southside Bancshares, Inc., a representative Texas bank, Basel II regulatory capital savings can be stockpiled or deployed

Capital Savings: \$7.0 million or 3.5%

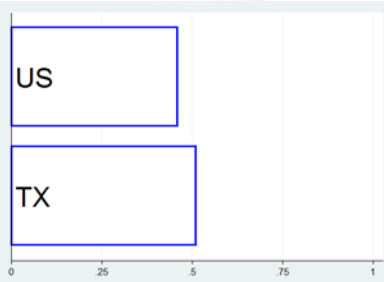
Regulatory Capital Requirement



Southside Bancshares, Inc. Tyler, TX Highlights

- *Stockpile.* Under Basel II, total RBC increases from 17.3% to 17.9%, an amount equal to \$7.0 million or 3.5% of the existing capital base.
- *Deploy.* Incremental capital can be deployed with a variety of balance sheet actions that preserve the current 17.3% total RBC ratio:
 - Issue a special dividend of \$0.50 per share
 - Repurchase 312,373 shares, increasing EPS \$0.03 or 2.3%
 - Organically grow assets by \$85 million

Capital Savings Percentile



Capital Metrics and Management

Total Assets (millions)	\$2,524	
Gross Income Margin	2.7%	
Tangible Common Equity	4.7%	
Leverage Ratio	7.6%	
Capital Estimates	Current	Basel II
Tier 1 RBC	15.6%	16.2%
Total RBC	17.3%	17.9%
Potential Use of Basel II Capital Savings		
Special Dividend (\$/share)	\$0.50	
Share Repurchase (7/29/2008 price)	312,373	
Change in EPS	\$0.03	
Organic Asset Growth (millions)	\$86	

Asset Mix



Upon request, Second Pillar Consulting can provide similar information for all 593 Texas banks free of charge

Texas banks with the highest percentage changes in regulatory capital under Standardized Basel II

Name	City	Asset Size (\$000's)	Basel II Capital Impact	
			Dollar Change (\$000)	Percent Change
T Bank, National Association	Dallas	\$ 139,406	\$ 2,768	23.6%
La Coste National Bank	Lacoste	\$ 36,433	\$ 811	23.0%
Bank of River Oaks	Houston	\$ 163,951	\$ 3,842	22.3%
United Bank of El Paso del Norte	El Paso	\$ 113,988	\$ 2,124	22.1%
Commercial State Bank	Andrews	\$ 394,849	\$ 5,717	21.9%
Guadalupe National Bank	Kerrville	\$ 28,255	\$ 1,102	21.6%
Brush Country Bank	Freer	\$ 46,186	\$ 472	21.5%
Third Coast Bank, SSB	Humble	\$ 51,820	\$ 2,804	21.3%
Southwest Bank	Odessa	\$ 170,355	\$ 2,843	21.3%
Access 1st Capital Bank	Denton	\$ 58,371	\$ 2,293	21.2%
Pegasus Bank	Dallas	\$ 97,872	\$ 2,651	20.3%
Frontier Bank of Texas	Elgin	\$ 51,886	\$ 4,106	20.3%
First State Bank	Rice	\$ 25,190	\$ 855	20.1%
First Bank and Trust of Memphis	Memphis	\$ 57,324	\$ 1,027	19.5%
West Texas State Bank	Odessa	\$ 233,350	\$ 4,443	19.5%
Austin County State Bank	Bellville	\$ 33,996	\$ 932	19.4%
Brazos Valley Bank, NA	College Station	\$ 120,819	\$ 1,680	19.1%
Texas National Bank of Jacksonville	Jacksonville	\$ 165,510	\$ 2,288	18.9%
Trinity Bank, N.A.	Fort Worth	\$ 127,794	\$ 2,251	18.9%
Alliance Bank Central Texas	Waco	\$ 92,483	\$ 997	18.8%
Averages		\$ 110,491.90	\$ 2,300.21	20.7%

Source: 2008Q3 Call Reports; SPC estimates

Texas banks with the lowest or negative percentage changes in regulatory capital under Standardized Basel II

Name	City	Asset Size (\$000's)	Basel II Capital Impact	
			Dollar Change (\$000)	Percent Change
First National Bank in Falfurrias	Falfurrias	\$ 64,422	\$ (694)	-7.9%
Capital Bank of Texas	Carrizo Springs	\$ 36,688	\$ (564)	-8.0%
Farmers & Merchants Bank	De Leon	\$ 54,463	\$ (607)	-8.1%
CU Bank Shares, Inc.	Dallas	\$ 1,344,832	\$ (12,036)	-8.3%
First Bank of Muleshoe	Muleshoe	\$ 90,522	\$ (1,111)	-8.3%
Jourdanton State Bank	Jourdanton	\$ 79,565	\$ (1,394)	-8.4%
Synergy Bank, SSB	McKinney	\$ 144,684	\$ (1,203)	-8.9%
Citizens Bank	Claude	\$ 96,069	\$ (1,047)	-9.3%
First National Bank of Aspermont	Aspermont	\$ 36,776	\$ (1,087)	-9.4%
Donley County State Bank	Clarendon	\$ 39,127	\$ (801)	-9.7%
Bank of Texas	Austin	\$ 77,522	\$ (1,155)	-9.8%
First National Bank of Alvin	Alvin	\$ 94,414	\$ (1,599)	-9.8%
City State Bank of Palacios	Palacios	\$ 44,545	\$ (548)	-9.9%
First National Bank of Seymour	Seymour	\$ 38,915	\$ (535)	-10.1%
Citizens National Bank of Crosbyton	Crosbyton	\$ 38,958	\$ (719)	-10.9%
Colonial Savings, FA	Fort Worth	\$ 871,263	\$ (26,667)	-12.2%
Kent County State Bank	Jayton	\$ 15,063	\$ (167)	-12.5%
Woodforest Financial Group, Inc.	The Woodlands	\$ 2,802,164	\$ (41,777)	-12.9%
Eden State Bank	Eden	\$ 59,689	\$ (936)	-13.8%
Trust Company	San Antonio	\$ 34,410	\$ (2,105)	-20.9%
Averages		\$ 303,205	\$ (4,838)	-10.5%

Source: 2008Q3 Call Reports; SPC estimates

But banks must be prepared to answer the tough risk management questions posed by Basel II compliance

- Do you have a well-functioning risk oversight structure?
- Do you have clear risk management policies and procedures?
- Have you identified the important risks faced by your institution?
- Have you articulated an institutional appetite for risk-taking?
- Do you have accessible data on the risk characteristics of your existing portfolio?
- Do you have accessible data on the past performance of your portfolio?
- Do you have personnel that can fill critical risk assessment gaps?
- Do you actively manage and plan your capital position?
- Are you committed to enhancing your overall risk and capital management?

Second Pillar Consulting can help banks prepare for Basel II compliance

- Our principals have over thirty years of experience in enterprise risk management, regulatory capital compliance, and regulatory relations
 - Supported International Basel II compliance at a top-ten bank
 - Developed analytical and reporting capabilities
 - Created governance structure and supporting policies
 - Led regulatory exams for approval
 - Managed risk in retail banking, commercial banking, and insurance
 - Focused on building strong regulatory relationships
 - Active participants in several Basel II industry and regulatory forums that facilitated drafting the new rules
 - Frequent speakers at industry and regulatory conferences on Basel
 - Several Basel II academic papers written jointly with regulators

Summary

- Second Pillar Consulting is uniquely positioned to help banks comply with Basel II and get the capital relief they deserve
 - Services
 - Detailed Capital Savings Estimate
 - Gap Analysis
 - The Internal Capital Adequacy Assessment Process or ICAAP
 - Education
 - We conduct seminars for institutions and organizations on topics including Basel II compliance, Enterprise Risk Management, Capital Management, and Balance Sheet Strategy
 - Facilitation
 - We are currently coordinating the NPR response for the Risk Management Association and can help organizations and institutions with their response

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