



SMALL BANK

Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

PUBLIC DISCLOSURE

July 7, 2008

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

The Carlsbad National Bank
Charter Number 12569

202 West Stevens Street
Carlsbad, New Mexico 88220

Office of the Comptroller of the Currency

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.

INSTITUTION'S CRA RATING: This institution is rated Satisfactory.

Carlsbad National Bank's (CNB) lending performance reflects a satisfactory response to the community credit needs. The following criteria support this rating.

- The loan-to-deposit ratio (LTD) is reasonable given the bank's size, financial condition, and assessment area's (AA) credit needs.
- A substantial majority of the bank's loans originated within the bank's AA.
- The distribution of loans to individuals of different income levels and businesses of different sizes reflects reasonable penetration given the demographics of the bank's AA.

SCOPE OF EXAM

This examination consisted of a full scope review of the bank's single AA. The lending test covered loans originated from January 2006 through May 2008. We identified business and residential real estate loans as the bank's primary products based on the number and dollar amount of loans originated in the evaluation period. There were no affiliate loans to review.

We sampled 20 loans from each of the bank's primary loan products. The data from the original business and residential real estate loan sample was used to calculate the inside/outside AA ratio. To perform other lending tests, we eliminated loans outside the AA from the sample and added enough additional loans to provide a sample of 20 business and 20 residential real estate loans inside the AA. The sample represents the bank's business strategy since the last examination.

DESCRIPTION OF INSTITUTION

CNB is a community bank headquartered in Carlsbad, New Mexico, which is a non-metropolitan area in the southeastern part of the state. As of March 31, 2008, CNB had \$194 million in average assets and net total loans of \$90 million, or 44 percent of total assets. CNB operates a main office, two branches, and one deposit-taking ATM all located in Carlsbad, New Mexico. The bank has neither opened nor closed any branch offices during the evaluation period.

Carlsbad Bancorporation, 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 business and residential real estate lending. In terms of dollar volume, commercial loan originations represent 46 percent and residential real estate loan originations represent 45 percent of the bank's total loan originations for the evaluation period.

There are no financial or legal impediments that hinder the bank's ability to help meet the credit needs of the AA. The bank was previously rated Satisfactory at its last CRA examination as of February 3, 2003.

Maps and additional information about the bank's AA may be found in the bank's Public File, maintained at the main office of the bank.

DESCRIPTION OF ASSESSMENT AREA(S)

CNB designated nine contiguous census tracts (CT) in southern Eddy County, including the cities of Carlsbad and Loving, as its AA. The entire area is a non-metropolitan statistical area. The AA consists of six middle- and three upper-income CTs. The AA does not have any low- or moderate-income (LMI) CTs. The AA meets the legal requirements of the regulation and does not arbitrarily exclude LMI geographies.

The economy of the AA has historically been based in oil and gas, potash mining and tourism. Major employers include Westinghouse (which manages the Waste Isolation Pilot Plant – WIPP), two potash mines, the school district, and the regional medical center. CNB is in an area with a diversified employment base. Local economic conditions are improving. Over the last four years, unemployment for the area has fallen from 5.9 percent to 2.3 percent, due primarily to the success of oil and gas production and potash mining.

Competition for financial services is strong. The June 30, 2007 FDIC Deposit Market Share Report shows three other financial institutions competed for over \$403 million of insured deposits. The nature of this competition includes one branch of a nation-wide financial institution, one state-chartered financial institution, and one federally-regulated thrift. In addition to these, there are three credit unions and eleven non-bank financial institutions. CNB's market share of 39 percent is the largest of any financial institution within its AA.

There are no similarly situated banks to CNB in the marketplace. The majority of the other competitors have a significant presence and access to other loans and deposits outside the local market.

To gather more information on the nature of the economic conditions and potential community development opportunities in the AA, we contacted a local community leader during this examination. The contact reported economic conditions as strong with exceptional growth from the oil, gas, and mining industries. The Waste Isolation Pilot Plant program continues to support the economy, but because of the shelf-life of the program it was also viewed as a long-term issue facing the community. The contact also indicated that there is a growing need for increased financial education among high school students and recent graduates. In the short-term, the greatest threat to the community is lack of housing. Due to the success of the local industries, the rental and real estate markets have been strained with minimal new construction taking place. Part of the problem is that high residential construction lending rates have inhibited builders from migrating into the area. In addition, the recent tightening in lending practices has made it difficult for borrowers to obtain mortgages. The contact is in the economic development business and identified the primary credit need as residential construction financing.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

Loan-to-Deposit Ratio

CNB's average LTD ratio of 49 percent is reasonable given the bank's size, financial condition, and the credit needs within the AA. As shown in the table below, CNB has the lowest quarterly average LTD ratio of its competitors but it is also the only bank that operates solely in the

southern CTs of Eddy County. Both of the bank’s identified competitors have a significant percentage of their business outside of the AA, allowing for more lending opportunities. The competitors listed below do not include the branch of the nation-wide financial institution, as the comparison would not be meaningful. In addition, from March 31, 2004 to March 31, 2008 CNB sold nearly \$46 million of its 1-4 family residential loans into the secondary market, contributing to the below-peer LTD ratio.

Bank	Average Quarterly Loan-to-Deposit Ratio
Carlsbad National Bank	49%
Bank A	66%
Bank B	86%

Source: Uniform Bank Performance Report

Lending in Assessment Area

A substantial majority of the sampled loans originated inside the AA. Our analysis determined that 93 percent of the number and 82 percent of the dollar amount of the loans in the sample were made within the bank’s AA. The table below depicts the level of lending in and out of the bank’s AA based on our sample.

Lending in Southern Eddy County										
Loan Type	Number of Loans					Dollars of Loans				
	Inside		Outside		Total	Inside		Outside		Total
	#	%	#	%		\$000	%	\$000	%	
Commercial	17	85%	3	15%	20	\$1,913	70%	\$839	30%	\$2,752
Residential RE	20	100%	0	0%	20	\$1,951	100%	\$0	0%	\$1,951
Total	37	93%	3	7%	40	\$2,752	82%	\$839	18%	\$4,703

Source: Loan Sample

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

The borrower distribution of loans originated in the AA reflects reasonable penetration overall in loans to individuals of different incomes, and businesses of different sizes. The bank’s primary products are about equally divided between commercial and residential real estate loans, so neither product is given more weight than the other.

Commercial Loans

The distribution of loans to businesses reflects excellent penetration among businesses of different sizes. Of the 20 loans we sampled, 63 percent of the number of the bank’s loans to businesses originated and purchased during the evaluation period were made to small businesses which slightly exceeds the 61 percent of small businesses within the AA. Small businesses are defined as businesses with gross annual revenues of one million dollars or less. The following table shows the details of the borrower distribution analysis for business loans by gross annual revenue.

Borrower Distribution of Loans to Businesses in Southern Eddy County
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Business Revenues (or Sales)	≤\$1,000,000	>\$1,000,000	Unavailable / Unknown	Total
% of AA Businesses	61%	6%	33%	100%
% of Bank Loans in AA by #	63%	35%	2%	100%
% of Bank Loans in AA by \$	60%	25%	15%	100%

Source: Loan sample; Dunn and Bradstreet data.

Residential Real Estate

The distribution of residential real estate loans to borrowers reflects reasonable penetration among borrowers of different income levels. Of the 20 loans we sampled, 16 percent were originated for moderate-income borrowers but none were originated for low-income borrowers. One explanation for the lack of loans to low-income borrowers is that 16 percent of families in the AA are below the poverty level. But affordable housing was determined to be a credit need in the community, and there are ways to meet that need that were not reflected in our sample. The loans originated for moderate-income borrowers slightly exceeds the demographics of 15 percent in the AA.

Borrower Distribution of Residential Real Estate Loans in Southern Eddy County								
Borrower Income Level	Low		Moderate		Middle		Upper	
	% of AA Families	% of Number of Loans	% of AA Families	% of Number of Loans	% of AA Families	% of Number of Loans	% of AA Families	% of Number of Loans
Residential RE	21%	0%	15%	16%	17%	26%	47%	58%

Source: Loan sample; U.S. Census Data

Geographic Distribution of Loans

We did not perform an analysis of the bank's geographic distribution of loans. The AA includes only middle- and upper-income CTs and such an analysis would not be meaningful.

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 or Other Illegal Credit Practices Review

We found no evidence of discriminatory or other illegal credit practices inconsistent with helping to meet community credit needs.