Real estate loans held for sale represent loans originated for the purpose of purchasing or refinancing one-to-four family residential properties. These loans are originated by the bank with the intent to sell to secondary market investors. The loans are generally sold within 30 days after origination. Real estate loans held for sale decreased by $701 thousand or 5% from June 30, 2012 to June 30, 2013.

Loans to governmental entities decreased by $9.5 million from June 30, 2012. The decrease was due to primarily one large loan to a tax-paying entity for short term purposes that paid off in early October of 2012. Loans in this category generally produce tax free income much like a municipal bond.

Commercial & industrial loans increased from $113.9 million at June 30, 2012 to $129 million at June 30, 2013, an increase of $14.8 million or 13%. Loans in this category include oil and gas production loans, loans to oil and gas service companies, and loans to manufacturing and wholesale supply companies and miscellaneous other commercial businesses.

Consumer loans declined by $889 thousand or 9% from June 30, 2012 to June 30, 2013. The decline was the result of regular monthly payments on installment loan contracts. The Company had previously financed car loans for a car dealer in one of our markets. The amount of volume under this relationship has declined over the last two years so that monthly payments exceed the amount of new volume being placed on the books. The Company is interested in making consumer loans of all types, but consumer lending is not its primary focus. Recently, the Company purchased consumer credit underwriting software and hired a seasoned consumer credit underwriting manager. Management anticipates that our consumer loan portfolio will increase over the next year.

All other loans increased by $30 million from June 30, 2012 to June 30, 2013. Included in this category are loans to finance agriculture, loans to purchase securities, and loans to non-depository institutions. In late December of 2012, the Company entered into an agreement with another Texas bank to purchase participations in mortgage warehouse lines of credit that the bank has outstanding to several mortgage origination companies, which are classified as loans to non-depository institutions. Previously, these loans were categorized as 1-4 family loans held for sale and were re-classed in the first quarter of 2013 to loans to non-depository institutions. These loans represent $30.5 million or 99% of other loans as of June 30, 2013.

Asset Quality:

The allowance for loan losses is the amount we determine as of a specific date to be appropriate to absorb probable losses on existing loans in which full collectability is unlikely based on our review and evaluation of the loan portfolio. The provision for loan losses was $625 thousand for the period ended June 30, 2013 as compared to $700 thousand for same period in 2012. Our asset quality remains strong and our allowance for loan loss was adequate; therefore, there wasn’t the need to take as much provision expense in the first quarter of 2013. As a percent of average loans, net loan charge-offs were 0.00% at June 30, 2013 and 0.32% at June 30, 2012. Comparatively, the peer group averages for the same periods were 0.26% and 0.47%, respectively. Our allowance for loan losses as a percent of loans was 1.25% as of June 30, 2013, as compared to 1.19% as of June 30, 2012.

As of June 30, 2013, past due loans over 90 days as a percentage of total loans were 0.00%, the same can be said for the same period in 2012. Loans placed on non-accrual status as a percentage of total loans were 0.17% as of June 30, 2013 compared to 0.23% at June 30, 2012. Our peer group for the same time period was 1.63% and 2.32%, respectively.

Another common measure of asset quality is the Texas Ratio. The Texas Ratio is calculated as the sum of restructured loans plus non-accrual loans plus real estate acquired in foreclosure divided by the sum of equity capital plus the allowance for loan losses. As of June 30, 2013, the Company's Texas Ratio was 1.72% as compared to the peer group of 20.24%. For the same date in 2012, the Company had a Texas Ratio of 1.72% as compared to its peer group of 26.87%.

Interest-Bearing Deposits in Banks:

The Company had interest-bearing deposits in banks of $125.6 million as of June 30, 2013, as compared to $134.9 million as of June 30, 2012. The average yield on these balances was 0.50% for both periods. These balances were held with various regional banks located within the state of Texas. Management evaluates the financial strength of each bank it holds balances with on a quarterly basis to assure the safety of the investment in each bank.

Available-for-Sale and Held-to-Maturity Securities:

At June 30, 2013, available-for-sale securities had a fair value of $40.2 million and held-to-maturity securities had an amortized cost of $24.2 million. As of June 30, 2013, the portion of the securities portfolio classified as available-for-sale had a market loss of approximately $388 thousand and the portion of the portfolio classified as held-to-maturity had an approximate market gain of $1.1 million. The Company did not hold any securities as of June 30, 2013 or 2012 that would be classified as below investment grade or with any impairment.

As of June 30, 2013, the tax-exempt yield to maturity on the portion of the securities portfolio classified as available-for- sale was 4.27%. The tax-exempt yield to maturity on that portion of the portfolio classified as held-to-maturity was 4.76%. Our overall tax-exempt yield to maturity on our portfolio at June 30, 2013 was 4.45%.

As of June 30, 2012, the tax-exempt yield to maturity on the portion of the securities portfolio classified as available-for- sale was 3.63%. The tax-exempt yield to maturity on that portion of the portfolio classified as held-to-maturity was 3.94%. The overall tax-exempt yield to maturity on our portfolio at June 30, 2012 was 3.80%.

All yields are computed on a tax-equivalent basis assuming a marginal tax rate of 34.00%. Yields on available-for-sale securities are based on amortized cost. Maturities of mortgage-backed securities are based on contractual maturities and could differ due to prepayments of underlying mortgages. Maturities of other securities are reported at the earlier of maturity date or call date.

Deposits:

Deposits represent our primary source of funding. Total deposits were $615.7 million as of June 30, 2013 compared to $559.3 million as of the same period in 2012. Deposits increased by $56.5 million or 10.1% from June 30, 2012 to June 30, 2013. The growth was mostly attributed to increases in Jumbo Certificates of Deposit of $36.4 million.

Composition of Deposits ($ in 000's)

	June 30 2013	June 30 2012	Incr./ (Decr.)	% change
Non-interest bearing demand	$200,573	$193,604	$6,969	3.60%
Interest-bearing demand	48,879	37,177	11,702	31.48%
Money market and savings	126,440	127,848	(1,407)	-1.10%
Certificates of deposits ≥ $100,000	212,208	175,789	36,419	20.72%
Certificates of deposits < $100,000	27,644	24,873	2,771	11.14%
Total Deposits	$615,744	$559,291	$56,453	10.09%

The average cost of interest-bearing deposits as of June 30, 2013 was .51% which compares to .58% for the same period in 2012. The primary reason for the decline in the average cost of interest-bearing deposits was the maturing certificates of deposits re-pricing into the extended low interest rate environment.

Capital Resources:

We evaluate capital resources by our ability to maintain adequate regulatory capital ratios to do business in the banking industry. Issues related to capital resources arise primarily when we are growing at an accelerated rate exceeding the rate of growth in our earnings or if we experience significant asset quality deterioration.

Total shareholders' equity was $74.7 million, or 10.71% of total assets, at June 30, 2013, as compared to $69.8 million, or 10.97% of total assets, at June 30, 2012. The Company engaged in a stock offering in the first quarter of 2012 that ended on April 2, 2012. The Company sold $12.0 million in new common stock and $5.6 million in new preferred stock in the offering which boosted the Company's capital levels. The new capital provides additional room for growth and enabled the Company to be better positioned for new regulatory capital minimums.

Banking regulators measure capital adequacy by means of the risk-based capital ratios and leverage ratio. The risk-based capital rules provide for the weighting of assets and off-balance-sheet commitments and contingencies according to prescribed risk categories ranging from 0% to 100%. Regulatory capital is then divided by risk-weighted assets to determine the risk-adjusted capital ratios. The leverage ratio is computed by dividing shareholders' equity less intangible assets by quarter-to-date average assets less intangible assets. Regulatory minimums for total risk-based, Tier 1 risked-based and leverage ratios are 8.00%, 4.00% and 3.00%, respectively. As of June 30, 2013, our total risk-based, Tier 1 risk-based and leverage capital ratios were 17.04%, 15.85% and 11.18%, respectively, as compared to total risk-based,

Tier 1 risked-based and leverage capital ratios of 17.57%, 16.49% and 11.46% as of June 30, 2012. We believe by all measurements our capital ratios remain well above regulatory minimums.

Dividend Policy:

To pay dividends, we must maintain adequate capital above regulatory guidelines. In addition, if the applicable regulatory authority believes that a bank under its jurisdiction is engaged in or is about to engage in an unsafe or unsound practice (which, depending on the financial condition of the bank, could include the payment of dividends), the authority may require, after notice and hearing, that such bank cease and desist from the unsafe practice. The Federal Reserve Board, the FDIC and the OCC have each indicated that paying dividends that deplete a bank's capital base to an inadequate level would be an unsafe and unsound banking practice. The Federal Reserve Board, the OCC and the FDIC have issued policy statements that recommend that bank holding companies and insured banks should generally only pay dividends out of current operating earnings.

The Company has not paid dividends since its inception due to the need to maintain capital for growth purposes. We anticipate that we will continue to have strong growth and that we will not begin paying dividends in the immediate future. However, if growth slows, the Company could consider paying dividends at a later date.

CAPITALIZATION

The following table represents, on a consolidated basis, the capitalization of the Company as of June 30, 2013.

	At June 30 2013
Long-Term Indebtedness:	
Junior subordinated debentures - trust preferred securities	$ 3,093,000
Total indebtedness	$ 3,093,000
Shareholders' Equity:	
Common stock, par value $1.00 per share, 15,000,000 shares authorized, 9,439,992 shares issued, 9,430,686 shares outstanding as of June 30, 2013	$ 9,439,992
Preferred stock, par value $1.00 per share, 5,000,000 shares authorized, 937,044 Series 2009 shares issued and outstanding as of June 30, 2013	937,044
Surplus	
Common	31,554,551
Preferred	8,399,979
Surplus	39,954,530
Treasury stock	(87,825)
Retained earnings	24,719,906
Accumulated other comprehensive income	(255,972)
Total shareholders' equity	$ 74,707,675
Capital Ratios (Bank):	
Tier 1 to average assets capital ratio	9.53%
Tier 1 risk-based capital ratio	13.52%
Total risk-based capital ratio	14.71%

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TED AWERKAMP
Chief Operating Officer

JAY W. ISAACS
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TRACY BACON
Chief Financial Officer

J. GREG BURGESS
Chief Lending Officer

GEORGE H. REEVES
Chief Operations Officer

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President, Midland Market

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Executive Vice President & Loan Operations & Credit Administration Manager

TRACY A. TIMLIN
Executive Vice President & Chief Mortgage Officer

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Senior Vice President, Midland Lending Manager & Senior Relationship Manager

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Senior Vice President & Team Resources Manager

JEREMY M. BISHOP
Senior Vice President & Senior Relationship Manager

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Senior Vice President & Marketing, Training, & Call Center Manager

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Senior Vice President & Trust Officer

CHRIS L. McGINNIS
Senior Vice President & IT Manager

TOBY D. PAYNE
Senior Vice President & Senior Relationship Manager

ROBIN RICHEY
Senior Vice President & Trust Administration

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Vice President & Controller

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Assistant Vice President & Loan Operations Manager

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Assistant Vice President & IT Specialist

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Assistant Vice President & BSA Officer

CHRIS ANN WHITNEY
Assistant Vice President, Branch Manager & Personal Banker

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Banking Officer & Branch Manager

BETHANY ETHEREDGE
Banking Officer & Relationship Manager

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Banking Officer & Branch Manager

EDGAR PAZ
Banking Officer & Loan Servicing Assistant

JANA SALDIVAR
Banking Officer & Credit Administration Manager

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Banking Officer & Information Security Officer

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President, Amarillo Market

LACIE McDOWELL

Senior Vice President & Treasury Management

DONALD TAYLOR

Senior Vice President & Relationship Manager

MURIELLE BARNES

Vice President & Mortgage Underwriter

BRUCE FIELDER

Vice President & Mortgage Operations Manager

ANITA K. FINK

Vice President & Assistant Operations Manager

M. KAY KUHN

Vice President & Amarillo Mortgage Manager

KENNETH L. BURGESS, III

Assistant Vice President & Relationship Manager

CARMELLA SMITH

Assistant Vice President & Wire Transfer Manager

ABBY SNYDER

Assistant Vice President & Branch Manager

BRAD STUTEVILLE

Assistant Vice President & Relationship Manager

KYLE BALL

Banking Officer & Relationship Manager

LANCE GREEN

Banking Officer & Relationship Manager

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TONY PENA

President, Lubbock Market

MARILANDA CRISTAN

Senior Vice President & Consumer Credit Underwriting Manager

DARRELL HILL

Senior Vice President & Senior Relationship Manager

ROSALINDA VILLALON

Senior Vice President & Compliance Officer

TRAVIS HILLMAN

Vice President, Relationship Manager

LISHA KING

Vice President & Operations Manager

CINDI LEA

Vice President & Lubbock Mortgage Manager

DANA PHILLIPS

Vice President & Relationship Manager

SHIRLEY WIGLEY

Vice President & Compliance Specialist II

YOLANDA BELGARA

Banking Officer & Consumer Underwriter

CATHY COPPLE

Banking Officer & Loan Documentation Preparation Department Manager

JASON SHIPP

Banking Officer & Relationship Manager

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