



PUBLIC DISCLOSURE

October 24, 2016

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

The Carlsbad National Bank
Charter Number 12569

202 West Stevens Street Carlsbad, NM 88220

Office of the Comptroller of the Currency

Denver Field Office
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Denver, Colorado 80202-5534

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.

The Lending Test is rated: Satisfactory

The Community Development Test is rated: Satisfactory

The overall performance of The Carlsbad National Bank (CNB) is "Satisfactory". The primary factors contributing to the bank's rating are:

- The bank's loan-to-deposit (LTD) ratio is reasonable given the bank's size, financial condition, and the credit needs of the assessment area (AA).
- A substantial majority of the loans were made inside the bank's AA.
- Lending activities represent excellent penetration to individuals of different income levels
- Community development (CD) activities demonstrate an adequate responsiveness to the needs in the bank's AA.

Scope of Examination

This Performance Evaluation (PE) assesses CNB's Community Reinvestment Act (CRA) performance using the Intermediate Small Bank (ISB) examination procedures. An ISB examination consists of two tests: a lending test and a community development (CD) test.

The lending test evaluates the bank's record of meeting the credit needs in its AA through its lending activity. We focused our review on loans originated in 2014, 2015, and through August 31, 2016. This is referred to as the evaluation period. We further focused our review on commercial and consumer loans. These loans are identified as the bank's primary products based on number and dollar volume of loans originated in the evaluation period. To assess lending performance we reviewed a sample of 20 commercial loans and 22 consumer loans.

Table 1 - Loan Originations for Evaluation Period	% of Dollar Amount of Loans	% of Number of Loans
Commercial Loan Originations as a % of Total Originations	49%	24%
Consumer Loan Originations as a % of Total Originations	9%	51%

The CD test includes a review of qualified loans, investments and/or donations, and services made in the bank's AA that have the primary purpose of community development. We evaluated CD loans, investments, and services made or provided since the prior CRA examination. The prior CRA examination is dated October 21, 2013.

We used demographic information from the 2010 U.S. Census.

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. The bank is a subsidiary of a one-bank holding company Carlsbad Bancorporation, Inc. The holding company owns 100% of the bank's stock. As of June 30, 2016, CNB maintained \$322 million in total assets and \$120 million (or 38% of total average assets) in loans.

CNB operates a main office, two branches, and three ATMs, one of which is deposit-taking, all located in Carlsbad, New Mexico. The bank has neither opened nor closed any branch offices during the evaluation period.

CNB's strategic focus is to support the economic growth and development of its AA by providing competitive banking solutions for commercial and consumer customers. The bank's primary lending focus is small business and consumer loans. The bank originates residential real estate loans, the majority of which are sold on the secondary market.

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" under Small Bank examination procedures at its prior CRA examination. Additional details about the bank may be found in its Public File. The Public File is maintained at the main office of the bank.

Description of Assessment Area

CNB designated all census tracts (CT) in Eddy County, including the cities of Carlsbad, Loving and Artesia, as its AA. The entire area is a non-metropolitan statistical area. The AA consist of 12 CT and includes 6 middle-income and 6 upper-income tracts. The AA meets the legal requirements of the regulation and does not arbitrarily exclude low- or moderate-income (LMI) geographies.

The economy of the AA is concentrated in oil and gas, potash mining, government, and tourism. Major employers include Nuclear Waste Partnership, LLC (which manages the Waste Isolation Pilot Plant), two potash mines, the school district, and the regional medical center. CNB is in an area with a diversified employment base. Government-owned lands account for almost 82 percent of the county's 2.7 million acres and include the Waste Isolation Pilot Plant, Lincoln National Forest, Carlsbad Caverns National Park, and Brantley Lake State Park. Local economic conditions have deteriorated slightly due to the decline in the oil industry and consolidation in the local pot ash industry. The unemployment rate increased from 4.0 percent in 2013 to 6.7 percent in June 2016. The median household income was \$48,801 in 2015.

Demographic Information for the AA

TABLE 2 - DEMOGRAPHIC INFORMATION FOR THE AA						
	#	Low % of #	Moderate % of #	Middle % of #	Upper % of #	% Unknown
Geographies (Census Tracts)	12	0	0	50	50	0
Population by Geography	53,829	0	0	44	56	0
Owner-Occupied Housing by Geography	14,431	0	0	39	64	0
Business by Geography	3,163	0	0	47	53	0
Farms by Geography	148	0	0	25	75	0
Family Distribution by Income Level	13,411	15	17	16	51	0
Distribution of Low and Moderate Income Families throughout AA Geographies	4,304	0	0	51	49	0
Median Family Income (MFI)	46,354	Median Housing Value		96,127		
FFIEC Adjusted MFI for 2014	47,200	Households Below the Poverty Level		14%		
FFIEC Adjusted MFI for 2015	48,400	Unemployment Rate		3.51%		
FFIEC Estimated MFI for 2016	50,700					

Source: 2010 U.S. Census Data and FFIEC Updated MFI

Competition in the AA

There is strong competition for financial services in the AA. The annual FDIC Market Share Report for June 30, 2015 shows 8 financial institutions competed for almost \$1.3 billion of insured deposits. The competition includes 1 mega-bank, one large federal bank, three regional banks, and three large state banks. CNB is ranked second with a 33.79 percent share of the marketplace.

No banks in CNB's AA are considered truly comparable as the banks differ significantly in size and geographic area served. The competitor banks used to evaluate the CNB's LTD ratio are community banks that operate inside the AA and are identified as competitors to CNB.

Community Contact

To gather current information on the nature of the economic conditions and potential CD opportunities in the AA, we contacted one local community leader. The contact described the importance of the oil and potash industry in the area as a primary drivers of the local economy. The contact noted the oil industry downturn in the prior few years reduced tax revenue, increased unemployment, and reduced area population. The contact stated the economic conditions are showing signs of improvement and conditions should continue to improve as oil prices increase.

The contact stated local financial institutions are generally supportive in meeting the small business and community development needs in the area. The contact is in the economic development business and identified the primary and continuing credit need as increased financing for lodging accommodations including affordable/subsidized apartment complexes, and affordable single-family residential units. The contact stated that the tightening in lending practices has made it difficult for individuals to obtain mortgages.

Conclusions with Respect to Performance Tests

The bank's overall CRA performance is "Satisfactory". This is supported by separate conclusions for the lending test and the CD test.

LENDING TEST

The bank's performance under the lending test is rated "Satisfactory". The LTD ratio is reasonable given the bank's size, financial condition, and the credit needs of its AA. A substantial majority of the bank's loans are made in its AA. Lending activities represent an excellent penetration to borrowers of different income levels and businesses of different sizes.

Loan-to-Deposit Ratio

CNB's LTD ratio is reasonable given the bank's size, financial condition, and credit needs of the AA. CNB's quarterly average loan-to-deposit (LTD) ratio from the evaluation period March 2013 to June 2016 is 42 percent. This reasonably compares to competitor banks that maintained a quarterly average LTD over the same period of 48 percent, with a high of 56 percent and a low of 44 percent. The competitor banks are all community banks with similar business models and a substantial portion of their business completed in CNB's AA.

Although CNB's LTD ratio is lower than the competitors, the bank's LTD ratio is not fully reflective of all of its lending activity. CNB originates and sells residential real estate loans into the secondary market. These loans are not included in the LTD ratio. From January 1, 2014 to August 31, 2016 the bank sold 266 loans that totaled \$44.3 million. Additionally, CNB originates a large number of small dollar consumer loans to meet the credit needs of the community. These small dollar loans do not significantly impact the LTD ratio.

Lending in Assessment Area

As evidenced in Table 3, a substantial majority of the loans in our sample were originated inside the bank's AA. Our random sample of 20 commercial loans and 20 consumer loans originated in the evaluation period showed 95 percent by number and 98 percent by dollar amount of loans were originated in the AA.

Loan Type	Number of Loans					Dollars of Loans				
	Inside		Outside		Total	Inside		Outside		Total
	#	%	#	%		\$	%	\$	%	
Commercial	20	100	0	0	20	3,158	100	0	0	3,158
Consumer	18	90	2	10	20	136	63	79	37	215
Total	38	95	2	5	40	3,294	98	79	2	3,373

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

The borrower distribution of commercial and consumer loans originated inside the AA reflects excellent penetration among individuals of different income levels and businesses of different sizes.

Commercial Loans

CNB exceeds the standard for loans to borrowers with gross annual revenue of \$1 million or less. Table 4A shows the bank originated 85 percent by number and a comparable 70 percent by dollar of its commercial loans to businesses with gross annual revenues of \$1 million or less. This exceeds the standards of the demographic data that shows 73 percent of businesses in the AA with gross annual revenue of \$1 million or less.

Business Revenues (or Sales)	≤\$1,000,000	>\$1,000,000	Unavailable/ Unknown	Total
% of AA Business	73	6	21	100
% of Bank Loans in AA by #	85	15	0	100
% of Bank Loans in AA by \$	70	30	0	100

Consumer Loans

CND exceeds the standard for consumer loans to individuals of different income levels. Table 4B shows the bank originated 25 percent and 30 percent by number of loans to low- and moderate-income households, respectively. This is comparable to the demographic data that shows 19 percent and 15 percent of households are low- and moderate-income, respectively.

Borrower Income Level	Low		Moderate		Middle		Upper	
	% of AA Households	% of # of Loans	% of AA Households	% of # of Loans	% of AA Households	% of # of Loans	% of AA Households	% of # of Loans
Consumer Loans	19	25	15	30	16	10	50	35

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

There were no complaints related to CRA or unfair credit practices received by the bank or the OCC in the evaluation period.

COMMUNITY DEVELOPMENT TEST

The bank's performance in the CD test is "Satisfactory". CNB demonstrates adequate responsiveness to CD needs in the AA after consideration of the available opportunities and the bank's capacity and business strategy.

There are no LMI census tracts, or distressed areas, in the bank's AA. As such, CNB's CD activities are primarily to benefit low-or-moderate individuals.

Number and Amount of Community Development Loans

CNB's CD lending demonstrates adequate responsiveness to needs in the AA. Since the prior CRA examination, CNB funded \$4.6 million CD loans. This amounts to 15 percent of capital as of June 30, 2016. The loans include 42 mortgage loans that created affordable housing for LMI individuals in the bank's AA and 2 loans to a non-profit organization that created jobs and provided affordable housing to LMI individuals.

Number and Amount of Qualified Investments

Qualified investments demonstrate poor responsiveness to needs in the AA. Since the last examination, CNB made limited qualified investments in the form of donations to non-profit organizations which primarily target LMI individuals. Donations totaled \$5,500 and represent a nominal percent of capital as of June 30, 2016. CNB made a number of donations to different organizations that did not qualify for CD investment.

Extent to Which the Bank Provides Community Development Services

The bank demonstrates adequate responsiveness to the CD service needs in the AA. Since the prior CRA examination, CNB employees provided a combined 1,288 hours of service to six qualified organizations. Participating employees provided CD services in the form of financial expertise to benefit the AA. Employees serving in these roles over multiple years is evidence of a continued commitment to CD services. Many other employees at CNB are active in the community and provide non-financial services to the AA.

CNB offers delivery systems for retail services that make banking accessible to LMI individuals. The bank has three branches within Carlsbad. Each branch has an ATM on location. There are no low- or- moderate income tracts in CNB's assessment area. The branches are located in the downtown, western, and southern areas of Carlsbad to provide ease of accessibility. The bank offers a variety of services to the community ranging from checking and savings accounts to certificates of deposits (CD's) and individual retirement accounts. CNB offers low-fee, low-minimum balance deposit accounts within its checking and savings account product lines. The Bank also offers free checking accounts.

Responsiveness to Community Development Needs

Overall, CNB demonstrated adequate responsiveness to CD needs in the bank's AA through its adequate CD lending practices, limited CD investment activities, and adequate service activities.

Fair Lending or Other Illegal Credit Practices Review

Pursuant to 12 C.F.R. § 25.28(c) in determining a national bank's (bank) CRA rating, the OCC considers evidence of discriminatory or other illegal credit practices in any geography by the bank, or in any assessment area by an affiliate whose loans have been considered as part of the bank's lending performance.

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