

When one financial institution
takes the lead in defining what
banking should be, it becomes...



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FINANCIAL REVIEW



One Bank, Banking Ahead

SOUTHWEST BANK OF TEXAS

Dear Shareholders, Cu

Our eleventh year of business at Southwest Bank of Texas will be long remembered by our shareholders, customers and staff alike.

The world of banking is changing at breakneck speed. And with another consecutive year of record growth and innovation behind us, Southwest Bank of Texas has emerged definitively, not only as a key participant in this rapidly evolving environment, but also as a break-away innovator and leader.

This year's theme, "One Bank, Banking Ahead," capsulizes this breakaway leadership. And it is a bold statement that only Southwest Bank of Texas can truly make. It articulates our corporate culture, business mindset, and acknowledged position as an innovative leader in exemplifying what successful banking should be. It expresses the incremental value our customers have come to expect from us. It reflects our engaged, proactive involvement in the communities we serve. And it codifies our vision of the boundless opportunities that are ahead.

Marking the beginning of the new millennium, the year 2000 was, for Southwest Bank of Texas, a period of substantial achievement, growth and transition. Here are some highlights.

PERFORMANCE. Our "star" shined brightly in 2000 as one of the top-performing bank stocks in the country. Compounded annual operating earnings per share (as originally reported) have grown 23 percent over the last five years, a clear testament to Southwest Bank of Texas' strong performance.

ASSET GROWTH. From \$3.27 billion in 1999, to 2000's close of \$3.94 billion ... growth of approximately 20 percent.

OPERATING INCOME. In 2000, rising 32 percent to \$46.9 million ... with 2000 operating earnings per diluted share up 29 percent to \$1.39, an increase from \$1.08 in 1999.

LEGAL LOAN LIMIT. Up to \$49 million from \$40 million last year.

LOANS OUTSTANDING. A 23 percent increase from the \$2.04 billion reported in December 1999 to \$2.51 billion.

EXPANSION. With the successful merger of the three subsidiary banks of Citizens Bankers, Inc. into Southwest Bank of Texas, we marked positive progress in our carefully planned expansion strategy. The Citizens merger grants us a preferential presence in the Baytown area of Houston's east side. With the merger comes Citizens' strong deposit portfolio, and substantial retail and middle-market business customer base.

TECHNOLOGY LEADERSHIP. Southwest Bank of Texas continues to lead with the launch of expanded versions of our proprietary, Internet-based retail and commercial banking tools, NetST@RSM and bank@home. (We were one of the first banks in the United States to offer Internet-delivered e-statements.) Our commitment to facilitating our customers' growth and success through the development and integration of e-commerce and e-financial solutions is a hallmark of our "Banking Ahead" approach to customer service.

RECOGNITION. Southwest Bank of Texas is now included in the Standard and Poors Small-Cap 600, in addition to our inclusion in 17 other key financial indices.

Customers and Friends,

INNOVATION. Ribbon cutting at our new experience-based branches in downtown Houston's 1 Houston Center and in The Woodlands introduced our visionary new concept of customer-focused branch design, merchandising and service delivery.

ACCOLADES. A nationally recognized survey that measures customers' perceptions and attitudes toward financial institutions found Southwest Bank of Texas cited among the top five percent of banks in the United States vis-à-vis customer service, responsiveness and value.

CONTRIBUTION. Another year of rewarding work outside our offices and in our community, both corporately and individually. Our philosophy of improving and enabling the communities we serve through our corporate and human resources brings immeasurable rewards to everyone involved. To schools and students. To first-time home buyers. To young businesses. To those who are trying, but can use some help ... Southwest Bank of Texas is there.

For Southwest Bank of Texas, our momentum and Banking Ahead philosophy is possible largely because of our solid grounding in—and vigilant stewardship of—banking fundamentals. Fundamentals that have served us for eleven years. Fundamentals we all share.

Walter E. Johnson is the bank's Founder and Chairman of the Board. Since his banking career began more than 40 years ago in Houston, Johnson has fostered strong business relationships that have passed the test of economic cycles and time. While leading Southwest Bank of Texas to a \$3.94 billion level, he has also remained committed to bettering the Houston community, as evidenced in the many civic endeavors Johnson has spearheaded to raise funds for the less fortunate.

The Southwest Bank of Texas fundamentals are worth repeating here:

- Straightforward, commonsense decision making
- Superior service
- Strong customer relationships
- State-of-the-art technology
- Responsive turnaround
- A collective direction
- Respect for the valued customers we serve

Being guided by these fundamentals allows us to break away from the pack and create the new definition of what banking should be. That's who we are today. Southwest Bank of Texas. One Bank, Banking Ahead.

Respectfully,

Paul B. Murphy, Jr.

Paul B. Murphy, Jr.
Chief Executive Officer & President

Walter E. Johnson

Walter E. Johnson
Chairman of the Board



Paul B. Murphy, Jr. serves as Chief Executive Officer, President and Director of Southwest Bank of Texas. He has worked with Walter for 20 years, for the past 11 as a co-manager of Southwest Bank. His business development savvy has strengthened the bank's tremendous regional presence. Like Johnson, Murphy is dedicated to supporting the community through his involvement with several non-profit, civic, health and religious organizations.

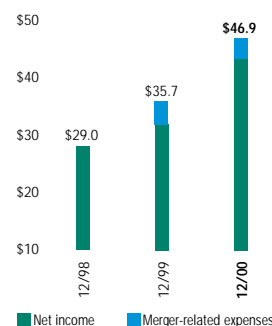
Highlights

CONSOLIDATED FINANCIAL HIGHLIGHTS

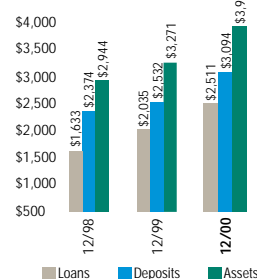
(dollars in thousands, except per share amounts)

	Years Ended December 31,		
	2000	1999	Change
Balance Sheet Data:			
Assets	\$3,940,342	\$ 3,271,188	20.5%
Deposits	3,093,870	2,531,633	22.2
Loans	2,511,437	2,035,342	23.4
Allowance for loan losses	28,150	22,436	25.5
Investment securities	848,164	890,369	-4.7
Equity	298,125	233,076	27.9
Income Statement Data:			
Interest income	\$ 272,166	\$ 211,232	28.8%
Interest expense	121,662	88,219	37.9
Net interest income	150,504	123,013	22.3
Provision for loan losses	7,053	6,474	8.9
Net interest income after provision	143,451	116,539	23.1
Noninterest income	42,893	37,464	14.5
Merger-related expenses	4,122	4,474	-7.9
Noninterest expense	116,035	100,037	16.0
Income before taxes	66,187	49,492	33.7
Federal income taxes	22,607	17,500	29.2
Income before minority interest	43,580	31,992	36.2
Minority interest	119	29	310.3
Net income	\$ 43,461 (1)	\$ 31,963 (2)	36.0%
Common Share Data:			
Basic earnings per common share	\$1.34	\$1.01	32.7%
Diluted earnings per common share	\$1.29	\$0.97	33.0%
Book value per share @ period-end	\$9.12	\$7.28	25.3%
Selected Performance Ratios:			
Return on average assets	1.23% (3)	1.06%	
Return on average common equity	17.00% (3)	14.70%	
Tier I capital to average assets	7.71%	7.81%	
Net interest margin	4.64%	4.44%	
Efficiency ratio	61.98% (3)	65.07%	
Asset Quality Data:			
Nonperforming assets to total loans & ORE	0.41%	0.31%	
Net charge-offs to average loans	0.06%	0.09%	
Allowance for loan losses to:			
Total loans @ period-end	1.16%	1.15%	
Nonperforming loans @ period-end	297.82%	519.59%	

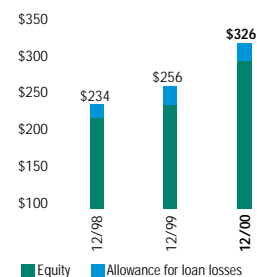
Net Income (in millions)



Balance Sheet Data (in millions)



Primary Capital (in millions)



- (1) Excluding merger-related expenses and net losses on the sales of securities, net income available to common shareholders would have been \$46,888, or \$1.39 per diluted common share, for the year ended December 31, 2000.
- (2) Excluding merger-related expenses and net losses on the sales of securities, net income available to common shareholders would have been \$35,675, or \$1.08 per diluted common share, for the year ended December 31, 1999.
- (3) Excluding merger-related expenses and net losses on the sales of securities, ROA, ROE and efficiency ratio would have been 1.33%, 18.34% and 60.00% respectively, for the year ended December 31, 2000.

"Can a bank grow bigger and still be better?"



We have.

With consistent growth comes the persistent challenge to be even better. It's a challenge we've grown to embrace in eleven years on the ascending curve. And we wouldn't have it any other way.

At Southwest Bank of Texas, being better is actually a prerequisite for growing bigger. In fact, we attribute our eleventh consecutive year of double-digit growth to our primary focus on being better.

Better for our customers. Better for our employees. Better for our community. And better for our shareholders.

By listening better, we're providing meaningful answers to a broader spectrum of customer needs.

By eagerly investing time with our commercial customers—at their places of business—we're delivering ever-increasing value to higher and higher levels of their organizations.

Through expanded services. Innovative technology. And an ever-deepening pool of competitively priced banking products.

Pair this with our reputation for flexibility, customer-responsiveness and creative problem solving ... and the word gets out. To a lot of people.

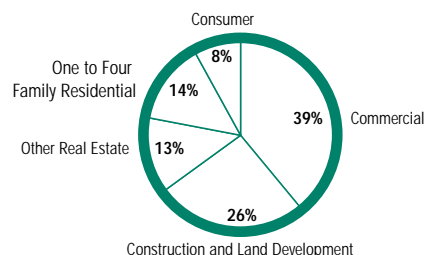
And we grow.

Year 2000 concludes with Southwest Bank of Texas reporting assets in excess of \$3.94 billion, the largest independent bank serving the eight-county Houston area, now with 32 full-service banking centers and one community lending office.

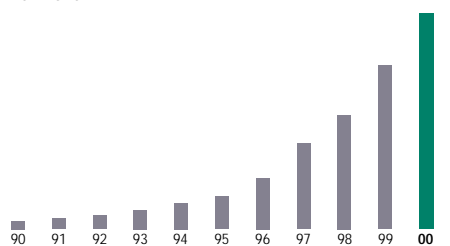
Southwest Bank of Texas. Growing bigger. Growing better.

One Bank, Banking Ahead.

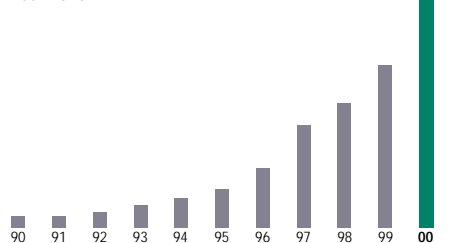
LOAN DISTRIBUTION



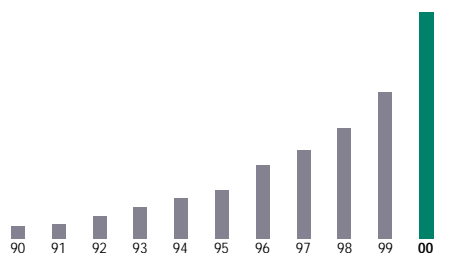
LOAN GROWTH



ASSET GROWTH



DEPOSIT GROWTH



"Can a mid-cap financial institution outpace the index giants?"



You be the judge.

It appears a little bold at first.

That a regional financial institution—like Southwest Bank of Texas, for instance—would compare itself to global growth stock leaders.

Recognized leaders such as Walt Disney Productions. General Electric. Coca-Cola.

But the simple truth is that many of the corporate and business characteristics you'll find in successful global, growth-oriented companies are also found at Southwest Bank of Texas.

Focus. Keen management. Momentum. Forward-directed culture. And innovation that is customer-driven and profit-minded.

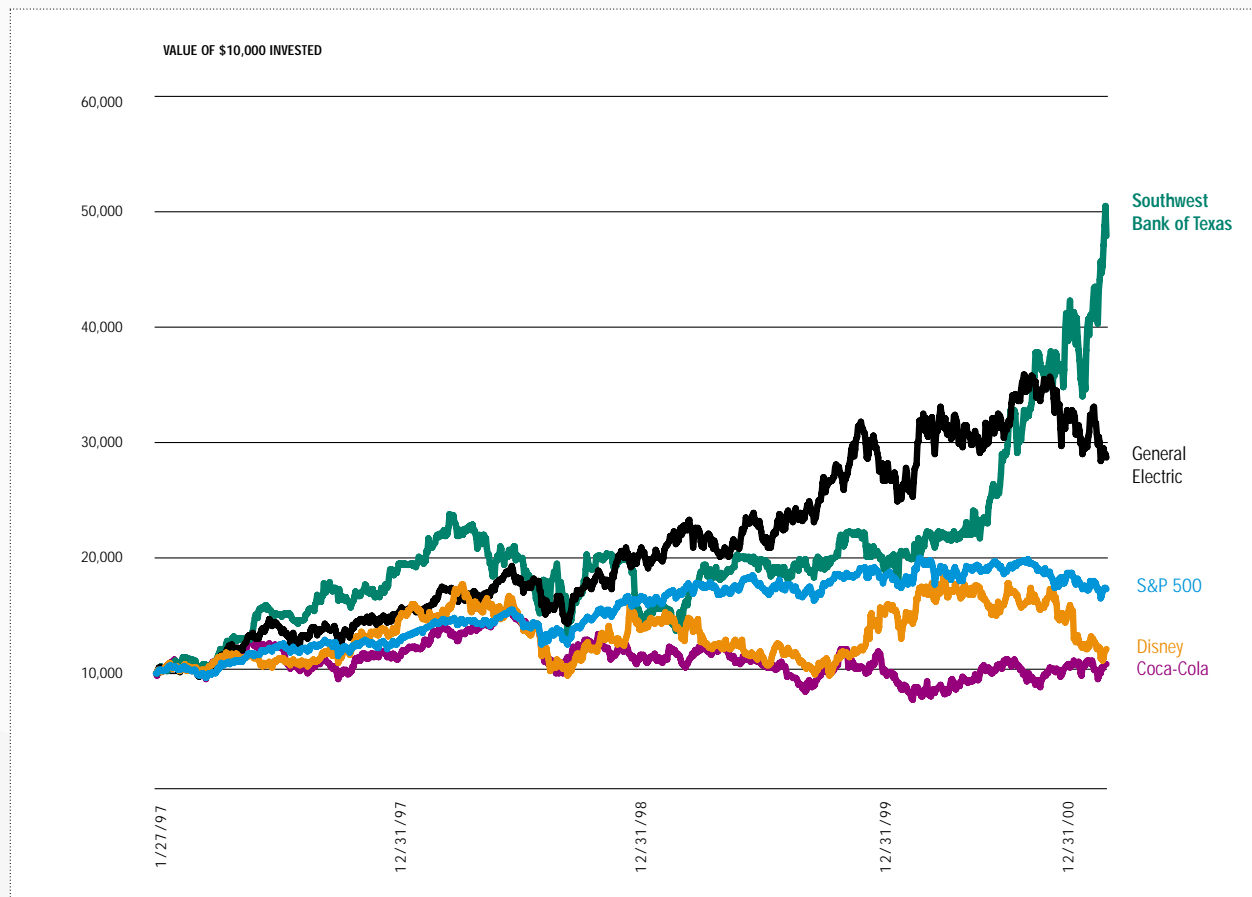
For eleven years, Southwest Bank of Texas has maintained an ascending curve in every measurable business arena. Including shareholder value.

While, as in life, there are no guarantees in stock performance, we thought we'd take this opportunity to thank our shareholders for their trust in our ability to serve their interests, and our customers for their trust in our abilities to satisfy their growing needs.

For their ongoing confidence in our management and staff.

And for their part in helping us take the lead in defining what banking can be.

One Bank, Banking Ahead.





"Can technology actually make customers happier?"

Ours does.

After all, isn't that the point?

Year 2000 saw further strengthening of Southwest Bank of Texas' reputation and leadership in financial and banking technology applications.

From the expansion of our own e-delivery of banking services (NetST@RSM and bank@home). To automated internal business processes and practices. To advancing our role as technology advisors and e-enablers for many of our commercial customers.

Our strategy of software development and application consultation is serving our bank and commercial customers well.

In fact, not only are customers relying on us for e-solutions development, we also execute, host and fulfill the financial services we help develop. With security and privacy features that are second to none.

In this way, we've created a unique interface between the Internet-based financial or sales utility on our customers' Web site—and us.

Profitable. For our customers. And for us.

But that's just part of the story.

By enlisting our considerable technical expertise and muscle to help customers get the most from their e-solutions investment, our customers invite us into a level of understanding of their businesses that few banks achieve.

Between our own e-banking services and services we provide for customers, Southwest Bank of Texas is hosting, managing and transacting an average of more than 10 million hits per month.

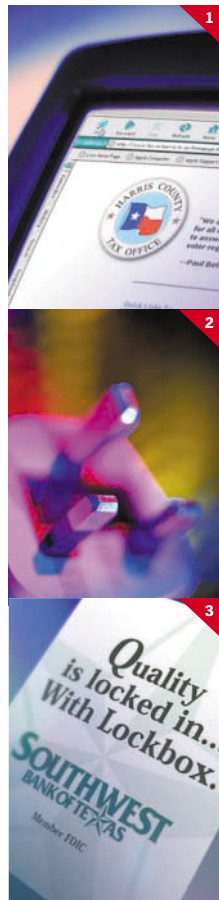
And we anticipate significant growth to come.

In volume. In quality. And in the smiles that appear with technology that works.

1 TAX AUTHORITY Harris County's Tax Office serves the third-most populous county in the nation. When Tax Assessor-Collector Paul Bettencourt wanted county taxpayers to "get online instead of in line," he turned to Southwest Bank of Texas as a key technology outsource to help execute the ambitious Internet presentation and collection initiative. Working closely with Harris County Financial Services, Southwest Bank of Texas turn-keyed the credit card processing of the Tax Office online property payment system. Southwest Bank of Texas directly processed over 5,000 online payments totaling \$7.6 million dollars; payments cleared and settled in a compressed time frame, providing a seamless real-time payment/reporting cycle to the county tax office ... and a convenient, easy-to-use payment option for all county citizens.

2 SWITCHED-ON SAVINGS Additional utility costs due to billing errors in a business' utility bills may run as high as three percent. But for many businesses, the expense of periodic audits exceed the excess utility costs. One business customer asked if there was anything we could do. Southwest Bank of Texas met the challenge with a unique e-commerce solution. A solution that required us to take the lead in vendor negotiation, implementation, coordination and programming. This nontraditional role as solutions provider also involves our ongoing participation as an application service provider. We collect multivendor bills in differing formats and translate those bills into a single, standard form that can be imported into clients' native accounting environments. Now, utility bill audits are not only possible, they're simplified. Staff resources are minimized. And management reports are allowing our customer to optimize utility use to save even more in basic operations costs. Good news for the company. And good news for Southwest Bank of Texas: Solving one company's problem now allows us to leverage this unique technology solution for other bank customers.

3 QUALITY LOCKED-IN While Remittance Banking has been available to businesses since 1951, we've taken these common "Lockbox" services to uncommon levels of quality, security and value through our innovative application of technology. Southwest Bank of Texas now processes an average of more than 600,000 items per month through our Remittance Banking Service. This escalating volume with an unheard of three-year average accuracy rate of 99 percent is great news for us—and great news for our customers. Through early morning, e-delivery of remittance transactions—including check and documentation images—customers enjoy the benefits of accelerated cash flow plus the security of automated remittance processing. It's a combination of technology and customer-focused innovation that continues to set Southwest Bank of Texas apart.



"Do relationships still count in a high-tech world?"



Absolutely.

The value of relationships runs deep at Southwest Bank of Texas. Relationships with our customers. With our community at large. And within our own Southwest Bank of Texas family.

We build these relationships with open ears and open minds. Listening carefully to our customers and to the community. And to our colleagues. Taking a little extra time to consider what we've heard.

And responding. With ideas. With solutions.

Solutions that, in many cases, might be considered "outside of the box" for a financial institution.

And that's how we build trust. The cornerstone of any relationship.

Inspiring customers to turn to us—to rely on us—more and more.

This is particularly evident in the ongoing growth of Southwest Bank of Texas Investment Services which includes:

- Personal investment advisors located in our network of retail branches
- Institutional services for fixed-income and cash management
- Retirement services helping commercial customers introduce 401k and retirement-related benefits into their businesses

In a related area, we have continued to expand and invest in Private Client Financial Services. This is a direct result of an increasing number of individuals who in their personal financial management partner, seek the service, attention to detail and trustworthy advice they receive every day in business from our Private Bankers and Investment Advisors. That's true relationship extension. True relationship banking.

Also this year, we've increased our retail presence with the addition of seven full-service branches—continuing our ambitious retail development strategy that we began last year.

Our customers enjoy the convenience of the branch experience. And we enjoy the benefits of an additional broad base of deposits, loans and fee-based service income.

This is how we grow. Through value. Through trust. Through relationships. Built one at a time.

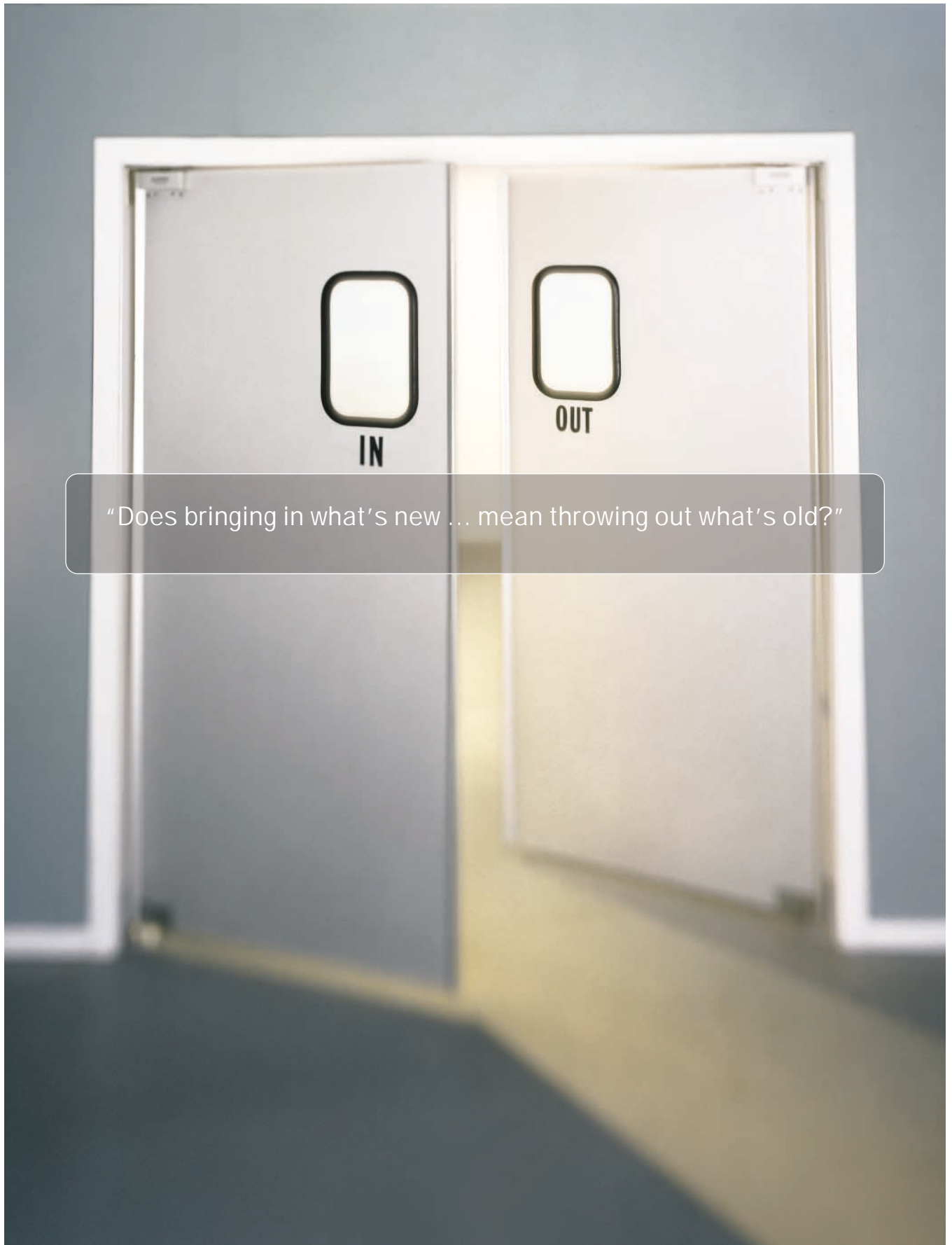
1 CONSOLIDATED EFFORT The Dubose Model Home Company is a lessor and reseller of model homes—and a customer of Southwest Bank of Texas. The Dubose Company buys model homes built by developers and then leases the home back to the builder until the time that the subdivision has sold out and the builder no longer needs a model home. Dubose, in turn, sells them to consumers. It's good

business all around. Except that Dubose may carry an inventory of 300 homes at any one time through various partnerships. And that has meant 300 individual mortgages in the company system. We suggested—and helped implement—a simple solution. We recommended that Dubose self-finance its inventory purchases by setting up an in-house finance company. We helped with the financial structuring and consolidation of outstanding mortgages. Dubose not only saves money, the company can also track and manage its finances more efficiently. And they couldn't be more pleased. Not a typical bank solution. But then, we're not a typical bank.

2 BRICKS AND MORTAR While so many global banks seem to be driving customers out of their branch facilities, Southwest Bank of Texas, this year, quietly initiated a unique plan to invite more customers into ours. It's a key component in "our way" of building real relationships with our customers. And a key component of our way of extending and solidifying our brand. By extending the "portal" concept of our Internet-enabled e-banking products, the new Southwest Bank of Texas branch facilities are a carefully designed and arranged mix of electronic and people-assisted banking services. (Even special computer kiosks for kids in our Woodlands branch, where families comprise the majority of branch traffic.) Everything in place to allow customers to access what they've told us they want. Everything created to encourage customer participation in developing the relationship. Call in. Click in. Or come by. At Southwest Bank of Texas, we're here for our customers.

3 BUILDING RELATIONSHIPS The Houston-based Sueba Company is the U.S. subsidiary of one of the largest residential developers in Western Europe. Southwest Bank of Texas, aware of the company's ongoing activity in the Houston market, kept local Sueba representatives informed of our desire to work with them. In spite of Sueba's traditional and almost exclusive reliance upon German-based institutions. However, this year, recognizing a need to move faster and smarter in the dynamic U.S. market, Sueba began the process of choosing a U.S. banking institution to serve its business. In Houston, Southwest Bank of Texas competed with the largest names in national banking. And won. Based on our demonstrated interest in their business over time. Based on our ability to move faster than the rest. And based on our ability to bring creative solutions to the relationship. We're proud of our new relationship with such a fine company. And we anticipate a long and mutually rewarding future together. This is just the beginning.





"Does bringing in what's new ... mean throwing out what's old?"

Not necessarily.

"Banking Ahead" banking doesn't discard what's come before. We build upon it. Expand through it. And evolve from it.

At Southwest Bank of Texas, our leadership in innovative banking is driven by our dedication to what we call "The Fundamentals."

The core practices of which we believe no bank should lose sight ... they are the practical value we've been delivering to our customers since our founding in 1990.

Through competitively priced commercial and retail banking products and services. Time-saving technology. And unsurpassed customer service.

From Commercial. To Retail. From Automated Treasury Solutions. To Mortgage Lending. To Benefits Management.

And through this philosophy of thoughtful and constant reevaluation and response, rather than reaction and reinvention, we're able to sensitively guide most customers to higher and higher levels of efficiencies and economies in banking. As they're ready.

On their schedules. Not ours.

It's a philosophy of respect. For customers. For fundamentals. For what's come before. It's what's guiding our bank into the future.

1 BANK@HOME 2.0 Our retail, Internet-based e-banking service, bank@home, continues to garner national attention as a standard to pursue. This year not only introduced a clean, new look to the service, but also ushered in a range of new, enhanced and expanded features, including:

■ Real-Time Environment

- Online Enrollment
- Online User ID Selection
- Funds Transfer as Immediate, Scheduled or Recurring
- Data Export to Quicken® and Microsoft® Money
- Balance Alerts as Balances Exceed or Fall Below Predetermined Amount Thresholds
- Telephone-Accessible Internet Customer Service Representatives
- Customizable Web Site Links
- Online Check Reordering

2 SWEEPING UP Year 2000 saw the introduction of our Eurodollar Sweep account, yet another investment vehicle available for our customers. By chartering a Southwest Bank of Texas branch in the Cayman Islands, our Eurodollar Sweep offers customers the option of earning interest on unused funds residing in primary operating or concentration accounts. This sweep feature, available at Southwest Bank of Texas through qualifying money fund accounts and repurchase agreements, allows customers the option of investing otherwise dormant funds, even if just overnight. For many businesses, it makes a lot of sense. And generates a significant return. Just one more way we're making sure our customers can make the best choices possible, from among the best financial tools available.

3 NETST@R SHINING EVEN BRIGHTER With customer usage of (and delight with) NetST@RSM growing, Southwest Bank of Texas continues to innovate and expand this industry model for commercial e-banking services. New and expanded features include:

- Data Importability to a Variety of Client-Based Accounting and Financial Program Packages
- Real-Time Reporting
- Positive Pay Fraud Protection
- Longer 45-Day Retained Transaction History
- Customer-Initiated Electronic Wire Transfers, Both Domestic and International
- Online Viewing of Paid Checks—Both Front and Back Imaging

NetST@RSM is now the day-to-day interface with Southwest Bank of Texas for our commercial customers, allowing our commercial banking representatives to focus even more on customers' big-picture financial issues. And providing big-picture financial solutions.



"Should a community leader strive to do even more?"



Why not?

Service to our community—it's some of the best work we can do.

It restores us as individuals. And it inspires us as a corporation.

It demonstrates that, as members of the communities we serve, our claim to valuing relationships has substance. That relationships are, in fact, the very heart of our company.

Last year, Southwest Bank of Texas employees donated countless personal hours to worthy causes throughout the Greater Houston area.

That's no surprise to us. Just another indicator of the quality of the individuals who choose to work here.

And we've been busy as a corporation, too. In year 2000:

We continued our business and corporate relationship with KIPP (Knowledge Is Power Program) Academy Charter School. We are particularly proud of KIPP's national recognition as a leader in education—culminating with the school's on-stage appearance at the Republican National Convention. Our hats are off to the accomplishments that the faculty, staff and student body have worked so hard to achieve. And we remain committed to helping KIPP grow to even greater success.

Our fourth annual Houston Ministerial Conference grew to "standing-room-only" proportions. More than 250 respected clergy and community leaders attended this day-long conference to learn about available community development loans and how to access them. They will share this knowledge within their respective communities.

And Southwest Bank of Texas Chairman Walter Johnson personally committed to raise \$1.6 million to benefit more than 65,000 at-risk youths in the Houston area through local chapters of the Boy Scouts of America and their scouting programs.

Our ongoing pledge to our communities is to listen. Respond by doing what we can. And then do even more.

To help create a prosperity that can only be accounted for in the sustained health and happiness of our neighborhoods.

1 LENDING SUPPORT Southwest Bank of Texas co-founded the Third Coast Community Development Corporation—a not-for-profit alliance of area businesses and business leaders dedicated to helping viable but at-risk businesses succeed. Third Coast targets small, promising, minority-owned businesses serving

their communities, struggling to grow, with loans in partnership with traditional banking institutions. With each \$35,000 loaned, businesses must add at least one new employee, thus creating a positive impact in the community as we help enable their growth. With Southwest Bank of Texas as a key participant, Third Coast has, to date, infused businesses with loans of up to \$100,000 in partnership with seven area banks.

2 A CREDIT TO THE COMMUNITY Southwest Bank of Texas continues the positive outreach and support of the Houston Credit Coalition—a unique educational program directed at helping lower-income consumers access available resources and use credit wisely. The free, six-week, 15 hour course focuses on building and maintaining creditworthiness, as well as recovering from past mistakes ... and how to avoid those pitfalls in the future. More than 500 mostly lower-income families and individuals have graduated from the program. The success of the Credit Coalition has recently attracted the attention of the National Community Reinvestment Corporation and resulted in a unique alliance for support and possible expansion in collaboration with this organization.

3 REBUILDING DREAMS The unprecedented development and re-development of Houston's inner-city neighborhoods continually threatens to displace many of these communities' long-time, lower-income residents. In response, Southwest Bank of Texas supports numerous efforts to help. One example is our work with the Avenue Community Development Corporation in its mission to build affordable housing in Houston's historic, yet

rapidly gentrifying, First and Sixth Wards. As with other projects of this kind, Southwest Bank of Texas has contributed not simply cash, but invaluable assistance in applying for and securing available grants, as well as providing construction and permanent project financing. Our participation in this Sixth Ward project has helped to provide 74 new, affordable housing units that will help keep one of Houston's oldest and most diverse neighborhoods whole.





Financial Review

**Southwest Bancorporation
of Texas, Inc.
Stock Information**

NASDAQ Symbol "SWBT"
32,705,909 Shares
as of 12/31/00

Stock Transfer Agent --
Computershare Investor
Services

Market Maker Companies:

Keefe Bruyette
& Woods, Inc.

Legg Mason Wood Walker
Stephens, Inc.

U.S. Bancorp Piper
Jaffray Inc.

Morgan Keegan

Dain Rauscher Wessels

Putnam, Lovell & Thornton

Robinson-Humphrey

Stifel Nicolaus & Company

For Investor
Communications, please
call Susan Eckel at
713/232-1163 or email
seckel@swbanktx.com.

The 2001 annual shareholders meeting is scheduled for Wednesday, April 25, 2001,
at the St. Regis Houston, 1919 Briar Oaks Lane, Houston, Texas, at 5:00 p.m.

**SOUTHWEST BANK OF TEXAS,
N.A. BOARD OF DIRECTORS**

Willie J. Alexander
President
W. J. Alexander & Associates, PC

Nolan Bedford
Vice Chairman of the Board
Southwest Bank of Texas

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Director
Ocean Energy, Inc.

Timothy R. Brown
Partner
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✦ **Ernest H. Cockrell**
Chairman
Cockrell Oil Corporation

✦ **John H. Echols**
CEO — Baytown Region
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✦ **John W. Johnson**
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✦ **Walter E. Johnson**
Southwest Bank of Texas
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Barry M. Lewis
Goldeneye, Inc.

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Bunker Steel Corporation

Don R. Mullins
Owner
Don R. Mullins Interests

✦ **Paul B. Murphy, Jr.**
CEO & President
Southwest Bank of Texas

✦ **Andres Palandjoglou**
President
Rio Largo S.A.

✦ **A. A. Pfeffer, Jr.**
Private Investor

✦ **Beth Robertson**
President
Cockspur, Inc.

Thomas F. Soriero, Sr.
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President & CEO
Valco, Inc.

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Attorney at Law
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Manuel Urquidi
Senior Vice President
Seitel

✦ **Lane Ward**
Vice Chairman of the Board
Southwest Bank of Texas

✦ **Michael T. Willis**
Chairman, CEO & President
COMSYS

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The Ainbinder Co.

Lester L. Allison III
The Allison Company

Scott Anderson
Anderson Oil Company

Duke Austin
North Houston Pole Line

Carin M. Barth
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Brooks McGee
RAM Funds GP, L.L.C.

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Pappas Partners, L.P.

Kirk M. Pfeffer
LoneStar Alliance

Yale Smith
Olympia Capital Advisors

Kevin R. Snodgrass
Cushman Realty Corp.

Dave Stevenson
Stavinoha White Stevenson Financial
Group, Inc.

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✦ Advisory Director

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Bill Rowsey
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Memorial Hermann Hospital
The Woodlands

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The Woodlands Operating Co., L.P.

Eric Wojner
The Woodlands Operating Co., L.P.

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Hartman Newspapers

Lynne Humphries
Attorney At Law

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Home Lumber & Hardware Co.

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Retired – Imperial Holly Corporation

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Lee Mahlmann, D.D.S., M.S. Inc.

Ted Nelson
Terrabrook

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Digital Consulting and
Software Services, Inc.

Wayne O. Poldrack
Wayne O. Poldrack, CPA

Ray Rucksdashel
The Baro Companies

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Midway Development Company

Bill Schwer
Imperial Sugar Company

Cliff Terrell
Terrell Consulting

Joe C. Wessendorff
Ranching and Investments

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⌚ **Walter E. Johnson**
Chairman

⌚ **Paul B. Murphy, Jr.**
CEO & President

⌚ **Nolan Bedford**
Vice Chairman

⌚ **Lane Ward**
Vice Chairman

Dale Andreas
President, Mitchell Mortgage

⌚ **Joe Argue**
Group EVP

John Drew
EVP

⌚ **John H. Echols**
CEO – Baytown Region

⌚ **David Farries**
EVP & CFO

Debbie Innes
EVP

Jim Lowrey
EVP

Marylyn Manis
EVP

George Marshall
EVP

⊕ **Jim Massey**
EVP

⊕ **John McWhorter**
SVP & Controller

Randy Meyer
EVP

Ken Olan
EVP

⊕ **Steve Stephens**
EVP

BUSINESS MANAGERS
(alphabetic by line of business)

George Marshall
Commercial Construction Lending

Brian Stoker
Community Development

Walt Boyer
Correspondent Banking

Jenifer Stepanik
Custody Services

Steve Kennedy
Energy Lending

Alan Atchley
Factoring

Bodil Boest
Foreign Exchange

Laura McWilliams
International

Jim Lowrey
Private Banking

Greg Swank
Private Client Services

Don Hickey
Real Estate Income Property/Finance

Ed Jones
Residential Construction Lending

Mike Holtkamp
Residential Single Family Lending

Ken Olan
Retail Banking

Suzie Jones
Retirement Plans

Sharon Randle
Secondary Mortgage Markets

Debbie Innes
Treasury Management

**BANKING CENTER SENIOR
LEADERS AND MANAGERS**
(alphabetic by branch center name)

Mark DeVaney
Wendel Skolaski
Deborah Hines
1 Houston Center

Charlie Phillips
Dianna Saldivar
Bell Tower

Gloria Moreno
Bissonnet

Ron Brandt
Julie Douglas
Downtown

Rita Jochec
East Bernard

Leonard Hein
Fairmont Parkway

Randy Walker
Fernando Parra
Dwayne Whiddon
Galleria

Gayle Guidry
Garth Road

Johnny Brooks
Greenspoint

Missy Krantz
Laura Heinzen
Robert Dewhitt
Greenway Plaza

Morey Junod
Hempstead

Lynda Jackson
Katy

Milan Saunders
Rena Brown
Kingwood

Reggie Brewer
Betty Griffin
Lacy Drive

Mark Troth
Medical Center

Eric Corley
Sue Nelson
Memorial

Donna Sumrall
Memorial West

Steve Epps
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Angela Michot
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Kirk Wiginton
LuAnne Glover
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Fred Domin
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Deborah Olson
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Thass Young
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Connie Magouirk
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Rollingbrook

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Nelda Sullivan
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Sharon Jenkins
Spring

Bruce Mercer
Kathy Ballard
Sugar Land

Terrie Elkins
Richard McCardle
Tanglewood

Chris Denison
Susan Watthuber
The Woodlands

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

FORM 10-K

☒ **Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the Fiscal Year Ended December 31, 2000**

☐ **Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

Commission file number: 000-22007

SOUTHWEST BANCORPORATION OF TEXAS, INC.

(Exact Name of Registrant as Specified in its Charter)

Texas
(State or Other Jurisdiction of
Incorporation or Organization)

76-0519693
(I.R.S. Employer
Identification No.)

**4400 Post Oak Parkway
Houston, Texas 77027**
(Address of Principal Executive Offices, including zip code)

(713) 235-8800
(Registrant's telephone number, including area code)

Securities Registered Pursuant to Section 12(b) of the Act:
None

Securities Registered Pursuant to Section 12(g) of the Act:
Common Stock, \$1.00 par value
(Title of class)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.
Yes ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☐

There were 32,767,562 shares of the Registrant's Common Stock outstanding as of the close of business on February 16, 2001. The aggregate market value of the Registrant's Common Stock held by non-affiliates was approximately \$1.14 billion (based upon the closing price of \$43.00 on February 16, 2001, as reported on the NASDAQ National Market System).

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's Proxy Statement relating to the 2001 Annual Meeting of Shareholders, which will be filed within 120 days after December 31, 2000, are incorporated by reference into Part III of this Report.

PART I

Item 1. Business

SPECIAL CAUTIONARY NOTICE REGARDING FORWARD-LOOKING STATEMENTS

Certain of the matters discussed in this document and in documents incorporated by reference herein, including matters discussed under the caption "Management's Discussion and Analysis of Financial Condition and Results of Operations," may constitute forward-looking statements for purposes of the Securities Act of 1933, as amended, and the Securities Exchange Act of 1934, as amended, and as such may involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of Southwest Bancorporation of Texas, Inc. (the "Company") to be materially different from future results, performance or achievements expressed or implied by such forward-looking statements. The words "expect," "anticipate," "intend," "plan," "believe," "seek," "estimate," and similar expressions are intended to identify such forward-looking statements. The Company's actual results may differ materially from the results anticipated in these forward-looking statements due to a variety of factors, including, without limitation: (a) the effects of future economic conditions on the Company and its customers; (b) governmental monetary and fiscal policies, as well as legislative and regulatory changes; (c) the risks of changes in interest rates on the level and composition of deposits, loan demand, and the values of loan collateral, securities and interest rate protection agreements, as well as interest rate risks; (d) the effects of competition from other commercial banks, thrifts, mortgage banking firms, consumer finance companies, credit unions, securities brokerage firms, insurance companies, money market and other mutual funds and other financial institutions operating in the Company's market area and elsewhere, including institutions operating locally, regionally, nationally and internationally, together with such competitors offering banking products and services by mail, telephone, computer and the Internet; and (e) the failure of assumptions underlying the establishment of reserves for loan losses and estimations of values of collateral and various financial assets and liabilities and technological changes are more difficult or expensive than anticipated. All written or oral forward-looking statements attributable to the Company are expressly qualified in their entirety by these cautionary statements.

The Company

General. The Company was incorporated as a business corporation under the laws of the State of Texas on March 28, 1996, for the purpose of serving as a bank holding company for Southwest Bank of Texas National Association (the "Bank"). The holding company formation was consummated and the Company acquired all of the outstanding shares of capital stock of the Bank as of the close of business on June 30, 1996. Based upon total assets as of December 31, 2000, the Company ranks as the largest independent bank holding company headquartered in the Houston metropolitan area. The Company's headquarters are located at 4400 Post Oak Parkway, Houston, Texas 77027, and its telephone number is (713) 235-8800.

Mergers and Acquisitions. On August 1, 1997, Pinemont Bank was merged with and into the Bank in exchange for approximately 3.3 million shares of Company Common Stock in a transaction accounted for as a pooling-of-interests. The acquisition of Pinemont Bank added \$235 million in total assets and \$219 million in total deposits to the Company's balance sheet and nine banking locations to the Company's operations.

On April 1, 1999, Fort Bend Holding Corp. was merged with and into the Company and Fort Bend's subsidiary savings and loan association was merged with and into the Bank in exchange for approximately 4.1 million shares of Company Common Stock in a transaction accounted for as a pooling-of-interests. The acquisition of Fort Bend Holding Corp. added \$316 million in total assets and \$269 million in total deposits to the Company's balance sheet and seven banking locations to the Company's operations.

Through the merger with Fort Bend, the Company acquired Fort Bend's 51% ownership interest in Mitchell Mortgage Company L.L.C. ("Mitchell"), a full service mortgage banking affiliate of The Woodlands Operating Company

L.P. ("Woodlands"). On June 17, 1999, the Company issued 307,323 shares of Company Common Stock to Woodlands in exchange for Woodlands' 49% ownership interest in Mitchell and Mitchell became a wholly-owned subsidiary of the Bank effective as of June 30, 1999. As a result, 100% of the accounts and operations of Mitchell after that date are included in the financial statements of the Company.

On December 29, 2000, Citizens Bankers, Inc. was merged with and into the Company and the three wholly-owned subsidiary banks of Citizens Bankers, Inc. were merged with and into the Bank (and the assets and liabilities of a related partnership were acquired by the Bank) in exchange for approximately 4.0 million shares of Company Common Stock in a transaction accounted for as a pooling-of-interests. The acquisition of Citizens Bankers, Inc. added \$436 million in total assets and \$381 million in total deposits to the Company's balance sheet and seven banking locations to the Company's operations. See "Item 5.— Recent Sales of Unregistered Securities" for additional information on the Company's merger with Citizens Bankers, Inc.

Business Strategy. The Company provides an array of sophisticated products typically found only in major regional banks. These services are provided to middle market businesses in the Houston metropolitan area through 33 full service banking facilities. Each banking office has seasoned management with significant lending experience who exercises substantial autonomy over credit and pricing decisions, subject to loan committee approval for larger credits. This decentralized management approach, coupled with the continuity of service by the same staff members, enables the Company to develop long-term customer relationships, maintain high quality service and provide quick responses to customer needs. The Company believes that its emphasis on local relationship banking, together with its conservative approach to lending and resultant strong asset quality, are important factors in the success and the growth of the Company.

The Company seeks credit risks of good quality within its target market that exhibit positive historical trends, stable cash flows and secondary sources of repayment from tangible collateral. The Company extends credit for the purpose of obtaining and continuing long term relationships. Lenders are provided with detailed underwriting policies for all types of credit risks accepted by the Company and must obtain appropriate approvals for credit extensions in excess of conservatively assigned individuals' lending limits. The Company also maintains strict documentation requirements and extensive credit quality assurance practices in order to identify credit portfolio weaknesses as early as possible so any exposures that are discovered might be reduced.

The Company has a three-part strategy for growth. First, the Company will continue to actively target the "middle market" and private banking customers in Houston for loan and deposit opportunities as it has successfully done for the past ten years. The "middle market" is generally characterized by privately owned companies having annual revenues ranging from \$1 million to \$500 million and borrowings ranging from \$50,000 to \$10 million, but primarily in the \$150,000 to \$5 million range. Typical middle market customers seek a relationship with a local independent bank that is sensitive to their needs and understands their business philosophy. These customers desire a long-term relationship with a decision-making loan officer who is responsive and experienced and has ready access to a bank's senior management. In implementing this part of its strategy, the Company continues to explore opportunities (i) to solidify its existing customer relationships and build new customer relationships by providing new services required by its middle market customers and (ii) to expand its base of services in the professional and executive market to meet the demands of that sector.

Second, the Company intends to establish branches in areas that demographically complement its existing or targeted customer base. As other local banks are acquired by out-of-state organizations, the Company believes that the establishment of branches will better meet the needs of customers in many Houston area neighborhoods who feel disenfranchised by larger regional or national organizations.

Third, the Company may pursue selected acquisitions of other financial institutions. The Company intends to conduct thorough studies and reviews of any possible acquisition candidates to assure that they are consistent with the Company's existing goals, both from an economic and strategic perspective. The Company believes market and regulatory factors may present opportunities for the Company to acquire other financial institutions.

The Bank

The Bank provides a complete range of retail and commercial banking services that compete directly with major regional banks. Loans consist of commercial loans to middle market businesses, loans to individuals, commercial real estate loans, residential mortgages and construction loans. The Bank also originates and purchases residential and commercial mortgage loans to sell to investors with servicing rights retained. The Bank also promotes residential and commercial construction financing to builders and developers and acts as a broker in the origination of multi-family and commercial real estate loans. In addition, the Bank offers a broad array of fee income products including merchant card services, letters of credit, accounts receivable financing, customized cash management services, brokerage and mutual funds, trust and private banking activities.

The Bank maintains a staff of professional treasury management marketing officers who consult with middle market companies to design custom cost-effective cash management systems. The Bank offers a full product line of cash concentration, disbursement and automated information reporting services and a full suite of Internet products comparable to those offered by any major regional bank. Through the Bank's continued investment in new technology and people, the Bank has been able to attract some of Houston's largest middle market companies to utilize the Bank's treasury management products. The Bank has also been able to attract new loan customers through use of the Bank's treasury management products, such as an image-based lock box service and controlled disbursement and sweep products, which allow borrowers to minimize interest expense and convert excess operating funds into interest income. Through the use of an interactive terminal or personal computer, the Bank's NetStar system provides customers with instant access to all bank account information with multiple intraday updates. The Bank makes business communication more efficient through Electronic Data Interchange ("EDI"), which is an inter-organizational computer-to-computer exchange of business documentation in a standard computer-processable format. Through the use of EDI and electronic payments, the Bank can provide the customer with a paperless funds management system. Positive Pay, a service under which the Bank only pays checks listed on a legitimate "company issue" file, is another product which helps prevent check fraud. The Bank's average commercial customer uses five treasury management services. Because these services help customers improve their treasury operations and achieve new efficiencies in cash management, they are extremely useful in building and maintaining long-term relationships.

The Bank has a retail presence in 33 locations throughout the Houston metropolitan area. Such locations are emerging as an important source of bank funding and fee income. Retail products consist of both traditional deposit accounts such as checking, savings, money market accounts and certificates of deposit, and a wide array of consumer loan and electronic banking alternatives. The Bank is putting a strong emphasis on the cultivation of retail market opportunities and on its retail staff to help expand and deepen customer relationships.

The Bank maintains a strong community orientation by, among other things, supporting active participation of all employees in local charitable, civic, school and church activities. Several banking offices also appoint selected customers to a business development board that assists in introducing prospective customers to the Bank and in developing or modifying products and services to better meet customer needs.

Competition

The banking business is highly competitive, and the profitability of the Company will depend principally upon the Company's ability to compete in its market area. The Company competes with other commercial and savings banks, savings and loan associations, credit unions, finance companies, mutual funds, insurance companies, brokerage and investment banking firms, asset-based non-bank lenders and certain other non-financial institutions, including certain governmental organizations which may offer subsidized financing at lower rates than those offered by the Company. The Company has been able to compete effectively with other financial institutions by emphasizing technology and customer service, including local office decision-making on loans, establishing long-term customer relationships and building customer loyalty, and by providing products and services designed to address the specific needs of its customers.

The success of the Company is also highly dependent on the economic strength of the Company's general market area. Significant deterioration in the local economy or economic problems in the greater Houston area could substantially impact the Company's performance. In addition, the enactment of the Gramm-Leach-Bliley Act (see discussion below) which breaks down many barriers between the banking, securities and insurance industries, may significantly affect the competitive environment in which the Company operates.

Employees

As of December 31, 2000, the Company had 1,313 full-time employees, 415 of whom were officers of the Bank. The Company provides medical and hospitalization insurance to its full-time employees. The Company has also provided most of its employees with the benefit of Common Stock ownership through the Company's contributions to a 401(k) plan, in which 879 of its employees are currently participating. The Company considers its relations with its employees to be excellent.

Supervision and Regulation

The federal banking laws contain numerous provisions affecting various aspects of the business and operations of the Company and the Bank. The following description or references herein to applicable statutes and regulations, which are not intended to be complete descriptions of these provisions or their effects on the Company or the Bank, are brief summaries and are qualified in their entirety by reference to such statutes and regulations.

The Bank

As a national banking association, the Bank is principally supervised, examined and regulated by the Office of the Comptroller of the Currency (the "OCC"). The OCC regularly examines such areas as capital adequacy, reserves, loan portfolio, investments and management practices. The Bank must also furnish quarterly and annual reports to the OCC, and the OCC may exercise cease and desist and other enforcement powers over the Bank if its actions represent unsafe or unsound practices or violations of law. Since the deposits of the Bank are insured by the Bank Insurance Fund ("BIF") of the Federal Deposit Insurance Corporation (the "FDIC"), the Bank is also subject to regulation and supervision by the FDIC. Because the Board of Governors of the Federal Reserve System (the "Federal Reserve Board") regulates the Company, the Federal Reserve Board also has supervisory authority which affects the Bank.

Restrictions on Transactions With Affiliates and Insiders. The Bank is subject to certain federal statutes limiting transactions with the Company and its nonbanking affiliates. Section 23A of the Federal Reserve Act affects loans or other credit extensions to, asset purchases from and investments in affiliates of the Bank. Such transactions with the Company or any of its nonbanking subsidiaries are limited in amount to ten percent of the Bank's capital and surplus and, with respect to the Company and all of its nonbanking subsidiaries together, to an aggregate of twenty percent of the Bank's capital and surplus. Furthermore, such loans and extensions of credit, as well as certain other transactions, are required to be secured in specified amounts.

In addition, Section 23B of the Federal Reserve Act requires that certain transactions between the Bank, including its subsidiaries, and its affiliates must be on terms substantially the same, or at least as favorable to the Bank or its subsidiaries, as those prevailing at the time for comparable transactions with or involving other nonaffiliated persons. In the absence of such comparable transactions, any transaction between the Bank and its affiliates must be on terms and under circumstances, including credit standards, that in good faith would be offered to or would apply to nonaffiliated persons. The Bank is also subject to certain prohibitions against any advertising that indicates the Bank is responsible for the obligations of its affiliates.

The restrictions on loans to directors, executive officers, principal shareholders and their related interests (collectively referred to herein as "insiders") contained in the Federal Reserve Act and Regulation O apply to all insured institutions and their subsidiaries and holding companies. These restrictions include limits on loans to one borrower and conditions that must be met before such loans can be made. There is also an aggregate limitation on all loans to insiders and their related interests. These loans cannot exceed the institution's total unimpaired capital and surplus,

and the OCC may determine that a lesser amount is appropriate. Insiders are subject to enforcement actions for knowingly accepting loans in violation of applicable restrictions.

Interest Rate Limits. Interest rate limitations for the Bank are primarily governed by the National Bank Act which generally defers to the laws of the state where the bank is located. Under the laws of the State of Texas, the maximum annual interest rate that may be charged on most loans made by the Bank is based on doubling the average auction rate, to the nearest 0.25%, for 26 week United States Treasury Bills, as computed by the Office of the Consumer Credit Commissioner of the State of Texas. However, the maximum rate does not decline below 18% or rise above 24% (except for loans in excess of \$250,000 that are made for business, commercial, investment or other similar purposes in which case the maximum annual rate may not rise above 28%, rather than 24%). On fixed rate closed-end loans, the maximum non-usurious rate is to be determined at the time the rate is contracted, while on floating rate and open-end loans (such as credit cards), the rate varies over the term of the indebtedness. State usury laws (but not late charge limitations) have been preempted by federal law for loans secured by a first lien on residential real property.

Examinations. The OCC periodically examines and evaluates national banks. Based upon such an evaluation, the OCC may revalue the assets of a national bank and require that it establish specific reserves to compensate for the difference between the OCC-determined value and the book value of such assets. Onsite examinations are to be conducted every 12 months, except that certain well capitalized banks may be examined every 18 months. The Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA") authorizes the OCC to assess the institution for its costs of conducting the examinations.

Prompt Corrective Action. In addition to the capital adequacy guidelines, FDICIA requires the OCC to take "prompt corrective action" with respect to any national bank which does not meet specified minimum capital requirements. The applicable regulations establish five capital levels, ranging from "well capitalized" to "critically undercapitalized," which authorize, and in certain cases require, the OCC to take certain specified supervisory action. Under regulations implemented under FDICIA, a national bank is considered well capitalized if it has a total risk-based capital ratio of 10.0% or greater, a Tier 1 risk-based capital ratio of 8.0% or greater, and a leverage ratio of 5.0% or greater, and it is not subject to an order, written agreement, capital directive, or prompt corrective action directive to meet and maintain a specific capital level for any capital measure. A national bank is considered adequately capitalized if it has a total risk-based capital ratio of 8.0% or greater, a Tier 1 risk-based capital ratio of at least 4.0% and a leverage capital ratio of 4.0% or greater (or a leverage ratio of 3.0% or greater if the institution is rated composite 1 in its most recent report of examination, subject to appropriate federal banking agency guidelines), and the institution does not meet the definition of an undercapitalized institution. A national bank is considered undercapitalized if it has a total risk-based capital ratio that is less than 8.0%, a Tier 1 risk-based capital ratio that is less than 4.0%, or a leverage ratio that is less than 4.0% (or a leverage ratio that is less than 3.0% if the institution is rated composite 1 in its most recent report of examination, subject to appropriate federal banking agency guidelines). A significantly undercapitalized institution is one which has a total risk-based capital ratio that is less than 6.0%, a Tier 1 risk-based capital ratio that is less than 3.0%, or a leverage ratio that is less than 3.0%. A critically undercapitalized institution is one which has a ratio of tangible equity to total assets that is equal to or less than 2.0%. Under certain circumstances, a well capitalized, adequately capitalized or undercapitalized institution may be treated as if the institution were in the next lower capital category.

With certain exceptions, national banks will be prohibited from making capital distributions or paying management fees to a holding company if the payment of such distributions or fees will cause them to become undercapitalized. Furthermore, undercapitalized national banks will be required to file capital restoration plans with the OCC. Such a plan will not be accepted unless, among other things, the banking institution's holding company guarantees the plan up to a certain specified amount. Any such guarantee from a depository institution's holding company is entitled to a priority of payment in bankruptcy. Undercapitalized national banks also will be subject to restrictions on growth, acquisitions, branching and engaging in new lines of business unless they have an approved capital plan that permits otherwise. The OCC also may, among other things, require an undercapitalized national bank to issue shares or obligations, which could be voting stock, to recapitalize the institution or, under certain circumstances, to divest itself of any subsidiary.

The OCC is authorized by FDICIA to take various enforcement actions against any significantly undercapitalized national bank and any national bank that fails to submit an acceptable capital restoration plan or fails to implement a plan accepted by the OCC. These powers include, among other things, requiring the institution to be recapitalized, prohibiting asset growth, restricting interest rates paid, requiring primary approval of capital distributions by any bank holding company which controls the institution, requiring divestiture by the institution of its subsidiaries or by the holding company of the institution itself, requiring new election of directors, and requiring the dismissal of directors and officers.

Significantly and critically undercapitalized national banks may be subject to more extensive control and supervision. The OCC may prohibit any such institution from, among other things, entering into any material transaction not in the ordinary course of business, amending its charter or bylaws, or engaging in certain transactions with affiliates. In addition, critically undercapitalized institutions generally will be prohibited from making payments of principal or interest on outstanding subordinated debt. Within 90 days of a national bank becoming critically undercapitalized, the OCC must appoint a receiver or conservator unless certain findings are made with respect to the prospect for the institution's continued viability.

As of December 31, 2000, the Bank met the capital requirements of a "well capitalized" institution.

Dividends. There are certain statutory limitations on the payment of dividends by national banks. Without approval of the OCC, dividends may not be paid by the Bank in an amount in any calendar year which exceeds the Bank's total net profits for that year, plus its retained profits for the preceding two years, less any required transfers to capital surplus. In addition, a national bank may not pay dividends in excess of total retained profits, including current year's earnings after deducting bad debts in excess of reserves for losses. In some cases, the OCC may find a dividend payment that meets these statutory requirements to be an unsafe or unsound practice. Under FDICIA, the Bank cannot pay a dividend if it will cause the Bank to be undercapitalized.

FDIC Insurance Assessments

Pursuant to FDICIA, the FDIC adopted a risk-based assessment system for insured depository institutions that takes into account the risks attributable to different categories and concentrations of assets and liabilities. The risk-based system assigns an institution to one of three capital categories: (i) well-capitalized, (ii) adequately capitalized, or (iii) undercapitalized. These three categories are substantially similar to the prompt corrective action categories, with the "undercapitalized" category including institutions that are undercapitalized, significantly undercapitalized, and critically undercapitalized for prompt corrective action purposes. An institution is also assigned by the FDIC to one of three supervisory subgroups within each capital group. The supervisory subgroup to which an institution is assigned is based on an evaluation provided to the FDIC by the institution's primary federal regulator and information which the FDIC determines to be relevant to the institution's financial condition and the risk posed to the deposit insurance funds (which may include, if applicable, information provided by the institution's state supervisor). An institution's insurance assessment rate is then determined based on the capital category and supervisory category to which it is assigned.

Under the final risk-based assessment system there are nine assessment risk classifications (i.e., combinations of capital groups and supervisory subgroups) to which different assessment rates are applied. Assessment rates for deposit insurance currently range from zero basis points to 27 basis points. The supervisory subgroup to which an institution is assigned by the FDIC is confidential and may not be disclosed. A bank's rate of deposit insurance assessments will depend on the category and subcategory to which the bank is assigned by the FDIC. Any increase in insurance assessments could have an adverse effect on the earnings of insured institutions, including the Bank.

Under FDICIA, insurance of deposits may be terminated by the FDIC upon a finding that the institution has engaged in unsafe and unsound practices, is in an unsafe or unsound condition to continue operations, or has violated any applicable law, regulation, rule, order, or condition imposed by the FDIC. Management does not know of any practice, condition or violation that might lead to termination of deposit insurance.

Conservator and Receivership Powers. FDICIA significantly expanded the authority of the federal banking regulators to place depository institutions into conservatorship or receivership to include, among other things, appointment of

the FDIC as conservator or receiver of an undercapitalized institution under certain circumstances. In the event the Bank is placed into conservatorship or receivership, the FDIC is required, subject to certain exceptions, to choose the method for resolving the institution that is least costly to the BIF, such as liquidation.

Brokered Deposit Restrictions. The Financial Institutions Reform, Recovery and Enforcement Act of 1989 (“FIRREA”) and FDICIA generally limit institutions which are not well capitalized from accepting brokered deposits. In general, undercapitalized institutions may not solicit, accept or renew brokered deposits. Adequately capitalized institutions may not solicit, accept or renew brokered deposits unless they obtain a waiver from the FDIC. Even in that event, they may not pay an effective yield of more than 75 basis points over the effective yield paid on deposits of comparable size and maturity in the institution’s normal market area for deposits accepted from within that area, or the national rate paid on deposits of comparable size and maturity for deposits accepted from outside the institution’s normal market area.

Consumer Laws and Regulations. In addition to the laws and regulations discussed herein, the Bank is also subject to certain consumer laws and regulations that are designed to protect consumers in transactions with banks. While the list set forth herein is not exhaustive, these laws and regulations include the Truth in Lending Act, the Truth in Savings Act, the Electronic Funds Transfer Act, the Expedited Funds Availability Act, the Community Reinvestment Act, the Equal Credit Opportunity Act, and the Fair Housing Act, among others. These laws and regulations mandate certain disclosure requirements and regulate the manner in which financial institutions must deal with customers when taking deposits or making loans to such customers. The Bank must comply with the applicable provisions of these consumer protection laws and regulations as part of their ongoing customer relations.

Under Section 501 of the Gramm-Leach-Bliley Act (see discussion below), the federal banking agencies are required to establish appropriate standards for financial institutions regarding the implementation of safeguards to ensure the security and confidentiality of customer records and information, protection against any anticipated threats or hazards to the security or integrity of such records and protection against unauthorized access to or use of such records or information in a way that could result in substantial harm or inconvenience to a customer. The agencies have published a joint final rule which is effective July 1, 2001. Among other matters, the rule requires each bank to implement a comprehensive written information security program that includes administrative, technical and physical safeguards relating to customer information.

Under the Gramm-Leach-Bliley Act, a financial institution must provide its customers with a notice of privacy policies and practices. Section 502 prohibits a financial institution from disclosing nonpublic personal information about a consumer to nonaffiliated third parties unless the institution satisfies various notice and opt-out requirements and the customer has not elected to opt out of the disclosure. Under Section 504, the agencies are authorized to issue regulations as necessary to implement notice requirements and restrictions on a financial institution’s ability to disclose nonpublic personal information about consumers to nonaffiliated third parties. In June 2000, the federal banking agencies issued a final rule, effective November 13, 2000, but compliance with which is optional until July 1, 2001. Under the rule, all banks must develop initial and annual privacy notices which describe in general terms the bank’s information sharing practices. Banks that share nonpublic personal information about customers with nonaffiliated third parties must also provide customers with an opt-out notice and a reasonable period of time for the customer to opt out of any such disclosure (with certain exceptions). Limitations are placed on the extent to which a bank can disclose an account number or access code for credit card, deposit, or transaction accounts to any nonaffiliated third party for use in marketing.

The Company

The Company is a bank holding company registered under the Bank Holding Company Act of 1956 (the “BHCA”), and is subject to supervision and regulation by the Federal Reserve Board. The BHCA and other Federal laws subject bank holding companies to particular restrictions on the types of activities in which they may engage, and to a range of supervisory requirements and activities, including regulatory enforcement actions for violations of laws and regulations. As a bank holding company, the Company’s activities and those of its banking and nonbanking subsidiaries have in the

past been limited to the business of banking and activities closely related or incidental to banking. Under new banking legislation (see discussion of Gramm-Leach-Bliley Act below), however, national banks will have broadened authority, subject to limitations on investment, to engage in activities that are financial in nature (other than insurance underwriting, merchant or insurance portfolio investment, real estate development and real estate investment) through subsidiaries if the bank is well capitalized, well managed and has at least a satisfactory rating under the Community Reinvestment Act.

Because the Company is a legal entity separate and distinct from its subsidiaries, its right to participate in the distribution of assets of any subsidiary upon the subsidiary's liquidation or reorganization will be subject to the prior claims of the subsidiary's creditors. In the event of a liquidation or other resolution of the Bank, the claims of depositors and other general or subordinated creditors of the Bank are entitled to a priority of payment over the claims of holders of any obligation of the institution to its shareholders, including any depository institution holding company (such as the Company) or any shareholder or creditor thereof.

Safe and Sound Banking Practices. Bank holding companies are not permitted to engage in unsafe and unsound banking practices. For example, the Federal Reserve Board's Regulation Y requires a holding company to give the Federal Reserve Board prior notice of any redemption or repurchase of its own equity securities, if the consideration to be paid, together with the consideration paid for any repurchases or redemptions in the preceding year, is equal to 10% or more of the company's consolidated net worth. The Federal Reserve Board may oppose the transaction if it believes that the transaction would constitute an unsafe or unsound practice or would violate any law or regulation. As another example, a holding company could not impair its subsidiary bank's soundness by causing it to make funds available to nonbanking subsidiaries or their customers if the Federal Reserve Board believed it not prudent to do so.

FIRREA expanded the Federal Reserve Board's authority to prohibit activities of bank holding companies and their nonbanking subsidiaries which represent unsafe and unsound banking practices or which constitute violations of laws or regulations. Notably, FIRREA increased the amount of civil money penalties which the Federal Reserve Board can assess for certain activities conducted on a knowing and reckless basis, if those activities caused a substantial loss to a depository institution. The penalties can be as high as \$1,000,000 for each day the activity continues. FIRREA also expanded the scope of individuals and entities against which such penalties may be assessed.

Anti-Tying Restrictions. Bank holding companies and their affiliates are prohibited from tying the provision of certain services, such as extensions of credit, to other services offered by a holding company or its affiliates.

Annual Reporting; Examinations. The Company is required to file an annual report with the Federal Reserve Board, and such additional information as the Federal Reserve Board may require pursuant to the BHCA. The Federal Reserve Board may examine a bank holding company or any of its subsidiaries, and charge the Company for the cost of such an examination.

Capital Adequacy Requirements. The Federal Reserve Board has adopted a system using risk-based capital guidelines to evaluate the capital adequacy of bank holding companies. Under the guidelines, specific categories of assets and certain off-balance sheet assets such as letters of credit are assigned different risk weights, based generally on the perceived credit risk of the asset. These risk weights are multiplied by corresponding asset balances to determine a "risk-weighted" asset base. The guidelines require a minimum total risk-based capital ratio of 8.0% (of which at least 4.0% is required to consist of Tier 1 capital elements).

In addition to the risk-based capital guidelines, the Federal Reserve Board uses a leverage ratio as an additional tool to evaluate the capital adequacy of bank holding companies. The leverage ratio is a company's Tier 1 capital divided by its total consolidated average assets. Bank holding companies must maintain a minimum leverage ratio of at least 3.0%, although most organizations are expected to maintain leverage ratios that are 100 to 200 basis points above this minimum ratio.

The federal banking agencies' risk-based and leverage ratios are minimum supervisory ratios generally applicable to banking organizations that meet certain specified criteria, assuming that they have the highest regulatory rating.

Banking organizations not meeting these criteria are expected to operate with capital positions well above the minimum ratios. The federal bank regulatory agencies may set capital requirements for a particular banking organization that are higher than the minimum ratios when circumstances warrant. Federal Reserve Board guidelines also provide that banking organizations experiencing internal growth or making acquisitions will be expected to maintain strong capital positions substantially above the minimum supervisory levels, without significant reliance on intangible assets. In addition, the regulations of the Federal Reserve Board provide that concentration of credit risk and certain risks arising from nontraditional activities, as well as an institution's ability to manage these risks, are important factors to be taken into account by regulatory agencies in assessing an organization's overall capital adequacy.

The Federal Reserve Board recently adopted amendments to its risk-based capital regulations to provide for the consideration of interest rate risk in the agencies' determination of a banking institution's capital adequacy.

Gramm-Leach-Bliley Act

Traditionally, the activities of bank holding companies have been limited to the business of banking and activities closely related or incidental to banking. On November 12, 1999, however, the Gramm-Leach-Bliley Act was signed into law which permits bank holding companies to engage in a broader range of financial activities. Specifically, bank holding companies may elect to become "financial holding companies" which may affiliate with securities firms and insurance companies and engage in other activities that are financial in nature or incidental to a financial activity. A bank holding company may become a financial holding company under the new statute only if each of its subsidiary banks is well capitalized, is well managed and has at least a satisfactory rating under the Community Reinvestment Act. A bank holding company that falls out of compliance with such requirement may be required to cease engaging in certain activities. Any bank holding company which does not elect to become a financial holding company remains subject to the current restrictions of the Bank Holding Company Act.

Under the new legislation, the Federal Reserve Board serves as the primary "umbrella" regulator of financial holding companies with supervisory authority over each parent company and limited authority over its subsidiaries. The primary regulator of each subsidiary of a financial holding company will depend on the type of activity conducted by the subsidiary. For example, broker-dealer subsidiaries will be regulated largely by securities regulators and insurance subsidiaries will be regulated largely by insurance authorities.

Under the Gramm-Leach-Bliley Act, among the activities that will be deemed "financial in nature" for "financial holding companies" are, in addition to traditional lending activities, securities underwriting, dealing in or making a market in securities, sponsoring mutual funds and investment companies, insurance underwriting and agency activities, activities which the Federal Reserve Board determines to be closely related to banking, and certain merchant banking activities.

In January 2001, the Federal Reserve Board and the Secretary of the Treasury promulgated final regulations governing the scope of permissible merchant banking investments which are those made under Section 4(k)(4)(H) of the Bank Holding Company Act, as amended by the Gramm-Leach-Bliley Act, which authorizes a financial holding company, directly or indirectly as principal or on behalf of one or more persons, to acquire or control any amount of shares, assets or ownership interests of a company or other entity that is engaged in any activity not otherwise authorized for the financial holding company under Section 4 of the Bank Holding Company Act. Under the regulation, the types of ownership that may be acquired include shares, assets or ownership interests of a company or other entity including debt or equity securities, warrants, options, partnership interests, trust certificates or other instruments representing an ownership interest in a company or entity whether voting or nonvoting. The merchant banking investments may be made by the financial holding company or any of its subsidiaries, other than a depository institution or subsidiary of a depository institution. Before acquiring or controlling a merchant banking investment, a financial holding company must either be or have a securities affiliate registered under the Securities Exchange Act of 1934 or a qualified insurance affiliate. The regulation places restrictions on the ability of a financial holding company to become involved in the routine management or operation of any of its portfolio companies. The regulation also provides that a financial holding company may own or control shares, assets and ownership interests pursuant to the merchant banking provisions only

for such period of time as to enable the sale or disposition on a reasonable basis consistent with the financial viability of the financial holding company's merchant banking investment activities. Generally, the ownership period is limited to ten years. Special provisions are included in the regulation governing the investment by a financial holding company in private equity funds. Under the merchant banking regulation, a financial holding company may not, without Federal Reserve Board approval, have aggregate merchant banking investments exceeding 30 percent of the Tier 1 capital of the financial holding company; or after excluding interests in private equity funds, 20 percent of the Tier 1 capital of the financial holding company.

The Federal Reserve Board and Secretary of Treasury have also requested public comment on the issue of whether to add the activities of real estate brokerage and real estate management to the list of permissible activities for financial holding companies and financial subsidiaries of national banks. The Company cannot predict whether the proposal will be adopted or the form any final rule might take.

The Federal Reserve Board, the OCC, and the FDIC have proposed for comment a rule which would establish special minimum regulatory capital requirements for equity investments in non-financial companies. The proposed capital treatment would apply symmetrically to equity investments of banks and bank holding companies and would apply a series of marginal capital charges on covered equity investments that increase with the level of a banking organization's overall exposure to equity investments relative to the organization's Tier 1 Capital. This is the second proposal the agencies have made of this nature and the Company cannot predict what final form the regulation may take.

Enforcement Powers of the Federal Banking Agencies

The Federal Reserve Board and the OCC have broad enforcement powers, including the power to terminate deposit insurance, impose substantial fines and other civil and criminal penalties and appoint a conservator or receiver. Failure to comply with applicable laws, regulations and supervisory agreements could subject the Company or the Bank, as well as officers, directors and other institution-affiliated parties of these organizations, to administrative sanctions and potentially substantial civil money penalties. In addition to the grounds discussed above under " — The Bank — Prompt Corrective Action," the appropriate federal banking agency may appoint the FDIC as conservator or receiver for a banking institution (or the FDIC may appoint itself, under certain circumstances) if any one or more of a number of circumstances exist, including, without limitation, the fact that the banking institution is undercapitalized and has no reasonable prospect of becoming adequately capitalized; fails to become adequately capitalized when required to do so; fails to submit a timely and acceptable capital restoration plan; or materially fails to implement an accepted capital restoration plan.

Imposition of Liability for Undercapitalized Subsidiaries. FDICIA requires bank regulators to take "prompt corrective action" to resolve problems associated with insured depository institutions whose capital declines below certain levels. In the event an institution becomes "undercapitalized," it must submit a capital restoration plan. The capital restoration plan will not be accepted by the regulators unless each company having control of the undercapitalized institution guarantees the subsidiary's compliance with the capital restoration plan. Under FDICIA, the aggregate liability of all companies controlling an undercapitalized bank is limited to the lesser of 5% of the institution's assets at the time it became undercapitalized or the amount necessary to cause the institution to be "adequately capitalized." The guarantee and limit on liability expire after the regulators notify the institution that it has remained adequately capitalized for each of four consecutive calendar quarters. FDICIA grants greater powers to the bank regulators in situations where an institution becomes "significantly" or "critically" undercapitalized or fails to submit a capital restoration plan. For example, a bank holding company controlling such an institution can be required to obtain prior Federal Reserve Board approval of proposed dividends, or might be required to consent to a consolidation or to divest the troubled institution or other affiliates. At December 31, 2000, the Bank met the requirements of a "well capitalized" institution and, therefore, these requirements presently do not apply to the Company.

Acquisitions by Bank Holding Companies. The BHCA requires every bank holding company to obtain the prior approval of the Federal Reserve Board before it may acquire all or substantially all of the assets of any bank, or direct or indirect ownership or control of more than 5% of any class of voting shares of any bank.

The Federal Reserve Board will allow the acquisition by a bank holding company of an interest in any bank located in another state only if the laws of the state in which the target bank is located expressly authorize such acquisition. Texas law permits, in certain circumstances, out-of-state bank holding companies to acquire banks and bank holding companies in Texas.

Expanding Enforcement Authority

One of the major effects of FDICIA was the increased ability of banking regulators to monitor the activities of banks and their holding companies. In addition, the Federal Reserve Board and FDIC have extensive authority to police unsafe or unsound practices and violations of applicable laws and regulations by depository institutions and their holding companies. For example, the FDIC may terminate the deposit insurance of any institution which it determines has engaged in an unsafe or unsound practice. The agencies can also assess civil money penalties, issue cease and desist or removal orders, seek injunctions, and publicly disclose such actions.

Effect on Economic Environment

The policies of regulatory authorities, including the monetary policy of the Federal Reserve Board, have a significant effect on the operating results of bank holding companies and their subsidiaries. Among the means available to the Federal Reserve Board to affect the money supply are open market operations in U.S. Government securities, changes in the discount rate on member bank borrowings, and changes in reserve requirements against member bank deposits. These means are used in varying combinations to influence overall growth and distribution of bank loans, investments and deposits, and their use may affect interest rates charged on loans or paid for deposits.

Federal Reserve Board monetary policies have materially affected the operating results of commercial banks in the past and are expected to continue to do so in the future. The nature of future monetary policies and the effect of such policies on the business and earnings of the Company and its subsidiaries cannot be predicted.

Item 2. Properties

Facilities

The Company currently maintains 33 locations in the greater Houston area, fifteen of which are leased. The following table sets forth specific information on each branch, each of which offers full service banking. The Company's headquarters are located at 4400 Post Oak Parkway, in a 28-story office tower in the Galleria area in Houston, Texas.

Branch	Sq. Ft.	Location	Branch Deposits at December 31, 2000 (In thousands)
Galleria/Corporate(1)	154,200	4400 Post Oak Parkway	\$1,270,165
Northwest Crossing(1)	9,355	Highway 290 at Tidwell	291,680
Downtown-1100 Louisiana(1)	11,546	1100 Louisiana	93,455
12 Greenway Plaza(1)	2,669	12 Greenway Plaza	78,357
Medical Center(1)	2,437	6602 Fannin	19,386
Memorial City(1)	3,554	899 Frostwood	23,539
Downtown — One Houston Center(1)	6,604	909 Fannin	38,243
Sugar Land	4,000	14965 Southwest Freeway	51,962
Greenspoint	3,797	Sam Houston at Ronan Road	27,690
3 Greenway Plaza(1)	2,549	3 Greenway Plaza, Suite C118	3,221
Hempstead	17,000	12130 Hempstead Highway	123,172
Tanglewood	5,625	5791 Woodway	88,472
Pasadena	4,900	4207 Fairmont Parkway	36,844
Memorial West(1)	1,700	14803 Memorial	9,096
Spring	6,300	2000 Spring Cypress Road	46,670
Bell Tower(1)	4,500	1330 Wirt Road	61,268
Kingwood	5,500	29805 Loop 494	49,045
North Point	5,000	9191 North Loop East	10,059
Porter(1)	2,450	23741 Highway 59, Suite 2	10,280
Rosenberg	45,000	3400 Avenue H	139,907
East Bernard	1,500	9212 Highway 60	19,366
Needville	2,500	3328 School Street	38,750
Bissonnet(1)	1,520	10881 Bissonnet	15,927
Katy(1)	2,800	919 Avenue C	14,177
Missouri City(1)	8,446	5819 Highway 6	24,075
The Woodlands	27,387	4576 Research Forest Drive	128,109
Baytown	49,781	1300 Rollingbrook	245,222
Garth Road(1)	2,000	6900 Garth Road	3,163
Lacy Drive	9,200	1308 Lacy Drive	64,309
Fairmont Parkway	3,200	1401 Fairmont Parkway	13,459
Red Bluff	6,400	3901 Red Bluff	25,079
South Shaver	2,750	2222 South Shaver	6,780
Bay City	10,000	1700 Sixth Street	22,943
			\$3,093,870

(1) Leased location.

Item 3. Legal Proceedings

The Company is involved in various legal proceedings that arise in the normal course of business. In the opinion of management of the Company, after consultation with its legal counsel, such legal proceedings are not expected to have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows.

Item 4. Submission of Matters to a Vote of Security Holders

No matter was submitted during the fourth quarter of the fiscal year covered by this Annual Report to a vote of the Company's security holders.

PART II

Item 5. Market for Registrant's Common Equity and Related Stockholder Matters

The Company's Common Stock began trading on the NASDAQ Stock Market on January 28, 1997, and is quoted in such Market under the symbol "SWBT". The Company's Common Stock was not publicly traded, nor was there an established market therefor, prior to January 28, 1997. On February 16, 2001, there were approximately 1,059 holders of record of the Company's Common Stock.

No cash dividends have ever been paid by the Company on its Common Stock, and the Company does not anticipate paying any cash dividends on its Common Stock in the foreseeable future. The Company's principal source of funds to pay cash dividends on its Common Stock would be cash dividends from the Bank. There are certain statutory limitations on the payment of dividends by national banks. Without approval of the OCC, dividends in any calendar year may not exceed the Bank's total net profits for that year, plus its retained profits for the preceding two years, less any required transfers to capital surplus or to a fund for the retirement of any preferred stock. In addition, a dividend may not be paid in excess of a bank's cumulative net profits after deducting bad debts in excess of the allowance for loan losses. As of December 31, 2000, approximately \$104.4 million was available for payment of dividends by the Bank to the Company under these restrictions without regulatory approval. See "Item 1. Business—Supervision and Regulation."

The following table presents the range of high and low sale prices reported on the NASDAQ during the years ended December 31, 2000 and December 31, 1999.

	2000				1999			
	Fourth Qtr.	Third Qtr.	Second Qtr.	First Qtr.	Fourth Qtr.	Third Qtr.	Second Qtr.	First Qtr.
Common stock sale price:								
High	\$ 45 ⁵ / ₈	\$ 34 ⁵ / ₈	\$ 21 ¹¹ / ₁₆	\$ 20 ¹ / ₄	\$20	\$18 ⁷ / ₁₆	\$18 ⁵ / ₈	\$18 ³ / ₁₆
Low	29 ¹⁵ / ₁₆	20 ⁷ / ₁₆	18 ¹ / ₄	14 ⁷ / ₈	16 ¹ / ₈	16 ¹ / ₈	12 ³ / ₈	11 ⁷ / ₈

Recent Sales of Unregistered Securities

On December 29, 2000, (i) Citizens Bankers, Inc., a Texas corporation ("Citizens") was merged with and into the Company pursuant to an Agreement and Plan of Merger dated October 16, 2000 (the "Merger Agreement"), between the Company and Citizens, and (ii) the Bank acquired all of the assets and liabilities of Citizens Bankers Limited Partnership, a Texas limited partnership ("CBLP") pursuant to a Purchase Agreement dated as of November 9, 2000 (the "Purchase Agreement") among the Company, the Bank, CBLP and Baytown Land I, Ltd. (The office building that houses Citizens and its principal subsidiary bank and certain unrelated tenants was the only significant asset of CBLP.) In addition, on that date (i) the three wholly-owned subsidiary banks of Citizens (Citizens Bank and Trust Company of Baytown, Texas, Baytown State Bank and Pasadena State Bank) were merged into the Bank and their seven banking locations became branches of the Bank, and (ii) the 57.834% owned subsidiary bank of Citizens, First National Bank of Bay City, became a 57.834% owned subsidiary bank of the Company as a result of the merger.

No underwriters were involved in the transaction; however, Keefe, Bruyette & Woods, Inc. acted as a financial advisor to Citizens and Legg Mason Wood Walker, Incorporated acted as a financial advisor to the Company.

A total of approximately 4.0 million shares of Company Common Stock were issued to the shareholders of Citizens and the partners of CBLP in the combined transaction, which has been accounted for as a pooling-of-interests. As of December 31, 2000, Citizens had total assets of \$436 million, net loans of \$133 million, total deposits of \$381 million and total shareholders' equity of \$47 million.

The shares of Company Common Stock issued pursuant to the Merger Agreement and the Purchase Agreement were issued in a transaction exempt from registration under the Securities Act of 1933 pursuant to Regulation D thereunder. Citizens and CBLP were closely held entities with over 77% of the equity interests being owned beneficially by members of two families. In accordance with Regulation D, the shares of Company Common Stock issued in the transaction were issued to 38 accredited investors and 23 non-accredited investors. Keefe, Bruyette & Woods, Inc. acted as the purchaser representative for the non-accredited investors.

Item 6. Selected Consolidated Financial Data

The following selected consolidated financial data should be read in conjunction with the Consolidated Financial Statements of the Company and the Notes thereto, appearing elsewhere in this Annual Report, and the information contained in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations." The selected historical consolidated financial data as of the end of and for each of the five years in the period ended December 31, 2000 are derived from the Company's Consolidated Financial Statements which have been audited by independent public accountants. Historical results have been restated to reflect the operations of Citizens Bankers, Inc. and Citizens Bankers Limited Partnership prior to December 29, 2000, the date on which they were merged into the Company in a transaction accounted for as a pooling of interests.

	Years Ended December 31,				
	2000	1999	1998	1997	1996
(Dollars in thousands, except per share data)					
Income Statement Data:					
Interest income	\$ 272,166	\$ 211,232	\$ 185,663	\$ 155,077	\$ 120,534
Interest expense	121,662	88,219	80,080	67,110	52,605
Net interest income	150,504	123,013	105,583	87,967	67,929
Provision for loan losses	7,053	6,474	4,261	4,242	2,482
Net interest income after provision for loan losses	143,451	116,539	101,322	83,725	65,447
Noninterest income	42,893	37,464	31,537	24,136	17,957
Noninterest expenses	120,157	104,511	87,870	71,756	56,436
Income before taxes and minority interest	66,187	49,492	44,989	36,105	26,968
Provision for income taxes	22,607	17,500	15,766	12,237	9,081
Minority interest	119	29	205	373	58
Net income before preferred stock dividend	43,461	31,963	29,018	23,495	17,829
Preferred stock dividend	—	—	—	36	457
Net income available to common shareholders	\$ 43,461	\$ 31,963	\$ 29,018	\$ 23,459	\$ 17,372
Per Share Data:					
Basic earnings per common share(1)	\$ 1.34	\$ 1.01	\$ 0.97	\$ 0.83	\$ 0.69
Diluted earnings per common share(1)	\$ 1.29	\$ 0.97	\$ 0.91	\$ 0.78	\$ 0.64
Cash dividends per common share paid by Fort Bend and Citizens	\$ 0.60	\$ 0.82	\$ 1.03	\$ 1.00	\$ 0.90
Book value per share	\$ 9.12	\$ 7.28	\$ 6.90	\$ 6.00	\$ 5.03
Average common shares (in thousands)	32,397	31,743	29,794	28,332	25,167
Average common share equivalents (in thousands)	1,232	1,200	2,947	3,080	3,304
Performance Ratios:					
Return on average assets	1.23%	1.06%	1.12%	1.10%	1.03%
Return on average common equity	17.00%	14.70%	15.10%	14.83%	14.69%
Net interest margin	4.64%	4.44%	4.38%	4.46%	4.36%
Efficiency ratio(3)	61.98%	65.07%	64.52%	64.28%	65.63%
Balance Sheet Data(2):					
Total assets	\$3,940,342	\$3,271,188	\$2,944,387	\$2,490,822	\$1,933,729
Securities	848,164	890,369	951,785	886,605	694,673
Loans	2,511,437	2,035,342	1,632,886	1,251,237	959,988
Allowance for loan losses	28,150	22,436	17,532	14,385	11,488
Total deposits	3,093,870	2,531,633	2,373,995	2,102,485	1,614,823
Total shareholders' equity	298,125	233,076	216,575	173,297	126,795
Capital Ratio:					
Average equity to average assets	7.23%	7.23%	7.39%	7.42%	7.00%
Asset Quality Ratios(2):					
Nonperforming assets(4) to loans and other real estate	0.41%	0.31%	0.31%	0.50%	0.51%
Net charge-offs to average loans	0.06%	0.09%	0.08%	0.12%	0.17%
Allowance for loan losses to total loans	1.16%	1.15%	1.08%	1.16%	1.20%
Allowance for loan losses to nonperforming loans(5)	297.82%	519.59%	441.39%	312.38%	391.68%

- (1) Basic earnings per common share is computed by dividing net income available to common shareholders by the weighted average number of common shares outstanding for the period. Diluted earnings per common share is computed by dividing net income available to common shareholders adjusted for any changes in income that would result from the assumed conversion of all potential dilutive common shares, by the sum of the weighted average number of common shares outstanding and the effect of all dilutive potential common shares outstanding for the period.
- (2) At period end, except net charge-offs to average loans.
- (3) Calculated by dividing total noninterest expenses by net interest income plus noninterest income, excluding net security gains (losses).
- (4) Nonperforming assets consist of nonperforming loans and other real estate owned.
- (5) Nonperforming loans consist of nonaccrual loans, troubled debt restructurings and loans contractually past due 90 days or more.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

Management's Discussion and Analysis of Financial Condition and Results of Operations analyzes the major elements of the Company's consolidated financial statements and should be read in conjunction with the Consolidated Financial Statements of the Company and Notes thereto and other detailed information appearing elsewhere in this Annual Report.

For the Years Ended December 31, 2000, 1999 and 1998

Overview

On December 29, 2000, Southwest Bancorporation of Texas, Inc. (the "Company") and Citizens Bankers, Inc. ("Citizens") completed their merger, which was accounted for as a pooling of interests. The merger agreement provided for the exchange of 249,443 shares of the Company's Common Stock for each share of Citizens Stock, resulting in the issuance of approximately 3.9 million shares of Company Common Stock on a fully diluted basis. In connection with this merger, the Company incurred approximately \$4.1 million in pretax merger-related expenses and other charges including investment banking fees, other professional fees and severance expenses (the "special charge").

In a related transaction, the Company, Citizens Bankers Limited Partnership ("CBLP") and Baytown Land I, Ltd., the general partner of CBLP, entered into an agreement pursuant to which the Company acquired the assets and assumed the liabilities of CBLP. CBLP's primary assets and liabilities were the bank building located at 1300 Rollingbrook and the related debt to third parties. In connection with this agreement, the Company issued approximately 106,000 shares of the Company's Common Stock on a fully diluted basis. The historical financial data has been restated to include the accounts and operations of Citizens and CBLP for all periods presented.

Total assets at December 31, 2000, 1999 and 1998 were \$3.94 billion, \$3.27 billion, and \$2.94 billion, respectively. This growth was a result of a strong local economy, the addition of new loan officers, aggressive marketing, and the Company's overall growth strategy. Loans were \$2.51 billion at December 31, 2000, an increase of \$476.1 million or 23% from \$2.04 billion at the end of 1999, marking the third consecutive year that total loan growth exceeded \$350 million. Loans were \$1.63 billion at year end 1998. Deposits increased to \$3.09 billion at year end 2000 from \$2.53 billion at year end 1999 and \$2.37 billion at year end 1998.

Net income available for common shareholders was \$43.5 million, \$32.0 million, and \$29.0 million and diluted earnings per common share was \$1.29, \$0.97, and \$0.91 for the years ended 2000, 1999 and 1998, respectively. This increase in net income was primarily the result of strong loan growth, maintaining strong asset quality and expense control and resulted in returns on average assets ("ROA") of 1.23%, 1.06%, and 1.12% and returns on average common equity ("ROE") of 17.00%, 14.70%, and 15.10% for the years ended 2000, 1999 and 1998, respectively.

Results for 2000 include the impact of the special charge taken in the fourth quarter. On an operating basis, excluding this special charge, the Company's net income was \$46.9 million, resulting in an ROA of 1.33%, ROE of 18.34%, and an efficiency ratio of 60.00%. Results for 1999 include \$4.5 million of merger-related expenses and other charges. On an operating basis, excluding these charges, the Company's net income was \$35.7 million, resulting in an ROA of 1.19%, ROE of 16.41%, and an efficiency ratio of 62.29%.

Results of Operations

Net Interest Income

Net interest income represents the amount by which interest income on interest-earning assets, including securities and loans, exceeds interest expense incurred on interest-bearing liabilities, including deposits and other borrowed funds. Net interest income is the principal source of the Company's earnings. In 2000, net interest income provided 77.8 % of the Company's net revenues, compared with 76.7% in 1999 and 77.0% in 1998. Interest rate fluctuations, as well as changes in the amount and type of earning assets and liabilities, combine to affect net interest income.

2000 versus 1999. Net interest margin increased 20 basis points in 2000 to 4.64%. The principal factor contributing to the increase was higher yielding earning assets partially offset by higher cost of funds resulting in slightly higher interest rate spreads.

Net interest income was \$150.5 million in 2000 compared to \$123.0 million in 1999, an increase of \$27.5 million or 22%. Growth in average earning assets was \$472.7 million or 17% while yields increased 77 basis points to 8.39%. Yields increased throughout 2000 as the Bank's prime lending rate increased. The yield on earning assets during the fourth quarter was the highest for the year, resulting in increased yields on a weighted average basis.

Net interest margin risk is typically related to a narrowing of the prime rate and cost of funds. The Company reduced this risk with a modestly asset sensitive balance sheet during 2000. On February 4, 2000 the Federal Reserve increased the federal funds rate and discount rate by 25 basis points. This was followed by two additional increases on March 23, 2000 and May 17, 2000 of 25 and 50 basis points, respectively. Due to the Bank's asset sensitivity, the net interest margin gradually increased during the second half of the year. This resulted in net interest margins of 4.64% and 4.44% and net interest spreads of 3.45% and 3.44% for 2000 and 1999, respectively.

The increase in net interest income was due primarily to a \$472.7 million or 17% increase in average earning assets. Average loans grew \$518.5 million or 29% during 2000 while average securities decreased \$45.1 million or 5% during the same period. The yield earned on average loans outstanding increased 71 basis points to 9.25% in 2000. Overall, the yield earned on average earning assets increased 77 basis points to 8.39% in 2000 compared to a 76 basis point increase in the rate paid on average interest-bearing liabilities.

1999 versus 1998. Net interest income totaled \$123.0 million in 1999 compared to \$105.6 million in 1998, an increase of \$17.4 million or 16%. This resulted in net interest margins of 4.44% and 4.38% and net interest spreads of 3.44% and 3.28% for 1999 and 1998, respectively.

The increase in net interest income was due primarily to a \$360.7 million or 15% increase in average interest-earning assets. Average loans grew \$352.8 million or 25% during 1999 while average securities grew \$110.1 million or 13% during the same period. The increase in net interest income caused by this increase in average interest-earning assets was partially offset by an increase in average interest-bearing liabilities of \$297.9 million or 16%. The yield earned on average interest-earning assets decreased eight basis points to 7.62% in 1999 compared to an overall decrease in the yield earned on average interest-bearing liabilities of 24 basis points to 4.18% for the period.

The following table presents, for the periods indicated, the total dollar amount of interest income from average interest-earning assets and the resultant yields, as well as the interest expense on average interest-bearing liabilities, expressed both in dollars and rates. No tax equivalent adjustments were made and all average balances are daily average balances. Nonaccruing loans have been included in the table as loans carrying a zero yield. The yield on the securities portfolio is based on average historical cost balances and does not give effect to changes in fair value that are reflected as a component of consolidated shareholders' equity.

Year Ended December 31,									
2000			1999			1998			
Average Outstanding Balance	Interest Earned/ Paid	Average Yield/ Rate	Average Outstanding Balance	Interest Earned/ Paid	Average Yield/ Rate	Average Outstanding Balance	Interest Earned/ Paid	Average Yield/ Rate	
(Dollars in thousands)									
Assets									
Interest-earning assets:									
Loans	\$2,281,340	\$210,990	9.25%	\$1,762,826	\$150,576	8.54%	\$1,410,061	\$125,847	8.92%
Securities	909,512	57,755	6.35	954,593	58,007	6.08	844,494	51,503	6.10
Federal funds sold and other	53,163	3,421	6.43	53,900	2,649	4.91	156,024	8,313	5.33
Total interest-earning assets	3,244,015	272,166	8.39%	2,771,319	211,232	7.62%	2,410,579	185,663	7.70%
Less allowance for loan losses	(25,326)			(20,161)			(15,825)		
	3,218,689			2,751,158			2,394,754		
Noninterest-earning assets	315,444			257,607			205,109		
Total assets	\$3,534,133			\$3,008,765			\$2,599,863		
Liabilities and shareholders' equity									
Interest-bearing liabilities:									
Money market and savings deposits	\$1,217,866	50,375	4.14%	\$1,008,980	34,766	3.45%	\$ 934,398	35,032	3.75%
Certificates of deposit	829,047	48,313	5.83	718,037	35,383	4.93	644,480	33,412	5.18
Repurchase agreements and borrowed funds	415,029	22,974	5.54	381,052	18,070	4.74	231,287	11,636	5.03
Total interest-bearing liabilities	2,461,942	121,662	4.94%	2,108,069	88,219	4.18%	1,810,165	80,080	4.42%
Noninterest-bearing liabilities:									
Noninterest-bearing demand deposits	774,111			656,428			573,708		
Other liabilities	42,487			26,840			23,842		
Total liabilities	3,278,540			2,791,337			2,407,715		
Shareholders' equity	255,593			217,428			192,148		
Total liabilities and shareholders' equity	\$3,534,133			\$3,008,765			\$2,599,863		
Net interest income	\$150,504			\$123,013			\$105,583		
Net interest spread			3.45%			3.44%			3.28%
Net interest margin			4.64%			4.44%			4.38%

The following table presents the dollar amount of changes in interest income and interest expense for the major components of interest-earning assets and interest-bearing liabilities and distinguishes between the increase (decrease) related to higher outstanding balances and the volatility of interest rates. For purposes of this table, changes attributable to both rate and volume which cannot be segregated have been allocated.

Year Ended December 31,							
2000 vs. 1999				1999 vs. 1998			
Increase (Decrease) Due to				Increase (Decrease) Due to			
Volume	Rate	Days	Total	Volume	Rate	Total	
(Dollars in thousands)							
Interest-earning assets:							
Loans	\$43,932	\$16,069	\$413	\$60,414	\$31,435	\$ (6,706)	\$24,729
Securities	(3,939)	3,528	159	(252)	6,696	(192)	6,504
Federal funds sold and other	(36)	801	7	772	(5,438)	(226)	(5,664)
Total increase (decrease) in interest income	39,957	20,398	579	60,934	32,693	(7,124)	25,569
Interest-bearing liabilities:							
Money market and savings deposits	7,162	8,352	95	15,609	2,780	(3,046)	(266)
Certificates of deposits	5,430	7,403	97	12,930	3,780	(1,809)	1,971
Repurchase agreements and borrowed funds	1,585	3,269	50	4,904	7,538	(1,104)	6,434
Total increase (decrease) in interest expense	14,177	19,024	242	33,443	14,098	(5,959)	8,139
Increase (decrease) in net interest income	\$25,780	\$ 1,374	\$337	\$27,491	\$18,595	\$ (1,165)	\$17,430

Provision for Loan Losses

The 2000 provision for loan losses was \$7.1 million, an increase of \$579,000 from 1999. The provision for the year ended 1999 was \$6.5 million, an increase of \$2.2 million from the year ended December 31, 1998. Net charge-offs during 2000 equaled \$1.3 million, which when subtracted from the provision for loan losses of \$7.1 million resulted in a net increase in the allowance for loan losses of \$5.8 million. Although no assurance can be given, management believes that the present allowance for loan losses is adequate considering loss experience, delinquency trends and current economic conditions. Management regularly reviews the Company's loan loss allowance as its loan portfolio grows and diversifies. (See "— Financial Condition — Loan Review and Allowance for Loan Losses.")

Noninterest Income

Noninterest income grew to \$42.9 million for the year ended December 31, 2000, an increase of \$5.4 million or 14% from 1999. Noninterest income totaled \$37.5 million in 1999, an increase of \$5.9 million or 19% from 1998.

Year Ended December 31,			
	2000	1999	1998
(Dollars in thousands)			
Service charges on deposit accounts	\$20,765	\$17,017	\$13,020
Investment services	6,017	4,868	4,173
Factoring fee income	4,063	3,169	1,775
Loan fee income	3,910	4,192	4,144
Bank-owned life insurance income	1,665	1,379	390
Letters of credit fee income	947	829	627
Gain (loss) on sale of securities, net	(467)	(134)	933
Other income	5,993	6,144	6,475
	\$42,893	\$37,464	\$31,537

The largest component of noninterest income is service charges, which were \$20.8 million for the year ended December 31, 2000, compared to \$17.0 million for 1999 and \$13.0 for 1998. These were increases of 22% and 31%, respectively for 2000 and 1999. Several factors contributed to this growth. First, during this three-year period the Company introduced several new products to their existing retail product line. Secondly, in August 1999, the Company initiated a deposit campaign encompassing all of their existing market areas and redesigned the consumer banking area which has experienced strong growth since its inception. Additionally, the number of deposit accounts grew from 116,197 at December 31, 1998 to 124,424 at December 31, 1999 and to 155,610 at December 31, 2000.

Additional areas of increased growth included investment services and factoring fee income. Factoring fee income is derived from the purchase of accounts receivable. Gross accounts receivable purchased was \$27.7 million at December 31, 2000, an increase of \$9.2 million from \$18.5 million at December 31, 1999. Investment services income grew to \$6.0 million, or 24% from the 1999 period. During the past several years, the international department and the foreign exchange division have experienced strong growth, including the addition of several experienced calling officers and an increase in referrals from the Company's growing customer base. This addition adds to the high quality of personal service and responsiveness to customer needs. Secondly the Company introduced new services such as confirmation of letters of credit for a variety of countries and banks. The international department also has a registered broker for non-U.S. citizens which allows the Company to offer investment products in that market as well.

Noninterest Expenses

For the year ended December 31, 2000, noninterest expenses totaled \$120.2 million, an increase of \$15.7 million, or 15%, from \$104.5 million during 1999, which had increased from \$87.9 million during 1998. The increase in noninterest expenses during these periods was due primarily to salaries and employee benefits and occupancy expenses. The efficiency ratio was 61.98%, 65.07% and 64.52% for the years ended December 31, 2000, 1999 and 1998 respectively.

Salaries and employee benefits expense was \$67.1 million for the year ended December 31, 2000, an increase of \$9.6 million or 17% from \$57.5 million for the year ended December 31, 1999. Salaries and employee benefits expense for the year ended December 31, 1999 increased \$6.6 million or 13% from the same period in 1998. This increase was due primarily to hiring of additional personnel required to accommodate the Company's growth. Total full-time equivalent employees for the years ended December 31, 2000, 1999 and 1998 were 1,313, 1,168, and 1,080, respectively.

Occupancy expense rose \$1.9 million to \$18.0 million in 2000. Major categories included within occupancy expense are building lease expense, depreciation expense, and maintenance contract expense. Building lease expense increased to \$4.7 million in 2000 from \$3.9 million in 1999, an increase of \$735,000 or 19%. The Company continues to increase the rentable square feet of the Galleria corporate location to accommodate the increases in personnel. In addition, the Company leased 91,689 square feet for an operations center in downtown Houston. Depreciation expense increased \$249,000 to \$8.0 million for the year ended December 31, 2000. This increase was due primarily to depreciation on equipment provided to new employees and expense related to technology upgrades throughout the Company. Maintenance contract expense for the year ended December 31, 2000 was \$2.5 million, an increase of \$678,000 or 38% compared to \$1.8 million in 1999 and \$1.5 million in 1998. The Company has purchased maintenance contracts for major operating systems throughout the organization.

During 2000 and 1999, the Company recorded, on a pre-tax basis, approximately \$4.1 million and \$4.5 million, respectively in merger-related expenses and other charges including investment banking fees, other professional fees and severance expenses associated with the merger of Citizens in 2000 and Fort Bend in 1999.

Income Taxes

Income tax expense includes the regular federal income tax at the statutory rate, plus the income tax component of the Texas franchise tax. The amount of federal income tax expense is influenced by the amount of taxable income, the amount of tax-exempt income, the amount of nondeductible interest expense, and the amount of other nondeductible

expenses. Taxable income for the income tax component of the Texas franchise tax is the federal pre-tax income, plus certain officers salaries, less interest income from federal securities. In 2000 income tax expense was \$22.6 million, an increase of \$5.1 million or 29% from the \$17.5 million of income tax expense in 1999 and an increase of \$1.7 million or 11% from the \$15.8 million of income tax expense in 1998.

Impact of Inflation

The effects of inflation on the local economy and on the Company's operating results have been relatively modest for the past several years. Since substantially all of the Company's assets and liabilities are monetary in nature, such as cash, securities, loans and deposits, their values are less sensitive to the effects of inflation than to changing interest rates, which do not necessarily change in accordance with inflation rates. The Company attempts to control the impact of interest rate fluctuations by managing the relationship between its interest rate sensitive assets and liabilities. See " — Financial Condition — Interest Rate Sensitivity and Liquidity" below.

Financial Condition

Loans Held for Investment

Loans held for investment were \$2.43 billion at December 31, 2000, an increase of \$467.2 million, or 24% from December 31, 1999. Loans were \$1.96 billion at December 31, 1999, an increase of \$340.7 million, or 21%, from \$1.62 billion at December 31, 1998.

During the past 5 years loans have grown at an annualized rate of 20%. This growth is consistent with the Company's strategy of targeting corporate "middle market" and private banking customers and providing innovative products with superior customer service. This plan also includes establishing new branches in areas that demographically complement existing or targeted customer base, pursuing selected mergers/acquisitions which will add new markets, delivery systems and talent to the Company and leveraging new or existing technology to improve the profitability of the Company and its customers.

The following table summarizes the loan portfolio of the Company by major category as of the dates indicated:

	Year Ended December 31,									
	2000		1999		1998		1997		1996	
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent
(Dollars in thousands)										
Commercial and industrial	\$ 954,912	39.37%	\$ 749,816	38.29%	\$ 667,918	41.29%	\$ 474,799	38.34%	\$347,193	36.27%
Real estate:										
Construction & land development	641,128	26.43	500,547	25.57	299,220	18.50	179,769	14.52	122,491	12.79
1-4 family residential	335,934	13.85	290,057	14.81	273,387	16.90	257,892	20.83	219,792	22.96
Commercial owner occupied	265,534	10.95	212,371	10.84	187,093	11.57	158,409	12.79	123,530	12.90
Farmland	5,753	0.24	13,218	0.67	8,416	0.52	8,384	0.68	8,879	0.93
Other	31,861	1.31	20,572	1.05	17,524	1.08	10,854	0.87	6,562	0.69
Consumer	190,376	7.85	171,714	8.77	164,018	10.14	148,210	11.97	128,881	13.46
Loans held for investment	\$2,425,498	100.00%	\$1,958,295	100.00%	\$1,617,576	100.00%	\$1,238,317	100.00%	\$957,328	100.00%

The primary lending focus of the Company is on small- and medium-sized commercial, construction and land development, residential mortgage and consumer loans. The Company offers a variety of commercial lending products including term loans, lines of credit and equipment financing. A broad range of short- to medium-term commercial loans, both collateralized and uncollateralized, are made available to businesses for working capital (including inventory and receivables), business expansion (including acquisitions of real estate and improvements) and the purchase of equipment and machinery. The purpose of a particular loan generally determines its structure.

Generally, the Company's commercial loans are underwritten in the Company's primary market area on the basis of the borrower's ability to service such debt from cash flow. As a general practice, the Company takes as collateral a lien on any available real estate, equipment or other assets. Working capital loans are primarily collateralized by short-term assets whereas term loans are primarily collateralized by long-term assets.

A substantial portion of the Company's real estate loans consists of loans collateralized by real estate and other assets of commercial customers. Additionally, a portion of the Company's lending activity consists of the origination of single-family residential mortgage loans collateralized by owner-occupied properties located in the Company's primary market area. The Company offers a variety of mortgage loan products which generally are amortized over five to 30 years.

Loans collateralized by single-family residential real estate generally have been originated in amounts of no more than 90% of appraised value. The Company requires mortgage title insurance and hazard insurance in the amount of the loan. Although the contractual loan payment periods for single-family residential real estate loans are generally for a 15 to 30 year period, such loans often remain outstanding for significantly shorter periods than their contractual terms.

The Company originates and purchases residential and commercial mortgage loans to sell to investors with servicing rights retained. The Company also provides residential and commercial construction financing to builders and developers and acts as a broker in the origination of multi-family and commercial real estate loans.

Residential construction financing to builders generally has been originated in amounts of no more than 80% of appraised value. The Company requires a mortgage title binder and builder's risk insurance in the amount of the loan. The contractual loan payment periods for residential constructions loans are generally for a six to twelve month period.

Consumer loans made by the Company include automobile loans, recreational vehicle loans, boat loans, home improvement loans, personal loans (collateralized and uncollateralized) and deposit account collateralized loans. The terms of these loans typically range from 12 to 84 months and vary based upon the nature of collateral and size of loan.

The contractual maturity ranges of the commercial and industrial and real estate construction loan portfolio and the amount of such loans with fixed interest rates and floating rates in each maturity range as of December 31, 2000 are summarized in the following table:

	December 31, 2000			
	One Year or Less	After One Through Five Years	After Five Years	Total
	(Dollars in thousands)			
Commercial and industrial	\$ 632,033	\$290,874	\$32,005	\$ 954,912
Real estate construction and land development	399,978	210,417	30,733	641,128
Total	<u>\$1,032,011</u>	<u>\$501,291</u>	<u>\$62,738</u>	<u>\$1,596,040</u>
Loans with a fixed interest rate	\$ 367,576	\$165,711	\$24,361	\$ 557,648
Loans with a floating interest rate	664,435	335,580	38,377	1,038,392
Total	<u>\$1,032,011</u>	<u>\$501,291</u>	<u>\$62,738</u>	<u>\$1,596,040</u>

Loans Held for Sale

Loans held for sale of \$85.9 million at December 31, 2000 increased from \$77.0 million at December 31, 1999. These loans are typically sold to investors within one year of origination.

Loan Review and Allowance for Loan Losses

The Company's loan review procedures include a Credit Quality Assurance Process that begins with approval of lending policies and underwriting guidelines by the Board of Directors, an independent loan review department staffed with OCC experienced personnel, low individual lending limits for officers, Senior Loan Committee approval for large credit relationships and quality loan documentation procedures. The Company also maintains a well developed

monitoring process for credit extensions in excess of \$100,000. The Company performs monthly and quarterly concentration analyses based on various factors such as industries, collateral types, business lines, large credit sizes, international investments and officer portfolio loads. The Company has established underwriting guidelines to be followed by its officers. The Company also monitors its delinquency levels for any negative or adverse trends. There can be no assurance, however, that the Company's loan portfolio will not become subject to increasing pressures from deteriorating borrower credit due to general economic conditions.

Historically, the Houston metropolitan area has been affected by the state of the energy business, but since the mid 1980's the economic impact has been reduced by a combination of increased industry diversification and less reliance on debt to finance expansion. When energy prices fluctuate, it is the Company's practice to review and adjust underwriting standards with respect to companies affected by oil and gas price volatility, and to continuously monitor existing credit exposure to companies which are impacted by this price volatility.

The allowance for loan losses is established through charges to earnings in the form of a provision for loan losses. Based on an evaluation of the loan portfolio, management presents a quarterly analysis of the allowance for loan losses to the Board of Directors, indicating any changes in the allowance since the last review and any recommendations as to adjustments in the allowance. In making its evaluation, management considers, among other things, growth in the loan portfolio, the diversification by industry of the Company's commercial loan portfolio, the effect of changes in the local real estate market on collateral values, the results of recent regulatory examinations, the effects on the loan portfolio of current economic indicators and their probable impact on borrowers, the amount of charge-offs for the period, the amount of nonperforming loans and related collateral security and the evaluation of its loan portfolio by the loan review function. Charge-offs occur when loans are deemed to be uncollectible.

In order to determine the adequacy of the allowance for loan losses, management considers the risk classification or delinquency status of loans and other factors, such as collateral value, portfolio composition, trends in economic conditions and the financial strength of borrowers. Management establishes specific allowances for loans which management believes require reserves greater than those allocated according to their classification or delinquent status. The Company then charges a provision for loan losses to operations determined on an annualized basis to maintain the allowance for loan losses at an adequate level determined according to the foregoing methodology.

Management believes that the allowance for loan losses at December 31, 2000 is adequate to cover losses inherent in the portfolio as of such date. There can be no assurance, however, that the Company will not sustain losses in future periods, which could be greater than the size of the allowance at December 31, 2000.

The following table presents, for the periods indicated, an analysis of the allowance for loan losses and other related data:

	Years Ended December 31,				
	2000	1999	1998	1997	1996
	(Dollars in thousands)				
Allowance for loan losses, beginning balance	\$22,436	\$17,532	\$14,385	\$ 11,488	\$ 9,662
Provision charged against operations	7,053	6,474	4,261	4,242	2,482
Charge-offs	(2,093)	(2,211)	(1,506)	(1,679)	(2,197)
Recoveries	754	641	374	334	806
Increase from acquisition	—	—	—	—	735
Adjustment to conform reporting periods	—	—	18	—	—
Allowance for loan losses, ending balance	\$28,150	\$22,436	\$17,532	\$ 14,385	\$ 11,488
Allowance to period-end loans	1.16%	1.15%	1.08%	1.16%	1.20%
Net charge-offs to average loans	0.06%	0.09%	0.08%	0.12%	0.17%
Allowance to period-end nonperforming loans	297.82%	519.59%	441.39%	312.38%	391.68%

The following table describes the allocation of the allowance for loan losses among various categories of loans and certain other information for the dates indicated. Portions of the allowance for loan losses are allocated to cover the estimated losses inherent in particular risk categories of loans. The allocation of the allowance for loan losses is based upon the Company's loss experience over a period of years and is adjusted for subjective factors such as economic trends, performance trends, portfolio age and concentrations of credit. Prior year allocations have been restated to conform to this methodology. The allocation is made for analytical purposes and is not necessarily indicative of the categories in which future loan losses may occur. The total allowance is available to absorb losses from any segment of loans.

	December 31,		December 31,		December 31,	
	2000		1999		1998	
	Amount	Percent of Loans to Total Loans	Amount	Percent of Loans to Total Loans	Amount	Percent of Loans to Total Loans
(Dollars in thousands)						
Balance of allowance for loan losses applicable to:						
Commercial and industrial	\$12,219	39.37%	\$10,793	38.29%	\$ 8,219	41.29%
Real estate:						
Construction and land development	5,733	26.43	4,184	25.57	2,418	18.50
1-4 family residential	3,294	13.85	2,498	14.81	2,424	16.90
Commercial owner occupied	2,676	10.95	1,962	10.84	1,767	11.57
Farmland	40	0.24	93	0.67	66	0.52
Other	1,253	1.31	143	1.05	134	1.08
Consumer	2,935	7.85	2,763	8.77	2,504	10.14
Total allowance for loan losses	\$28,150	100.00%	\$22,436	100.00%	\$17,532	100.00%

	December 31,		December 31,	
	1997		1996	
	Amount	Percent of Loans to Total Loans	Amount	Percent of Loans to Total Loans
(Dollars in thousands)				
Balance of allowance for loan losses applicable to:				
Commercial and industrial	\$ 5,958	38.34%	\$ 4,141	36.27%
Real estate:				
Construction and land development	1,664	14.52	1,283	12.79
1-4 family residential	2,546	20.83	2,340	22.96
Commercial owner occupied	1,717	12.79	1,528	12.90
Farmland	72	0.68	82	0.93
Other	93	0.87	63	0.69
Consumer	2,335	11.97	2,051	13.46
Total allowance for loan losses	\$14,385	100.00%	\$11,488	100.00%

Nonperforming Assets and Impaired Loans

The Company generally places a loan on nonaccrual status and ceases accruing interest when loan payment performance is deemed unsatisfactory. All loans past due 90 days are placed on nonaccrual status, unless the loan is both well collateralized and in the process of collection. Cash payments received while a loan is classified as nonaccrual are recorded as a reduction of principal as long as doubt exists as to collection. The Company is sometimes required to revise a loan's interest rate or repayment terms in a troubled debt restructuring.

Nonperforming assets were \$9.9 million at December 31, 2000, compared with \$6.2 million at December 31, 1999 and \$5.1 million at December 31, 1998. This resulted in a ratio of nonperforming assets to loans plus other real estate of 0.41%, 0.31%, and 0.31% for the years ended 2000, 1999, and 1998, respectively. Nonaccrual loans, the largest component of nonperforming assets, were \$8.3 million at December 31, 2000, an increase of \$5.8 million from \$2.5 million at December 31, 1999. This increase is primarily due to the addition of two loans — a \$5.1 million secured relationship which is expected to be a long term workout and a \$1.1 million loan secured by three houses which are expected to be sold in the near term.

The following table presents information regarding nonperforming assets as of the dates indicated:

	December 31,				
	2000	1999	1998	1997	1996
	(Dollars in thousands)				
Nonaccrual loans	\$ 8,345	\$2,471	\$2,369	\$3,324	\$2,214
Accruing loans 90 or more days past due	1,107	1,847	1,352	734	314
Restructured loans	—	—	251	547	405
Other real estate and foreclosed property	454	1,840	1,099	1,651	1,991
Total non-performing assets	\$ 9,906	\$6,158	\$5,071	\$6,256	\$4,924
Nonperforming assets to total loans and other real estate	0.41%	0.31%	0.31%	0.50%	0.51%

The Company regularly updates appraisals on loans collateralized by real estate, particularly those categorized as nonperforming loans and potential problem loans. In instances where updated appraisals reflect reduced collateral values, an evaluation of the borrower's overall financial condition is made to determine the need, if any, for possible writedowns or appropriate additions to the allowance for loan losses.

A loan is considered impaired when, based upon current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal and interest when due according to the contractual terms of the loan agreement. The Company's impaired loans were approximately \$10.8 million and \$13.7 million at December 31, 2000 and 1999, respectively. At December 31, 1999, the largest component of impaired loans was a commercial energy related loan of approximately \$10.8 million. This loan was not considered impaired at December 31, 2000 as a result of payments in accordance with terms for a period of at least twelve months. The decrease in the impaired loan balance associated with this loan was partially offset by the addition of two loans with a principal balance of \$6.2 million included in nonaccrual loans and discussed above. The average recorded investment in impaired loans during 2000, 1999 and 1998 was \$9.3 million, \$13.9 million and \$6.3 million, respectively. The total required allowance for loan losses related to these loans was \$1.0 million for 2000 and \$0 for 1999. Interest income on impaired loans of \$1.1 million, \$1.5 million and \$415,000 was recognized for cash payments received in 2000, 1999 and 1998, respectively.

The Bank is not committed to lend additional funds to debtors whose loans have been modified.

Securities

At the date of purchase, the Company classifies debt and equity securities into one of three categories: held to maturity, trading or available for sale. At each reporting date, the appropriateness of the classification is reassessed. Investments in debt securities classified as held to maturity are stated at cost, increased by accretion of discounts and reduced by amortization of premiums, both computed by the interest method. Management has the positive intent and ability to hold those securities to maturity. Securities that are bought and held principally for the purpose of selling them in the near term are classified as trading and measured at fair value in the financial statements with unrealized gains and losses included in earnings. Securities not classified as either held to maturity or trading are classified as available for sale and measured at fair value in the financial statements with unrealized gains and losses reported, net of tax, as a component of accumulated other comprehensive income (loss) until realized. Gains and losses on sales of securities are determined using the specific-identification method. The Company has classified all securities as available for sale at December 31, 2000. This allows the Company to manage its investment portfolio more effectively and to enhance the average yield on the portfolio.

The amortized cost of securities classified as available for sale and held to maturity is as follows:

	December 31,				
	2000	1999	1998	1997	1996
	(Dollars in thousands)				
Available for sale:					
U.S. Government securities	\$169,069	\$134,001	\$183,602	\$201,300	\$168,132
Mortgage-backed securities	618,523	678,523	623,964	473,523	330,923
Federal Reserve Bank stock	3,949	2,981	2,442	2,271	1,190
Federal Home Loan Bank stock	17,972	16,051	8,775	40,813	42,603
Other securities	43,411	24,307	10,141	33,545	16,154
Total securities available for sale	\$852,924	\$855,863	\$828,924	\$751,452	\$559,002
Held to maturity:					
U.S. Government securities	\$ —	\$ 12,761	\$ 23,837	\$ 26,247	\$ 17,493
Mortgage-backed securities	—	29,164	80,528	7,818	2,795
Other securities	—	17,019	13,964	100,444	118,544
Total securities held to maturity	\$ —	\$ 58,944	\$118,329	\$134,509	\$138,832

The following table presents the amortized cost of securities classified as held to maturity and available for sale and their approximate fair values as of the dates shown:

	December 31, 2000				December 31, 1999				December 31, 1998			
	Amortized Cost	Gross Gain	Unrealized Loss	Fair Value	Amortized Cost	Gross Gain	Unrealized Loss	Fair Value	Amortized Cost	Gross Gain	Unrealized Loss	Fair Value
	(Dollars in thousands)											
Available for sale:												
U.S. Government securities	\$169,069	\$1,080	\$ (819)	\$169,330	\$134,001	\$ 35	\$ (3,499)	\$ 130,537	\$183,602	\$1,878	\$ (25)	\$185,455
Mortgage-backed securities	618,523	2,088	(7,395)	613,216	678,523	470	(21,338)	657,655	623,964	5,294	(2,811)	626,447
Federal Reserve Bank stock	3,949	—	—	3,949	2,981	—	—	2,981	2,442	—	—	2,442
Federal Home Loan Bank stock	17,972	—	—	17,972	16,051	—	—	16,051	8,775	—	—	8,775
Other securities	43,411	335	(49)	43,697	24,307	77	(183)	24,201	10,141	219	(23)	10,337
Total securities available for sale	\$852,924	\$3,503	\$ (8,263)	\$848,164	\$855,863	\$ 582	\$ (25,020)	\$ 831,425	\$828,924	\$7,391	\$ (2,859)	\$833,456
Held to maturity:												
U.S. Government securities	\$ —	\$ —	\$ —	\$ —	\$ 12,761	\$ 1	\$ (287)	\$ 12,475	\$ 23,837	\$ 102	\$ (230)	\$ 23,709
Mortgage-backed securities	—	—	—	—	29,164	3	(612)	28,555	80,528	718	(298)	80,948
Other securities	—	—	—	—	17,019	28	(136)	16,911	13,964	258	—	14,222
Total securities held to maturity	\$ —	\$ —	\$ —	\$ —	\$ 58,944	\$ 32	\$ (1,035)	\$ 57,941	\$118,329	\$1,078	\$ (528)	\$118,879

In connection with the Citizens merger, the Company transferred all of Citizens' held to maturity debt securities to the available for sale category in 2000. The amortized cost of these securities at the time of transfer was \$55.8 million and the unrealized gain was \$267,000 (\$174,000 net of income taxes). In connection with the Fort Bend merger, the Company transferred all of Fort Bend's held to maturity debt securities to the available for sale category in 1999. The amortized cost of these securities at the time of transfer was \$57.8 million and the unrealized gain was \$80,000 (\$52,000 net of income taxes). The Company does not intend to sell these securities in the near term.

Securities totaled \$848.2 million at December 31, 2000, a decrease of \$42.2 million from \$890.4 million at December 31, 1999. During 1999, securities decreased \$61.4 million from \$951.8 million at December 31, 1998. The yield on the securities portfolio for 2000 was 6.35% while the yield was 6.08% in 1999.

The Company has no mortgage-backed securities that have been issued by non-agency entities. Included in the Company's mortgage-backed securities at December 31, 2000 were agency issued collateral mortgage obligations with a book value of \$300.7 million and a fair market value of \$296.6 million.

At December 31, 2000, \$427.2 million of the mortgage-backed securities held by the Company had final maturities of more than 10 years. At December 31, 2000, approximately \$104.4 million of the Company's mortgage-backed securities earned interest at floating rates and repriced within one year, and accordingly, were less susceptible to declines in value should interest rates increase.

The following table summarizes the contractual maturity of investments and their weighted average yields at December 31, 2000. The yield on the securities portfolio is based on average historical cost balances and does not give effect to changes in fair value that are reflected as a separate component of other comprehensive income.

December 31, 2000										
	Within One Year		After One Year But Within Five Years		After Five Years But Within Ten Years		After Ten Years			
	Amortized Cost	Yield	Amortized Cost	Yield	Amortized Cost	Yield	Amortized Cost	Yield	Total	Yield
(Dollars in thousands)										
U.S. Government securities	\$ 29,654	6.03%	\$132,932	6.29%	\$ 6,483	6.11%	\$ —	%	\$169,069	6.23%
Mortgage-backed securities	6,742	6.07	94,720	6.32	89,831	6.00	427,230	6.61	618,523	6.47
Federal Reserve Bank stock	3,949	6.00	—	—	—	—	—	—	3,949	6.00
Federal Home Loan Bank stock	17,972	6.70	—	—	—	—	—	—	17,972	6.70
Other securities	5,793	5.30	20,564	6.13	6,437	4.97	10,617	7.53	43,411	6.19
Federal funds sold	76,527	6.47	—	—	—	—	—	—	76,527	6.47
Interest-bearing deposits	2,814	6.63	—	—	—	—	—	—	2,814	6.63
Total investments	\$143,451	6.33%	\$248,216	6.29%	\$102,751	5.94%	\$437,847	6.64%	\$932,265	6.42%

Other Assets

Other assets were \$117.8 million at December 31, 2000, an increase of \$24.1 million from \$93.7 million at December 31, 1999. This increase is primarily attributable to increases in factored receivables, increases in mortgage servicing rights and on the increase in the cash value of Bank-owned life insurance policies. Cash value of bank-owned life insurance policies was approximately \$28.7 million at December 31, 2000 compared with a balance of \$27.2 million at December 31, 1999. This increase resulted from interest earned on these policies.

Factored receivables result from providing operating funds to businesses by converting their accounts receivable to cash. During 2000 factored receivables increased \$9.0 million to \$27.5 million. This increase was due to several factors including new officers hired and aggressive marketing, both internally and externally.

Capitalized mortgage servicing rights were \$12.3 million at December 31, 2000, an increase of \$5.6 million from \$6.7 million at December 31, 1999. This increase was due to Mitchell's purchase of \$5.5 million of mortgage servicing rights during the year.

Deposits

The Company offers a variety of deposit accounts having a wide range of interest rates and terms. The Company's deposits consist of demand, savings, NOW accounts, money market and time accounts. The Company relies primarily on customer service, advertising, and competitive pricing policies to attract and retain these deposits. As of December 31, 2000, the Company had less than two percent of its deposits classified as brokered funds and does not anticipate any significant increase. Deposits provide the majority of the funding for the Company's lending and investment activities, and the interest paid for deposits must be managed carefully to control the level of interest expense.

The Company's ratio of average demand deposits to average total deposits for the years ended December 31, 2000, 1999, and 1998 was 29.50%, 30.47%, and 30.67%, respectively.

Average total deposits during 2000 increased to \$2.82 billion from \$2.38 billion in 1999, an increase of \$437.6 million or 18%. Average noninterest-bearing deposits increased to \$774.1 million in 2000 from \$656.4 million in 1999 due to an increase in the number of deposit accounts. Average deposits in 1999 rose to \$2.38 billion from \$2.15 billion in 1998, an increase of \$230.9 million or 11%.

The average daily balances and weighted average rates paid on deposits for each of the years ended December 31, 2000, 1999, and 1998 are presented below:

	Years Ended December 31,					
	2000		1999		1998	
	Amount	Rate	Amount	Rate	Amount	Rate
(Dollars in thousands)						
NOW accounts	\$ 58,093	1.09%	\$ 69,859	1.63%	\$ 86,438	0.92%
Regular savings	74,380	2.28	70,308	2.28	68,621	1.22
Premium yield	659,979	5.25	471,523	4.25	414,841	5.59
Money market savings	425,414	3.16	397,290	3.02	364,498	2.80
CD's less than \$100,000	289,183	5.32	284,767	4.73	254,151	3.91
CD's \$100,000 and over	464,470	6.17	370,513	5.04	316,184	6.43
IRA's, QRP's and other	75,394	5.66	62,757	5.16	74,145	4.24
Total interest-bearing deposits	2,046,913	4.82%	1,727,017	4.06%	1,578,878	4.34%
Non interest-bearing deposits	774,111		656,428		573,708	
Total deposits	\$2,821,024		\$2,383,445		\$2,152,586	

The following table sets forth the maturity of the Company's time deposits that are \$100,000 or greater as of the dates indicated:

	December 31,		
	2000	1999	1998
(Dollars in thousands)			
3 months or less	\$265,232	\$186,970	\$226,353
Between 3 months and 6 months	124,144	75,389	60,652
Between 6 months and 1 year	61,774	77,604	53,506
Over 1 year	55,479	27,088	28,325
Total time deposits \$100,000 and over	\$506,629	\$367,051	\$368,836

Borrowings

Securities sold under repurchase agreements and other borrowings, consisting of federal funds purchased and treasury, tax, and loan deposits, generally represent borrowings with maturities ranging from one to thirty days. Information relating to these borrowings is summarized as follows:

	December 31,	
	2000	1999
	(Dollars in thousands)	
Securities sold under repurchase agreements:		
Average	\$209,816	\$184,358
Period-end	211,800	216,838
Maximum month-end balance during period	241,834	216,838
Interest Rate:		
Average	4.69%	4.06%
Period-end	4.89%	4.03%
Other borrowings:		
Average	\$205,213	\$196,694
Period-end	305,961	267,140
Maximum month-end balance during period	380,121	284,455
Interest rate:		
Average	6.39%	5.39%
Period-end	6.83%	5.27%

Securities sold under repurchase agreements are maintained in safekeeping by correspondent banks.

Interest Rate Sensitivity and Liquidity

Asset and liability management is concerned with the timing and magnitude of repricing assets compared to liabilities. It is the objective of the Company to generate stable growth in net interest income and to attempt to control risks associated with interest rate movements. In general, management's strategy is to reduce the impact of changes in interest rates on its net interest income by maintaining a favorable match between the maturities or repricing dates of its interest-earning assets and interest-bearing liabilities. The Company adjusts its interest sensitivity during the year through changes in the mix of assets and liabilities and may use interest rate products such as interest rate swap and cap agreements. The Company did not utilize derivative financial instruments to manage interest rate risk during the years ended December 31, 2000 and 1999. The Company's asset and liability management strategy is formulated and monitored by the Asset Liability Committee, which is composed of senior officers of the Bank and three outside directors, in accordance with policies approved by the Bank's Board of Directors. This Committee meets regularly to review, among other things, the sensitivity of the Bank's assets and liabilities to interest rate changes, the book and market values of assets and liabilities, unrealized gains and losses, purchase and sale activity, and maturities of investments and borrowings. The Asset Liability Committee also approves and establishes pricing and funding decisions with respect to the Bank's overall asset and liability composition. The Committee reviews the Bank's liquidity, cash flow flexibility, maturities of investments, deposits and borrowings, retail and institutional deposit activity, current market conditions, and interest rates on both a local and national level.

To effectively measure and manage interest rate risk, the Company uses simulation analysis to determine the impact on net interest income of changes in interest rates under various interest rate scenarios, balance sheet trends, and strategies. From these simulations, interest rate risk is quantified and appropriate strategies are developed and implemented.

The following table presents an analysis of the sensitivity inherent in the Company's net interest income and market value of portfolio equity. The interest rate scenarios presented in the table include interest rates at December 31, 2000 and 1999 and as adjusted by instantaneous rate changes upward and downward of up to 200 basis points. Each rate scenario reflects unique prepayment and repricing assumptions. Since there are limitations inherent in any methodology used to estimate the exposure to changes in market interest rates, this analysis is not intended to be a forecast of the actual effect of a change in market interest rates on the Company. The market value sensitivity analysis presented includes assumptions that (i) the composition of the Company's interest sensitive assets and liabilities existing at year end will remain constant over the twelve month measurement period; and (ii) that changes in market rates are parallel and instantaneous across the yield curve regardless of duration or repricing characteristics of specific assets or liabilities. Further, the analysis does not contemplate any actions that the Company might undertake in response to changes in market interest rates. Accordingly, this analysis is not intended and does not provide a precise forecast of the effect actual changes in market rates will have on the Company.

	Changes in Interest Rates				
	-200	-100	0	+100	+200
Impact on net interest income:					
December 31, 2000	-9.84%	-4.11%	0.00%	2.79%	6.54%
December 31, 1999	-7.12%	-2.54%	0.00%	2.88%	5.66%
Impact on market value of portfolio equity:					
December 31, 2000	-3.93%	-0.48%	0.00%	-1.68%	-3.94%
December 31, 1999	-0.59%	1.29%	0.00%	-1.80%	-3.41%

The interest rate sensitivity ("GAP") is defined as the difference between interest-earning assets and interest-bearing liabilities maturing or repricing within a given time period. A GAP is considered positive when the amount of interest rate sensitive assets exceeds the amount of interest rate sensitive liabilities. A GAP is considered negative when the amount of interest rate sensitive liabilities exceeds interest rate sensitive assets. During a period of rising interest rates, a negative GAP would tend to adversely affect net interest income, while a positive GAP would tend to result in an increase in net interest income. During a period of falling interest rates, a negative GAP would tend to result in an increase in net interest income, while a positive GAP would tend to affect net interest income adversely. While the GAP is a useful measurement and contributes toward effective asset and liability management, it is difficult to predict the effect of changing interest rates solely on that measure. Because different types of assets and liabilities with the same or similar maturities may react differently to changes in overall market rates or conditions, changes in interest rates may affect net interest income positively or negatively even if an institution were perfectly matched in each maturity category.

The Company's one-year cumulative GAP position at December 31, 2000 was positive \$109.9 million or 2.77% of assets. This is a one-day position that is continually changing and is not indicative of the Company's position at any other time. While the GAP position is a useful tool in measuring interest rate risk and contributes toward effective asset and liability management, shortcomings are inherent in GAP analysis since certain assets and liabilities may not move proportionally as interest rates change.

The following table sets forth an interest rate sensitivity analysis for the Company as of December 31, 2000:

	0-90 days	91-360 days	One to Three years	After Three years	Total
Interest-earning assets:					
Money market funds	\$ 2,272	\$ —	\$ —	\$ —	\$ 2,272
Securities	153,907	171,762	301,687	270,470	897,826
Loans	1,656,744	249,997	341,529	225,087	2,473,357
Overdrafts	8,439	—	—	—	8,439
Federal funds sold	50,985	—	—	—	50,985
Total interest-earning assets	1,872,347	421,759	643,216	495,557	3,432,879
Interest-bearing liabilities:					
Demand, money market and savings deposits	501,608	437,402	423,111	26,922	1,389,043
Certificates of deposit and other time deposits	351,547	364,792	181,886	27,743	925,968
Short-term borrowings	528,780	38	108	3,253	532,179
Long-term borrowings	—	—	—	—	—
Total interest-bearing liabilities	1,381,935	802,232	605,105	57,918	2,847,190
Period GAP	\$ 490,412	\$ (380,473)	\$ 38,111	\$437,639	\$ 585,689
Cumulative GAP	\$ 490,412	\$ 109,939	\$148,050	\$585,689	
Period GAP to total assets	12.36%	−9.59%	0.96%	11.03%	
Cumulative GAP to total assets	12.36%	2.77%	3.73%	14.76%	

Since December 31, 2000, market interest rates have declined as a result of the Federal Reserve's 100 basis point reduction in the prime rate. This decline in interest rates has adversely impacted the Company's net interest margin in 2001 as a result of its short term position GAP. While additional reductions in interest rates may be expected, the Company believes that its ability to manage its interest rate sensitivity will minimize the potential adverse impact on net interest income for the year 2001. For information on the Company's results of operations for the month of January 2001, see "Item 8 — Financial Statements and Supplementary Data" on pages 33-34.

Liquidity involves the Company's ability to raise funds to support asset growth or reduce assets to meet deposit withdrawals and other payment obligations, to maintain reserve requirements and otherwise to operate the Company on an ongoing basis. For the year ended December 31, 2000, the Company's liquidity needs have primarily been met by growth in core deposits, and increases in short-term borrowings, primarily from the Federal Home Loan Bank. The cash and federal funds sold position, supplemented by amortizing securities and loan portfolios, have generally created an adequate liquidity position and are expected to do so in 2001.

Subject to certain limitations, the Bank may borrow funds from the Federal Home Loan Bank ("FHLB") in the form of advances. Credit availability from the FHLB to the Bank is based on the Bank's financial and operating condition. Borrowings from the FHLB to the Bank were approximately \$193.4 million at December 31, 2000. In addition to creditworthiness, the Bank must own a minimum amount of FHLB capital stock. This minimum is 5.00% of outstanding FHLB advances. Unused borrowing capacity at December 31, 2000 was approximately \$293.2 million. The Bank uses FHLB advances for both long-term and short-term liquidity needs. Other than normal banking operations, the Bank has no long-term liquidity needs. The Bank has never been involved with highly leveraged transactions that may cause unusual potential long-term liquidity needs.

Capital Resources

Shareholders' equity increased to \$298.1 million at December 31, 2000 from \$233.1 million at December 31, 1999, an increase of \$65.0 million, or 28%.

Capital management consists of providing equity to support both current and future operations. The Company is subject to capital adequacy requirements imposed by the Federal Reserve Board and the Bank is subject to capital

adequacy requirements imposed by the OCC. Both the Federal Reserve Board and the OCC have adopted risk-based capital requirements for assessing bank holding company and bank capital adequacy. These standards define capital and establish minimum capital requirements in relation to assets and off-balance sheet exposure, adjusted for credit risk. The risk-based capital standards currently in effect are designed to make regulatory capital requirements more sensitive to differences in risk profiles among bank holding companies and banks, to account for off-balance sheet exposure and to minimize disincentives for holding liquid assets. Assets and off-balance sheet items are assigned to broad risk categories, each with appropriate relative risk weights. The resulting capital ratios represent capital as a percentage of total risk-weighted assets and off-balance sheet items.

Bank regulatory authorities in the United States have issued risk-based capital standards by which all bank holding companies and banks are evaluated in terms of capital adequacy. The risk-based capital standards issued by the Federal Reserve Board apply to the Company, and the OCC guidelines apply to the Bank. These guidelines relate a financial institution's capital to the risk profile of its assets. The risk-based capital standards require all financial organizations to have "Tier 1 capital" of at least 4.0% of risk-adjusted assets and "total risk-based" capital (Tier 1 and Tier 2) of at least 8.0% of risk-adjusted assets. "Tier 1 capital" includes, generally, common shareholders' equity and qualifying perpetual preferred stock together with related surpluses and retained earnings, qualifying perpetual preferred stock and minority interest in equity accounts of consolidated subsidiaries less deductions for goodwill and various other intangibles. "Tier 2 capital" may consist of a limited amount of subordinated debt, certain hybrid capital instruments and other debt securities, preferred stock not qualifying as Tier 1 capital, and a limited amount of the general valuation allowance for loan losses. The sum of Tier 1 capital and Tier 2 capital is "total risk-based capital."

The agencies have also adopted guidelines which supplement the risk-based capital guidelines with a minimum leverage ratio of Tier 1 capital to average total consolidated assets ("leverage ratio") of 3.0% for institutions with well diversified risk, including no undue interest rate exposure; excellent asset quality; high liquidity; good earnings; and that are generally considered to be strong banking organizations, rated composite 1 under applicable federal guidelines, and that are not experiencing or anticipating significant growth. Other banking organizations are required to maintain a leverage ratio of at least 4.0% to 5.0%. These rules further provide that banking organizations experiencing internal growth or making acquisitions will be expected to maintain capital positions substantially above the minimum supervisory levels and comparable to peer group averages, without significant reliance on intangible assets.

The following table compares the Company's and the Bank's leverage and risk-weighted capital ratios as of December 31, 2000 and 1999 to the minimum regulatory standards:

	Actual		Minimum Capital Requirement		Minimum To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
(Dollars in thousands)						
As of December 31, 2000						
Total Capital (to Risk Weighted Assets):						
The Company	\$318,039	10.49%	\$242,590	8.00%	\$303,238	10.00%
The Bank	332,092	11.03%	240,954	8.00%	301,193	10.00%
Tier I Capital (to Risk Weighted Assets):						
The Company	289,889	9.56%	121,295	4.00%	242,590	8.00%
The Bank	303,616	10.08%	120,477	4.00%	240,954	8.00%
Tier I Capital (to Average Assets):						
The Company	289,889	7.71%	112,867	3.00%	188,111	5.00%
The Bank	303,616	8.12%	112,199	3.00%	186,998	5.00%
As of December 31, 1999						
Total Capital (to Risk Weighted Assets):						
The Company	267,837	10.61%	201,968	8.00%	252,460	10.00%
The Bank	270,426	10.71%	201,956	8.00%	252,445	10.00%
Tier I Capital (to Risk Weighted Assets):						
The Company	245,401	9.72%	100,984	4.00%	201,968	8.00%
The Bank	248,485	9.84%	100,978	4.00%	201,956	8.00%
Tier I Capital (to Average Assets):						
The Company	245,401	7.81%	94,208	3.00%	157,013	5.00%
The Bank	248,485	7.88%	94,606	3.00%	157,677	5.00%

Pursuant to Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA"), each federal banking agency revised its risk-based capital standards to ensure that those standards take adequate account of interest rate risk, concentration of credit risk and the risks of nontraditional activities, as well as reflect the actual performance and expected risk of loss on multifamily mortgages. Also pursuant to FDICIA, each federal banking agency has promulgated regulations setting the levels at which an insured institution would be considered "well capitalized," "adequately capitalized," "undercapitalized," "significantly undercapitalized" and "critically undercapitalized." Under the Federal Reserve Board's regulations, the Bank is classified as "well capitalized" for purposes of prompt corrective action. See "Supervision and Regulation."

Other Matters

In June 1998, Statement of Financial Accounting Standards (SFAS) No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended, was issued by the Financial Accounting Standards Board to establish accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. SFAS No. 133 requires that an entity recognize those instruments at fair value. If certain conditions are met, a derivative may be specifically designated as (a) a hedge of the exposure to changes in the fair value of a recognized asset or liability or an unrecognized firm commitment, (b) a hedge of the exposure to variable cash flows of a forecasted transaction, or (c) a hedge of the foreign currency exposure of a net investment in a foreign operation, an unrecognized firm commitment, an available-for-sale security, or a foreign-currency-denominated forecasted transaction. The accounting for the changes in the fair value of a derivative depends on the intended use of the

derivative and the resulting designation. The Company adopted SFAS No. 133 on January 1, 2001. The impact of adoption was not material to the Company's consolidated financial position, results of operations or cash flows.

In December 1999, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 101, "Revenue Recognition in Financial Statements" (SAB No. 101). SAB No. 101, as amended, was implemented in the fourth quarter of 2000 and did not have a material effect on the Company's consolidated financial position, results of operations or cash flows.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

Management may use derivative contracts to manage its exposure to commitments to originate mortgage loans. All of the derivatives utilized by the Company are for purposes other than trading. The derivatives utilized consist of purchased options on FNMA or FHLMC guaranteed mortgage-backed securities. These financial instruments are used to reduce the Company's exposure to the effects of fluctuations in interest rates on the Company's lending and secondary marketing activities. The notional amount and fair value of such derivatives was immaterial at December 31, 2000 and 1999.

In addition, reference is made to "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations — Financial Condition — Interest Rate Sensitivity and Liquidity" which is incorporated herein by reference.

Item 8. Financial Statements and Supplementary Data

Reference is made to the financial statements, the reports thereon, the notes thereto and supplementary data commencing at page F-1 of this Form 10-K, which financial statements, reports, notes and data are incorporated herein by reference.

Set forth below are certain unaudited financial results reflecting the combined operating results of the Company and Citizens for the thirty-one days ended January 31, 2001. These financial results are presented to satisfy the requirements for publication of combined results of operations with respect to affiliate trading restrictions as specified in pooling-of-interests accounting treatment. This information is presented only to satisfy such requirements and is not necessarily indicative of future operating results or financial condition.

Southwest Bancorporation of Texas, Inc. and Subsidiaries Condensed Consolidated Balance Sheet

(In thousands)

(Unaudited)

	January 31, 2001
Total Assets	\$4,090,100
Investment securities	842,112
Loans	2,547,362
Allowance for loan losses	28,602
Deposits	3,135,712
Shareholders' Equity	308,303

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Condensed Consolidated Statement of Income
(In thousands, except per share amounts)
(Unaudited)

	Month Ended January 31, 2001
Interest income:	
Loans	\$19,806
Securities	4,776
Federal funds sold and other	668
Total interest income	25,250
Interest expense on deposits and other borrowings	11,568
Net interest income	13,682
Provision for loan losses	588
Net interest income after provision for loan losses	13,094
Noninterest income:	
Service charges on deposit accounts	1,968
Investment services	762
Other fee income	886
Other operating income	946
Total noninterest income	4,562
Noninterest expenses:	
Salaries and employee benefits	6,456
Occupancy expense	1,708
Other operating expenses	3,323
Total noninterest expenses	11,487
Income before income taxes and minority interest	6,169
Provision for income taxes	1,981
Income before minority interest	4,188
Minority interest	13
Net income	\$ 4,175
Earnings per common share	
Basic	\$ 0.13
Diluted	\$ 0.12

During the first quarter of 2001, market interest rates declined due to the Federal Reserve's rapid interest rate reduction of 50 basis points on January 4 and another 50 basis points on February 4. This decline in interest rates will unfavorably impact the Company's net interest margin in 2001 due to its short term GAP position. As illustrated on page 29, a 100 basis point drop in interest rates, as we have experienced in the first quarter of 2001, may reduce the Company's net interest income by 4.11% for the year, assuming no additional change in interest rates. However as more fully described in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations — Interest Rate Sensitivity and Liquidity", there are inherent limitations in any methodology used to estimate the exposure to changes in market interest rates. The market value sensitivity analysis presented includes assumptions that (i) the composition of the Company's interest sensitive assets and liabilities existing at year end will remain constant over the twelve month measurement period; and (ii) that changes in market rates are parallel and instantaneous across the yield curve regardless of duration or repricing characteristics of specific assets or liabilities. Further, the analysis does not contemplate any actions that the Company might undertake in response to changes in market interest rates. Although it is difficult to predict the long term impact of this decline in interest rates, management expects the net interest margin for the first quarter of 2001 to be in the range of 4.40% to 4.55%, compared to 4.67% for the fourth quarter of 2000. Consistent with the Company's objective to generate stable growth in net interest income and to attempt to control risks associated with interest rate movements, management routinely implements activities which

adjust to changes in the interest rate environment. These activities are expected to have a favorable impact on net interest income over time.

Quarterly financial data (unaudited)

The following table represents summarized data for each of the quarters in fiscal 2000 and 1999 (in thousands, except earnings per share). Such information has been restated from amounts previously reported in the Company's Form 10-Q's to reflect the operations of Citizens Bankers, Inc. and Citizens Bankers Limited Partnership prior to December 29, 2000, the date on which they were merged into the Company in a transaction accounted for as a pooling-of-interests.

	2000				1999			
	Fourth Quarter	Third Quarter	Second Quarter	First Quarter	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Interest income	\$74,082	\$71,361	\$66,019	\$60,704	\$56,963	\$54,148	\$51,094	\$49,027
Interest expense	33,528	32,906	29,131	26,097	23,680	22,425	21,553	20,561
Net interest income	40,554	38,455	36,888	34,607	33,283	31,723	29,541	28,466
Provision for loan losses	1,805	1,791	1,896	1,561	1,538	1,547	1,843	1,546
Net interest income after provision for loan losses	38,749	36,664	34,992	33,046	31,745	30,176	27,698	26,920
Noninterest income	11,252	10,798	10,417	10,426	10,106	9,474	9,069	8,815
Noninterest expenses	34,862	28,968	28,285	28,042	26,883	25,262	28,436	23,930
Income before income taxes and minority interest	15,139	18,494	17,124	15,430	14,968	14,388	8,331	11,805
Provision for income taxes	5,459	6,192	5,769	5,187	5,044	5,008	3,314	4,134
Minority interest	16	21	39	43	17	16	46	(50)
Net income	\$ 9,664	\$12,281	\$11,316	\$10,200	\$ 9,907	\$ 9,364	\$ 4,971	\$ 7,721
Basic earnings per common share	\$ 0.30	\$ 0.37	\$ 0.35	\$ 0.32	\$ 0.31	\$ 0.29	\$ 0.16	\$ 0.25
Diluted earnings per common share	\$ 0.28	\$ 0.36	\$ 0.34	\$ 0.31	\$ 0.30	\$ 0.28	\$ 0.15	\$ 0.24
Weighted average common shares outstanding	34,042	33,791	33,332	33,105	33,082	33,009	32,928	32,750

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

There have been no disagreements with accountants on any matter of accounting principles or practices or financial statement disclosures during the two year period ended December 31, 2000.

PART III

Item 10. Directors and Executive Officers of the Registrant

For information regarding the directors and persons nominated to become directors of the Company, reference is made to the information presented in the Company's definitive Proxy Statement for its 2001 Annual Meeting of Shareholders to be filed with the Commission pursuant to Regulation 14A under the Securities and Exchange Act of 1934 (the "2001 Proxy Statement"). All of such information is incorporated herein by reference.

Item 11. Executive Compensation

For information concerning the compensation paid by the Company during the year ended December 31, 2000 to its executive officers, reference is made to the information presented in the Company's 2001 Proxy Statement. Such information is incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management

For information concerning the beneficial ownership of the common stock of the Company by its directors and officers and by certain other beneficial owners, reference is made to the information presented in the Company's 2001 Proxy Statement. Such information is incorporated herein by reference.

Item 13. Certain Relationships and Related Transactions

For information regarding certain business relationships and related transactions involving the Company's officers and directors, reference is made to the information presented in the Company's 2001 Proxy Statement. Such information is incorporated herein by reference.

PART IV

Item 14. Exhibits, Financial Statement Schedules, and Reports on Form 8-K

(a) and (d) Financial Statements and Financial Statement Schedules

The financial statements and financial statement schedule listed on the accompanying Index to Financial Statements and Schedule (see page F-1) are filed as part of this Form 10-K.

(b) Reports on Form 8-K

One report on Form 8-K was filed by the Company during the three months ended December 31, 2000. The report was filed on October 17, 2000, and Item 5, was reported, including two exhibits.

(c) *Exhibits:

- 2.1 — Agreement and Plan of Merger dated October 16, 2000, between the Company and Citizens Bankers, Inc. (incorporated by reference to Exhibit 2.1 to the Company's Current Report on Form 8-K filed October 17, 2000)
- 2.2 — Purchase Agreement, dated November 9, 2000, among the Company, Southwest Bank of Texas National Association, Citizens Bankers Limited Partnership and Baytown Land I, Ltd. (incorporated by reference to Exhibit 2.1 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2000)
- 3.1 — Articles of Incorporation of the Company
- 3.2 — Bylaws of the Company (Restated as of December 31, 1996)
- 3.3 — Amendment dated December 18, 1996 to Articles of Incorporation of the Company
- 3.4 — Amendment dated May 1, 2000 to Articles of Incorporation of the Company (incorporated by reference to Exhibit 3.1 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2000)
- 4.1 — Specimen Common Stock certificate
- **4.2 — Loan Agreement (and form of \$10,000,000 Promissory Note) dated March 30, 2000, between the Company and Bank of Oklahoma, N.A.
- **4.3 — Loan Agreement (and form of \$5,000,000 Promissory Note) dated June 30, 2000, between the Company and Bank of Oklahoma, N.A.
- **4.4 — Assumption and Modification Agreement dated December 29, 2000 and First Amendment thereto dated January 10, 2001, between Southwest Bank of Texas National Association and American General Life and Accident Insurance Company, relating to Third Modification of Promissory Note (in the original principal amount of \$6,250,000), Deed of Trust and Security Agreement and of Assignment of Leases and Rents
- †10.1 — 1989 Stock Option Plan, amended and restated as of May 29, 1998 (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2000)
- †10.2 — 1993 Stock Option Plan, amended and restated as of May 29, 1998 (incorporated by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2000)
- †10.3 — Form of Stock Option Agreement under 1989 Stock Option Plan and 1993 Stock Option Plan
- †10.4 — 1996 Stock Option Plan, as amended January 24, 2000 (incorporated by reference to Exhibit 10.4 to the Company's Annual Report on Form 10-K for the year ended December 31, 1999)

†10.5	— Form of Incentive Stock Option Agreement under 1996 Stock Option Plan
†10.6	— Form of Non-qualified Stock Option Agreement under 1996 Stock Option Plan
†10.7	— Form of Stock Option Agreement for Directors under 1996 Stock Option Plan (incorporated by reference to Exhibit 10.8 to the Company's Form S-1 Registration Statement No. 333-16509)
†10.8	— Form of Change in Control Agreement, dated as of January 1, 2000, between the Company and Paul B. Murphy, Jr. (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2000)
†10.9	— Form of Change in Control Agreement, dated as of January 1, 2000, between the Company and each of Joseph H. Argue, J. Nolan Bedford, David C. Farries, James R. Massey and Steve D. Stephens (incorporated by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2000)
†10.10	— Employment Agreement between the Company and Walter Lane Ward, Jr. (incorporated by reference to Exhibit 10.11 to the Company's Annual Report on Form 10-K for the year ended December 31, 1999)
†***10.11	— Employment Agreement, amended and restated as of February 17, 2001, between the Company and Walter E. Johnson (incorporated by reference to the Company's Current Report on Form 8-K filed March 7, 2000)
***21.1	— List of subsidiaries of the Company
***23.1	— Consent of PricewaterhouseCoopers LLP

* All Exhibits except for those filed herewith and as otherwise indicated are incorporated herein by reference to the Exhibits bearing the same Exhibit numbers in the Company's Form S-1 Registration Statement No. 333-16509.

** This Exhibit is not filed herewith because it meets the exclusion set forth in Section 601(b)(4)(iii)(A) of Regulation S-K and the Company hereby agrees to furnish a copy thereof to the Commission upon request.

*** Filed herewith.

† Management contract or compensatory plan or arrangement.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

SOUTHWEST BANCORPORATION
OF TEXAS, INC.

By: /s/ PAUL B. MURPHY, JR.
Paul B. Murphy, Jr.
President and Chief Executive Officer

Date: March 1, 2001

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

<u>Signature</u>	<u>Title</u>	<u>Date</u>
<u>/s/ WALTER E. JOHNSON</u> Walter E. Johnson	Chairman of the Board	March 1, 2001
<u>/s/ PAUL B. MURPHY, JR.</u> Paul B. Murphy, Jr.	Director, President and Chief Executive Officer (Principal Executive Officer)	March 1, 2001
<u>/s/ JOHN H. ECHOLS</u> John H. Echols	Director, Chief Executive Officer, Baytown Region	March 1, 2001
<u>/s/ DAVID C. FARRIES</u> David C. Farries	Executive Vice President, Treasurer and Secretary (Principal Financial Officer)	March 1, 2001
<u>/s/ R. JOHN McWHORTER</u> R. John McWhorter	Senior Vice President and Controller (Principal Accounting Officer)	March 1, 2001
<u>/s/ JOHN W. JOHNSON</u> John W. Johnson	Director and Chairman of the Executive Committee of the Board	March 1, 2001
<u>/s/ JOHN B. BROCK III</u> John B. Brock III	Director	March 1, 2001
<u>/s/ ERNEST H. COCKRELL</u> Ernest H. Cockrell	Director	March 1, 2001
<u>/s/ J. DAVID HEANEY</u> J. David Heaney	Director	March 1, 2001
<u>/s/ ANDRES PALANDJOGLOU</u> Andres Palandjoglou	Director	March 1, 2001
<u>/s/ ADOLPH A. PFEFFER, JR.</u> Adolph A. Pfeffer, Jr.	Director	March 1, 2001
<u>/s/ WILHELMINA E. ROBERTSON</u> Wilhelmina E. Robertson	Director	March 1, 2001
<u>/s/ STANLEY D. STEARNS, JR.</u> Stanley D. Stearns, Jr.	Director	March 1, 2001
<u>/s/ DUNCAN W. STEWART</u> Duncan W. Stewart	Director	March 1, 2001
<u>/s/ WALTER LANE WARD, JR.</u> Walter Lane Ward, Jr.	Director	March 1, 2001
<u>/s/ MICHAEL T. WILLIS</u> Michael T. Willis	Director	March 1, 2001

SOUTHWEST BANCORPORATION OF TEXAS, INC. AND SUBSIDIARIES

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REPORT OF INDEPENDENT ACCOUNTANTS

To the Board of Directors and Shareholders
Southwest Bancorporation of Texas, Inc.:

In our opinion, the accompanying consolidated balance sheet and the related consolidated statements of income, of changes in shareholders' equity, and of cash flows present fairly, in all material respects, the consolidated financial position of Southwest Bancorporation of Texas, Inc. and Subsidiaries (the "Company") at December 31, 2000 and 1999, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2000, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

Houston, Texas
February 23, 2001

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Consolidated Balance Sheet

(Dollars in thousands, except share and per share amounts)

	December 31,	
	2000	1999
ASSETS		
Cash and due from banks	\$ 331,965	\$ 188,432
Federal funds sold and other cash equivalents	79,341	25,642
Total cash and cash equivalents	411,306	214,074
Securities — available for sale	848,164	831,425
Securities — held to maturity (fair value of \$57,941 at December 31, 1999)	—	58,944
Loans held for sale	85,939	77,047
Loans held for investment, net	2,397,348	1,935,859
Premises and equipment, net	52,462	39,632
Accrued interest receivable	27,334	20,492
Other assets	117,789	93,715
Total assets	\$3,940,342	\$3,271,188
LIABILITIES AND SHAREHOLDERS' EQUITY		
Deposits:		
Demand — noninterest-bearing	\$ 892,296	\$ 716,785
Demand — interest-bearing	62,773	70,935
Money market accounts	1,154,808	971,527
Savings	76,715	71,146
Time, \$100 and over	506,629	367,051
Other time	400,649	334,189
Total deposits	3,093,870	2,531,633
Securities sold under repurchase agreements	211,800	216,838
Other borrowings	305,961	267,140
Accrued interest payable	5,505	4,072
Other liabilities	23,768	17,332
Total liabilities	3,640,904	3,037,015
Minority interest in consolidated subsidiary	1,313	1,097
Commitments and contingencies		
Shareholders' equity:		
Common stock — \$1 par value, 75,000,000 shares authorized;		
32,705,909 issued and 32,704,877 outstanding at December 31, 2000 and		
32,877,395 issued and 32,028,726 outstanding at December 31, 1999	32,706	32,877
Additional paid-in capital	69,735	62,229
Retained earnings	198,835	157,716
Accumulated other comprehensive loss	(3,107)	(15,770)
Treasury stock, at cost — 1,032 shares and 848,669 shares, respectively	(44)	(3,976)
Total shareholders' equity	298,125	233,076
Total liabilities and shareholders' equity	\$3,940,342	\$3,271,188

The accompanying notes are an integral part of the consolidated financial statements.

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Consolidated Statement of Income

(Dollars in thousands, except per share amounts)

	Year Ended December 31,		
	2000	1999	1998
Interest income:			
Loans	\$210,990	\$150,576	\$125,847
Securities	57,755	58,007	51,503
Federal funds sold and other	3,421	2,649	8,313
Total interest income	272,166	211,232	185,663
Interest expense on deposits and other borrowings	121,662	88,219	80,080
Net interest income	150,504	123,013	105,583
Provision for loan losses	7,053	6,474	4,261
Net interest income after provision for loan losses	143,451	116,539	101,322
Noninterest income:			
Service charges on deposit accounts	20,765	17,017	13,020
Investment services	6,017	4,868	4,173
Other fee income	9,719	8,740	6,783
Other operating income	6,859	6,973	6,628
Gain (loss) on sale of securities, net	(467)	(134)	933
Total noninterest income	42,893	37,464	31,537
Noninterest expenses:			
Salaries and employee benefits	67,060	57,516	50,919
Occupancy expense	18,021	16,112	13,740
Merger-related expenses and other charges	4,122	4,474	67
Other operating expenses	30,954	26,409	23,144
Total noninterest expenses	120,157	104,511	87,870
Income before income taxes and minority interest	66,187	49,492	44,989
Provision for income taxes	22,607	17,500	15,766
Income before minority interest	43,580	31,992	29,223
Minority interest	119	29	205
Net income	\$ 43,461	\$ 31,963	\$ 29,018
Earnings per common share:			
Basic	\$ 1.34	\$ 1.01	\$ 0.97
Diluted	\$ 1.29	\$ 0.97	\$ 0.91

The accompanying notes are an integral part of the consolidated financial statements.

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Consolidated Statement of Changes in Shareholders' Equity
(Dollars in thousands, except share and per share amounts)

	Common Stock		Additional	Retained	Accumulated	Treasury	Total
	Shares	Dollars	Paid-in	Earnings	Other	Stock	Shareholders'
			Capital		Comprehensive		Equity
					Income		
BALANCE, DECEMBER 31, 1997	28,884,252	\$29,983	\$44,403	\$104,012	\$ 397	\$ (5,377)	\$173,418
Common stock issued in acquisition	280,000	280	304				584
Issuance of common stock to the recognition and retention plan	4,707	5	(5)				—
Exercise of stock options	713,457	713	3,061				3,774
Conversion of subordinated debentures	1,606,631	1,607	9,736				11,343
Deferred compensation amortization			187				187
Stock compensation			358				358
Cash dividends paid by Fort Bend				(723)			(723)
Cash dividends paid by Citizens				(3,008)			(3,008)
Treasury stock purchased	(4,989)					(55)	(55)
Comprehensive income:							
Net income for the year ended December 31, 1998				29,018			29,018
Net change in unrealized appreciation on securities available for sale, net of deferred taxes of (\$1,355)					2,540		2,540
Total comprehensive income							31,558
Adjustment to conform reporting periods	(80,110)	(80)	(446)	(335)	—	—	(861)
BALANCE, DECEMBER 31, 1998	31,403,948	32,508	57,598	128,964	2,937	(5,432)	216,575
Issuance of common stock to 401(k) plan	4,431	4	73				77
Exercise of stock options	313,024	313	2,150				2,463
Purchase of minority interest in Mitchell Mortgage	307,323	307	3,303				3,610
Deferred compensation amortization			106				106
Cancellation of treasury stock		(255)	(1,201)			1,456	—
Cash dividends paid by Fort Bend				(277)			(277)
Cash dividends paid by Citizens				(2,934)			(2,934)
Stock compensation			200				200
Comprehensive income:							
Net income for the year ended December 31, 1999				31,963			31,963
Net change in unrealized depreciation on securities available for sale, net of deferred taxes of \$9,996					(18,707)		(18,707)
Total comprehensive income							13,256
BALANCE, DECEMBER 31, 1999	32,028,726	32,877	62,229	157,716	(15,770)	(3,976)	233,076
Exercise of stock options	687,161	687	8,023				8,710
Forfeiture of stock options			(44)				(44)
Deferred compensation amortization			48				48
Cash dividends paid by Citizens				(2,342)			(2,342)
Cancellation of treasury stock		(858)	(3,234)			4,092	—
Treasury stock purchased	(9,978)					(116)	(116)
Creation of treasury stock	(1,032)		44			(44)	—
Conversion of partnership to C corp			2,669				2,669
Comprehensive income:							
Net income for the year ended December 31, 2000				43,461			43,461
Net change in unrealized appreciation on securities available for sale, net of deferred taxes of (\$7,015)					12,663		12,663
Total comprehensive income							56,124
BALANCE, DECEMBER 31, 2000	32,704,877	\$32,706	\$69,735	\$198,835	\$ (3,107)	\$ (44)	\$298,125

The accompanying notes are an integral part of the consolidated financial statements.

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Consolidated Statement of Cash Flows

(Dollars in thousands)

	Year Ended December 31,		
	2000	1999	1998
Cash flows from operating activities:			
Net income	\$ 43,461	\$ 31,963	\$ 29,018
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan losses	7,053	6,474	4,261
Depreciation	8,013	7,764	6,273
Realized (gain) loss on securities available for sale, net	467	134	(933)
Amortization	4,217	3,911	4,188
Minority interest in net income of consolidated subsidiary	119	29	205
Gain on sale of loans, net	(397)	(570)	(1,329)
Dividends on Federal Home Loan Bank stock	(1,025)	(617)	(936)
Origination of loans held for sale and mortgage servicing rights	(61,364)	(91,303)	(120,526)
Proceeds from sales of loans	45,607	74,935	115,725
Increase in accrued interest receivable, prepaid expenses and other assets	(31,031)	(19,853)	(14,922)
Increase in accrued interest payable and other liabilities	14,559	1,609	2,688
Other, net	215	1,391	(1,446)
Adjustment to conform reporting periods	—	—	2,650
Net cash provided by operating activities	29,894	15,867	24,916
Cash flows from investing activities:			
Proceeds from maturity of securities available for sale	2,890	41,622	284,996
Proceeds from maturity of securities held to maturity	8,705	9,275	22,751
Principal paydowns of mortgage-backed securities available for sale	97,614	160,901	197,514
Principal paydowns of mortgage-backed securities held to maturity	7,215	13,090	44,854
Proceeds from sale of securities available for sale	1,039,012	259,045	123,185
Purchase of securities available for sale	(1,085,192)	(429,662)	(697,150)
Purchase of securities held to maturity	(10,368)	(23,201)	(32,849)
Net increase in loans receivable	(467,742)	(389,555)	(394,711)
Purchase of Bank-owned life insurance policies	—	(5,000)	(20,000)
Purchase of premises and equipment	(21,100)	(10,664)	(11,760)
Other, net	50	2,090	197
Adjustment to conform reporting periods	—	—	9,654
Net cash used in investing activities	(428,916)	(372,059)	(473,319)
Cash flows from financing activities:			
Net increase in noninterest-bearing demand deposits	175,511	44,577	55,315
Net increase in time deposits	206,038	16,416	45,510
Net increase in other interest-bearing deposits	180,688	96,645	183,950
Net increase (decrease) in securities sold under repurchase agreements	(5,038)	35,142	25,864
Net proceeds from exercise of stock options	3,636	1,146	1,734
Net increase in other borrowings	39,701	162,905	83,188
Payment of dividends by Citizens and Fort Bend	(3,124)	(3,016)	(3,855)
Purchase of treasury stock	(116)	—	(55)
Other, net	(162)	(52)	(534)
Adjustment to conform reporting periods	—	—	(13,318)
Net cash provided by financing activities	596,254	353,763	377,799
Net increase (decrease) in cash and cash equivalents	197,232	(2,429)	(70,604)
Cash and cash equivalents at beginning of period	214,074	216,503	287,107
Cash and cash equivalents at end of period	\$ 411,306	\$ 214,074	\$ 216,503

The accompanying notes are an integral part of the consolidated financial statements.

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Notes to Consolidated Financial Statements

(Dollars in thousands, except share and per share amounts)

1. Nature of Operations and Summary of Significant Accounting Policies:

Basis of Presentation and Nature of Operations

The consolidated financial statements include the accounts of Southwest Bancorporation of Texas, Inc. (the "Company") and its direct and indirect wholly-owned subsidiaries, Southwest Holding Delaware Inc. (the "Delaware Company"), Southwest Bank of Texas National Association (the "Bank"), and Mitchell Mortgage Company, LLC ("Mitchell"). The consolidated financial statements also include the accounts of First National Bank of Bay City, a 58% owned subsidiary of the Delaware Company. All material intercompany accounts and transactions have been eliminated.

Substantially all of the Company's revenue and income is derived from the operations of the Bank. The Bank provides a full range of commercial and private banking services to small and middle market businesses and individuals in the Houston metropolitan area.

In connection with the Company's merger with Citizens Bankers, Inc. ("Citizens") and acquisition of all of the assets and liabilities of Citizens Bankers Limited Partnership ("CBLP") (as more fully discussed in note 2), the historical financial data has been restated to include the accounts and operations of Citizens and CBLP for all periods presented.

Management's Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of income and expenses during the reporting periods. Actual results could differ from those estimates.

Cash and Cash Equivalents

The Company considers federal funds sold, due from bank demand accounts and other highly liquid investments purchased with a maturity of three months or less to be cash equivalents. The Company classifies investments in money market funds as securities and not cash equivalents.

The Company is required to maintain noninterest-bearing cash reserve balances with the Federal Reserve Bank. The average of such cash balances was approximately \$5,325 and \$7,734 for the years ended December 31, 2000 and 1999, respectively.

Securities

Securities which management intends and has the ability to hold to maturity are classified as held to maturity. Securities held to maturity are stated at cost, increased by accretion of discounts and reduced by amortization of premiums, both computed by the interest method.

Securities to be held for indefinite periods of time, including securities that management intends to use as part of its asset/liability strategy, or that may be sold in response to changes in interest rates, changes in prepayment risk, the need to increase regulatory capital or other similar factors, are classified as available for sale and are carried at fair value. Fair values of securities are estimated based on available market quotations. Unrealized holding gains and losses, net of taxes, on available for sale securities are reported as a separate component of other comprehensive income until realized. The amortized cost of securities available for sale is increased by accretion of discounts and reduced by amortization of premiums, both computed by the interest method. Gains and losses on the sale of available for sale securities are determined using the specific identification method.

Southwest Bancorporation of Texas, Inc. and Subsidiaries

Notes to Consolidated Financial Statements — (Continued)

Trading securities are carried at market value. Realized and unrealized gains and losses on trading securities are recognized in the consolidated statement of income as they occur. The Company held no trading securities at December 31, 2000 and 1999.

The Company reviews its financial position, liquidity and future plans in evaluating the criteria for classifying investment securities. Securities are classified among categories at the time the securities are purchased. Declines in the fair value of individual held to maturity and available for sale securities below their cost that are other than temporary would result in write-downs of the individual securities to their fair value. The Company believes that none of the unrealized losses should be considered other than temporary.

Loans

Loans held for investment are reported at the principal amount outstanding, net of unearned discounts, deferred loan fees and the allowance for loan losses.

Loans on which the accrual of interest has been discontinued are designated as nonaccrual loans. Loans are designated as nonaccrual when reasonable doubt exists as to the full, timely collection of interest or principal. When a loan is placed on nonaccrual status, all interest previously accrued but not collected is reversed against current period interest income. Income on such loans is then recognized only to the extent that cash is received and where the future collection of interest and principal is probable. Interest accruals are resumed on such loans only when they are brought fully current with respect to interest and principal and when, in the judgment of management, the loans are estimated to be fully collectible as to both principal and interest.

A loan is considered impaired, based on current information and events, if it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. A loan is not considered impaired during a period of delay in payment if the Company expects to collect all amounts due, including interest past due. The Company generally considers a period of delay in payment to include delinquency up to 90 days. The measurement of impaired loans is based on the present value of expected future cash flows discounted at the loan's effective interest rate or the loan's observable market price or based on the fair value of the collateral if the loan is collateral-dependent. If the measure of the impaired loan is less than the recorded investment in the loan, an impairment is recognized through the provision for loan losses.

The accrual of interest on impaired loans is discontinued when, in management's opinion, the borrower may be unable to meet payments as they become due. When interest accrual is discontinued, all unpaid accrued interest is reversed. Interest income is subsequently recognized only to the extent cash payments are received.

Loans held for sale are carried at the lower of cost or market, which is computed by the aggregate method (unrealized losses are offset by unrealized gains). The carrying amount of loans held for sale in the near-term is adjusted by gains and losses generated from corresponding hedging transactions entered into to protect loss of value from increases in interest rates. Hedge positions are also used to protect the pipeline of loan applications in process from increases in interest rates. Gains and losses resulting from changes in the market value of the inventory and open hedge positions are netted.

Allowance for Loan Losses

The allowance for loan losses is established through a provision for such losses charged against operations. Loans are charged against the allowance for loan losses when management believes that the collectibility of the principal is unlikely. The allowance is an amount that management believes will be adequate to reflect the risks inherent in the existing loan portfolio and is based on evaluations of the collectibility and prior loss experience of loans. In making its evaluation, management considers growth in the loan portfolio, the diversification by industry of the Company's commercial loan portfolio, the effect of changes in the local real estate market on collateral values, the results of recent

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Notes to Consolidated Financial Statements — (Continued)

regulatory examinations, the effects on the loan portfolio of current economic indicators and their probable impact on borrowers, the amount of charge-offs for the period, the amount of nonperforming loans and related collateral security and the evaluation of its loan portfolio by the loan review function.

The evaluation of the adequacy of loan collateral is often based upon estimates and appraisals. Because of changing economic conditions, the valuations determined from such estimates and appraisals may also change. Accordingly, the Company may ultimately incur losses which vary from management's current estimates. Adjustments to the allowance for loan losses will be reported in the period such adjustments become known or are reasonably estimable.

Loan Fees and Costs

Nonrefundable loan origination and commitment fees net of certain direct costs associated with originating loans are deferred and recognized as an adjustment to the related loan yield.

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation and amortization. Depreciation expense is computed using the straight-line method and is charged to operating expense over the estimated useful lives of the assets. Depreciation expense has been computed principally using estimated lives of thirty years for premises, three to five years for hardware and software, and five to ten years for furniture and equipment. Leasehold improvements are amortized using the straight-line method over the shorter of the initial term of the respective lease or the estimated useful life of the improvement. Costs of major additions and improvements are capitalized. Expenditures for maintenance and repairs are charged to operations as incurred. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts and any resulting gain or loss is reflected in income for the period.

Other Real Estate Owned

Real estate acquired through foreclosure is carried at the lower of the recorded investment in the property or its fair value less estimated selling costs. Prior to foreclosure, the value of the underlying collateral of the loan is written down to its estimated fair value less estimated selling costs by a charge to the allowance for loan losses, if necessary. Any subsequent write-downs are charged against operations. Operating expenses of such properties are included in other operating expenses in the accompanying consolidated statement of income.

Mortgage Servicing

Mortgage servicing rights represent the right to receive future mortgage servicing fees. The Company recognizes as separate assets the right to service mortgage loans for others, whether the servicing rights are acquired through a separate purchase or through loan origination by allocating total costs incurred between the loan and the servicing rights retained based on their relative fair values. Mortgage servicing rights are amortized in proportion to, and over the period of, estimated net servicing income. The Company periodically evaluates the carrying value of the mortgage servicing rights in relation to the present value of the estimated future net servicing revenue based on management's best estimate of remaining loan lives.

Mortgage servicing rights are reported as a component of other assets in the accompanying consolidated balance sheet. Fair values are based on quoted market prices in active markets for loans and loan servicing rights. For purchased mortgage servicing rights, the cost of acquiring loan servicing contracts is capitalized to the extent such costs do not exceed the amount by which the present value of estimated future servicing revenue exceeds the present value of expected future servicing costs.

Southwest Bancorporation of Texas, Inc. and Subsidiaries

Notes to Consolidated Financial Statements — (Continued)

Mortgage loans serviced for others are not included in the consolidated balance sheet. The unpaid principal balance of mortgage loans serviced for others was approximately \$1,317,000 and \$908,000 at December 31, 2000 and 1999, respectively.

Custodial escrow balances maintained in connection with the foregoing loan servicing, and included in demand deposits, were approximately \$41,018 and \$21,306 at December 31, 2000 and 1999, respectively.

Earnings Per Common Share

Basic earnings per common share is computed by dividing income available for common shareholders by the weighted average number of common shares outstanding for the period. Diluted earnings per common share is computed by dividing income available for common shareholders, adjusted for any changes in income that would result from the assumed conversion of all potential dilutive common shares, by the sum of the weighted average number of common shares outstanding and the effect of all potential dilutive common shares outstanding for the period.

Income Taxes

Deferred income taxes are provided utilizing the liability method whereby deferred income tax assets or liabilities are recognized for the tax consequences in future years of differences in the tax bases of assets and liabilities and their financial reporting amounts based on enacted tax laws and statutory tax rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized.

Off-Balance Sheet Financial Instruments

In the ordinary course of business the Company has entered into off-balance sheet financial instruments consisting of commitments to extend credit, commitments to sell mortgage loans, commercial letters of credit and standby letters of credit. Such financial instruments are recorded in the financial statements when they are funded or related fees are incurred or received.

New Accounting Pronouncements

In June 1998, Statement of Financial Accounting Standards (SFAS) No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended, was issued by the Financial Accounting Standards Board to establish accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. SFAS No. 133 requires that an entity recognize those instruments at fair value. If certain conditions are met, a derivative may be specifically designated as (a) a hedge of the exposure to changes in the fair value of a recognized asset or liability or an unrecognized firm commitment, (b) a hedge of the exposure to variable cash flows of a forecasted transaction, or (c) a hedge of the foreign currency exposure of a net investment in a foreign operation, an unrecognized firm commitment, an available-for-sale security, or a foreign-currency-denominated forecasted transaction. The accounting for the changes in the fair value of a derivative depends on the intended use of the derivative and the resulting designation. The Company adopted SFAS No. 133 on January 1, 2001. The impact of the adoption was not material to the Company's consolidated financial position, results of operations or cash flows.

In December 1999, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 101, "Revenue Recognition in Financial Statements" (SAB No. 101). SAB No. 101, as amended, was implemented in the fourth quarter of 2000 and did not have a material effect on the Company's consolidated financial position, results of operations or cash flows.

2. Mergers:

On December 29, 2000, the Company consummated its merger with Citizens. Citizens was a multi-bank holding company and the parent company of Citizens Bank and Trust Co., Baytown State Bank and Pasadena State Bank (which

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Notes to Consolidated Financial Statements — (Continued)

also were merged into the Bank on December 29, 2000) and the majority owner of First National Bank of Bay City. In accordance with the Agreement and Plan of Merger, the Company exchanged 249,443 shares of the Company's common shares for each share of Citizens common stock, resulting in the issuance of approximately 3.9 million shares of Company Common Stock on a fully diluted basis. At December 29, 2000, Citizens had total assets of approximately \$436,000 and total deposits of approximately \$381,000. In a related transaction, the Company, CBLP and Baytown Land I, Ltd., the general partner of CBLP, entered into an agreement pursuant to which the Company acquired the assets and assumed the liabilities of CBLP. CBLP's primary assets and liabilities were the building in which Citizens main branch was located and the related debt to third parties. In connection with this agreement, the Company issued approximately 106,000 shares of the Company's Common Stock on a fully diluted basis. These transactions have been accounted for as a pooling of interests.

On April 1, 1999, the Company consummated its merger with Fort Bend Holding Corp. ("Fort Bend"). Fort Bend was the parent company of Fort Bend Federal Savings and Loan Association of Rosenberg (which also was merged into the Bank on April 1, 1999) and the majority owner of Mitchell. In accordance with the Agreement and Plan of Merger, the Company exchanged 1.45 shares of the Company's common shares for each share of Fort Bend common stock, resulting in the issuance of approximately 4.1 million shares of Company Common Stock. At March 31, 1999 Fort Bend had total assets of approximately \$316,000 and total deposits of approximately \$269,000. The transaction has been accounted for as a pooling of interests.

Through the merger with Fort Bend, the Company acquired Fort Bend's 51% ownership interest in Mitchell Mortgage Company L.L.C. ("Mitchell"), a full service mortgage banking affiliate of The Woodlands Operating Company L.P. ("Woodlands"). On June 17, 1999, the Company issued 307,323 shares of Company Common Stock to Woodlands in exchange for Woodlands' 49% ownership in Mitchell and Mitchell became a wholly-owned subsidiary of the Bank effective as of June 30, 1999. As a result, 100% of the accounts and operations of Mitchell after that date are included in the financial statements of the Company.

The Company's consolidated financial statements have been restated to include the accounts and operations of Citizens, CBLP and Fort Bend for all periods presented. Separate interest income and net income amounts of the merged entities are presented in the following table:

	2000	1999	1998
Interest income:			
Periods prior to consummation:			
Company	\$243,830	\$ 37,612	\$139,144
Citizens	28,336	25,009	23,916
Fort Bend	—	5,454	22,603
Periods subsequent to consummation	—	143,157	—
Total interest income	\$272,166	\$211,232	\$185,663
Net income:			
Periods prior to consummation:			
Company	\$ 37,825	\$ 6,305	\$ 22,470
Citizens	5,636	5,113	4,557
Fort Bend	—	410	1,991
Periods subsequent to consummation	—	20,135	—
Total net income	\$ 43,461	\$ 31,963	\$ 29,018

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Notes to Consolidated Financial Statements — (Continued)

3. Securities:

The amortized cost and fair value of securities classified as available for sale and held to maturity is as follows:

	Amortized Cost	December 31, 2000		Fair Value
		Gross Gains	Unrealized Losses	
Available for sale:				
U.S. Government securities	\$169,069	\$ 1,080	\$ (819)	\$169,330
Mortgage-backed securities	618,523	2,088	(7,395)	613,216
Federal Reserve Bank stock	3,949	—	—	3,949
Federal Home Loan Bank stock	17,972	—	—	17,972
Other securities	43,411	335	(49)	43,697
Total securities available for sale	\$852,924	\$ 3,503	\$ (8,263)	\$848,164
	Amortized Cost	December 31, 1999		Fair Value
		Gross Gains	Unrealized Losses	
Available for sale:				
U.S. Government securities	\$134,001	\$ 35	\$ (3,499)	\$130,537
Mortgage-backed securities	678,523	470	(21,338)	657,655
Federal Reserve Bank stock	2,981	—	—	2,981
Federal Home Loan Bank stock	16,051	—	—	16,051
Other securities	24,307	77	(183)	24,201
Total securities available for sale	\$855,863	\$ 582	\$ (25,020)	\$831,425
Held to maturity:				
U.S. Government securities	\$ 12,761	\$ 1	\$ (287)	\$ 12,475
Mortgage-backed securities	29,164	3	(612)	28,555
Other securities	17,019	28	(136)	16,911
Total securities held to maturity	\$ 58,944	\$ 32	\$ (1,035)	\$ 57,941

The scheduled maturities of securities classified as available for sale is as follows:

	December 31, 2000	
	Amortized Cost	Fair Value
Available for sale:		
Due in one year or less	\$ 21,359	\$ 21,395
Due from one year to five years	140,227	140,527
Due after five years	7,483	7,408
U.S. Government securities	169,069	169,330
Mortgage-backed securities	618,523	613,216
Federal Reserve Bank stock	3,949	3,949
Federal Home Loan Bank stock	17,972	17,972
Other securities	43,411	43,697
Total securities available for sale	\$852,924	\$848,164

Securities with a carrying value of \$593,672 and \$575,617 at December 31, 2000 and 1999, respectively, have been pledged to collateralize repurchase agreements, public deposits, Federal Home Loan Bank borrowings and other items.

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Notes to Consolidated Financial Statements — (Continued)

In connection with the Citizens merger, the Company transferred all of Citizens' held to maturity debt securities to the available for sale category. The amortized cost of these securities at the time of transfer was \$55,800 and the unrealized gain was \$267 (\$174 net of income taxes). In connection with the Fort Bend merger, the Company transferred all of Fort Bend's held to maturity debt securities to the available for sale category in 1999. The amortized cost of these securities at the time of transfer was \$57,800 and the unrealized gain was \$80 (\$52 net of income taxes). The Company does not intend to sell these securities in the near term.

Gross gains of \$307, \$286 and \$996 and gross losses of \$774, \$420 and \$63 were recognized on sales of investment securities for the years ended December 31, 2000, 1999 and 1998, respectively.

4. Loans:

A summary of loans outstanding follows:

	December 31,	
	2000	1999
Commercial and industrial	\$ 958,146	\$ 750,585
Real estate:		
Construction and land development	643,164	502,231
1-4 family residential	336,024	290,117
Other	303,568	246,442
Consumer	192,271	171,772
Less:		
Unearned income and fees, net of related costs	(7,675)	(2,852)
Allowance for loan losses	(28,150)	(22,436)
Loans held for investment, net	2,397,348	1,935,859
Loans held for sale	85,939	77,047
Total loans, net	\$2,483,287	\$2,012,906

An analysis of the allowance for loan losses is as follows:

	Years Ended December 31,		
	2000	1999	1998
Balance, beginning of year	\$22,436	\$17,532	\$14,385
Provision charged against operations	7,053	6,474	4,261
Charge-offs	(2,093)	(2,211)	(1,506)
Recoveries	754	641	374
Adjustment to conform reporting periods	—	—	18
Balance, end of year	\$28,150	\$22,436	\$17,532

The Company's impaired loans were approximately \$10,800 and \$13,700 at December 31, 2000 and 1999 respectively. The average recorded investment in impaired loans during 2000, 1999 and 1998 was \$9,300, \$13,900 and \$6,300, respectively. The total required allowance for loan losses related to these loans was \$1,000 and \$0 at December 31, 2000 and 1999, respectively. Interest income on impaired loans of \$1,100, \$1,500 and \$415 was recognized for cash payments received in 2000, 1999 and 1998, respectively.

The Bank is not committed to lend additional funds to debtors whose loans have been modified.

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Notes to Consolidated Financial Statements — (Continued)

The Company has loans, deposits, and other transactions with its principal shareholders, officers, directors and organizations with which such persons are associated which were made in the ordinary course of business. At December 31, 2000, the aggregate amount of loans and unfunded lines of credit to such related parties was \$65,302. Following is an analysis of activity with respect to these amounts:

	December 31, 2000
Balance, beginning of year	\$ 56,346
New loans and unfunded lines of credit	48,320
Repayments	(39,364)
Balance, end of year	<u>\$ 65,302</u>

5. Premises and Equipment:

Premises and equipment consist of the following:

	December 31,	
	2000	1999
Land	\$ 11,181	\$ 9,129
Premises and leasehold improvements	37,363	30,246
Furniture and equipment	50,878	40,370
	99,422	79,745
Less accumulated depreciation and amortization	(46,960)	(40,113)
	<u>\$ 52,462</u>	<u>\$ 39,632</u>

6. Other Assets:

Other assets consist of the following:

	December 31,	
	2000	1999
Foreclosed real estate	\$ 454	\$ 1,840
Deferred income taxes	13,053	15,766
Goodwill	2,847	3,103
Banker's acceptances	5,750	4,152
Investment in unconsolidated investees	6,557	5,474
Cash value of bank-owned life insurance	28,664	27,197
Factored receivables	27,503	18,542
Mortgage servicing rights	12,334	6,681
Other	20,627	10,960
	<u>\$117,789</u>	<u>\$93,715</u>

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Notes to Consolidated Financial Statements — (Continued)

7. Deposits:

At December 31, 2000, scheduled maturities of time deposits are summarized as follows:

	December 31, 2000
2001	\$719,458
2002	121,289
2003	21,807
2004	16,397
2005	26,625
Thereafter	1,702
	\$907,278

At December 31, 2000 and 1999, the aggregate amount of deposits from related parties was \$140,082 and \$47,021, respectively.

Brokered deposits were \$53,406 and \$30,056 at December 31, 2000 and 1999, respectively.

8. Securities Sold under Repurchase Agreements and Other Borrowings:

Securities sold under repurchase agreements and other borrowings, consisting of federal funds purchased and treasury, tax, and loan deposits, generally represent borrowings with maturities ranging from one to thirty days. Information relating to these borrowings is summarized as follows:

	December 31, 2000	December 31, 1999
Securities sold under repurchase agreements:		
Average	\$209,816	\$184,358
Year-end	211,800	216,838
Maximum month-end balance during year	241,834	216,838
Interest rate:		
Average	4.69%	4.06%
Year-end	4.89%	4.03%
Other borrowings:		
Average	\$205,213	\$196,694
Year-end	305,961	267,140
Maximum month-end balance during year	380,121	284,455
Interest rate:		
Average	6.39%	5.39%
Year-end	6.83%	5.27%

Securities sold under repurchase agreements generally include U.S. Government securities and are maintained in safekeeping by correspondent banks. The Company enters into these repurchase agreements as a service to its customers.

Subject to certain limitations, the Bank may borrow funds from the Federal Home Loan Bank ("FHLB") in the form of advances. Credit availability from the FHLB to the Bank is based on the Bank's financial and operating condition. Borrowings from the FHLB to the Bank were approximately \$193,400 and \$237,200 at December 31, 2000 and 1999, respectively. In addition to creditworthiness, the Bank must own a minimum amount of FHLB capital stock. This minimum is 5.00% of outstanding FHLB advances. Unused borrowing capacity at December 31, 2000 was approximately \$293,200.

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Notes to Consolidated Financial Statements — (Continued)

9. Income Taxes:

The income tax provision (benefit) for the years ended December 31, 2000, 1999 and 1998 is composed of the following:

	2000	1999	1998
Current	\$24,287	\$18,647	\$18,172
Deferred	(1,680)	(1,147)	(2,406)
Total	\$22,607	\$17,500	\$15,766

The types of temporary differences between the tax bases of assets and liabilities and their financial reporting amounts that give rise to deferred income tax assets and liabilities and their approximate tax effects are as follows:

	December 31, 2000		December 31, 1999	
	Temporary Differences	Tax Effect	Temporary Differences	Tax Effect
Future deductible differences:				
Unrealized loss on securities available for sale	\$ 4,760	\$ 1,653	\$24,438	\$ 8,668
Allowance for loan losses	28,004	9,780	20,984	7,326
Mortgage servicing rights	645	226	1,455	509
Bank premises	5,389	1,886	—	—
Other	2,402	817	2,075	750
Deferred income tax asset	\$41,200	\$14,362	\$48,952	\$17,253
Future taxable differences:				
Market discount on securities	\$ 477	\$ 167	\$ 577	\$ 202
Federal Home Loan Bank stock dividend	3,278	1,142	2,137	744
Bank premises	—	—	1,546	541
Deferred income tax liability	\$ 3,755	\$ 1,309	\$ 4,260	\$ 1,487
Net deferred income tax asset		\$13,053		\$15,766

In connection with the Company's merger with Citizens and CBLP, the Company recorded deferred tax assets of \$2,669 with an offsetting credit to additional paid in capital related to differences in the tax bases of assets and liabilities and their financial reporting amounts. Such deferred taxes were not previously recorded by CBLP as it was organized as a limited partnership.

The reconciliation between the Company's effective income tax rate and the statutory federal income tax rate is as follows:

	Year Ended December 31,		
	2000	1999	1998
Statutory federal income tax rate	35.0 %	35.0 %	35.0 %
Permanent differences	(0.91)	0.36	(0.09)
Effective income tax rate	34.09%	35.36%	34.91%

10. Employee Benefits:

Stock-Based Compensation Plan

The Company sponsors, and currently grants awards under, the Southwest Bancorporation of Texas, Inc. 1996 Stock Option Plan (the "Stock Option Plan"), which is a stock-based compensation plan as described below. The Company has also sponsored similar stock-based compensation plans in prior years.

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Notes to Consolidated Financial Statements — (Continued)

The Company applies the intrinsic value method in accounting for the Stock Option Plan and the Company's other prior stock-based compensation plans in accordance with Accounting Principles Board Opinion No. 25 ("APB 25"). In 1995, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 123, *Accounting for Stock-Based Compensation*, ("SFAS 123") which, if fully adopted by the Company, would change the method the Company applies in recognizing the expense of its stock-based compensation plans for awards subsequent to 1994. Adoption of the expense recognition provisions of SFAS 123 is optional and the Company decided not to elect these provisions of SFAS 123. However, pro forma disclosures as if the Company adopted the expense recognition provisions of SFAS 123 are required by SFAS 123 and are presented below.

The Stock Option Plan

Under the 1996 Stock Option Plan, the Company is authorized to issue up to 3,000,000 shares of common stock pursuant to "Awards" granted in the form of incentive stock options which qualify under Section 422 of the Internal Revenue Code of 1986, as amended (the "Code"), nonqualified stock options which do not qualify under Section 422 of the Code, and stock appreciation rights. Awards may be granted to selected employees and directors of the Company or any subsidiary. The Stock Option Plan provides that the exercise price of any incentive stock option may not be less than the fair market value of the common stock on the date of grant, and that the exercise price of any nonqualified stock option may be equal to, greater than or less than the fair market value of the common stock on the date of grant.

The Company granted 636,605, 353,893 and 640,552 stock options in 2000, 1999 and 1998, respectively. These stock options were granted with an exercise price, as determined in each individual grant agreement. The majority of the options granted vest over a five year period commencing on the date of grant (i.e., 60% vest on the third anniversary of the date of grant and 20% vest on each of the next two anniversaries of the date of grant) with the remaining options vesting over a period not to exceed five years.

In accordance with APB 25, compensation expense is recognized for discounted stock options granted and for performance-based stock options granted (but not for the nondiscounted stock options granted). The Company has recognized \$3, \$108 and \$172 of compensation expense in connection with these grants in 2000, 1999 and 1998, respectively.

A summary of the status of the Company's stock options as of December 31, 2000, 1999, and 1998 and the change during the years is as follows:

	2000		1999		1998	
	# Shares Underlying Options	Weighted Average Exercise Prices	# Shares Underlying Options	Weighted Average Exercise Prices	# Shares Underlying Options	Weighted Average Exercise Prices
Outstanding at beginning of the year	2,823,171	\$ 8.97	2,903,907	\$ 7.08	3,007,141	\$4.89
Granted at a discount	—	n/a	—	n/a	19,715	5.05
Granted at-the-money	636,605	19.19	353,893	14.35	620,837	8.16
Total granted	636,605	19.19	353,893	14.35	640,552	8.06
Exercised	(687,161)	5.26	(313,024)	3.32	(713,457)	1.26
Forfeited	(142,002)	15.66	(121,605)	12.71	(34,595)	6.10
Expired	—	n/a	—	n/a	—	n/a
Adjustment to conform reporting periods	—	n/a	—	n/a	4,266	5.86
Outstanding at end of year	2,630,613	\$12.06	2,823,171	\$ 8.97	2,903,907	\$7.08
Exercisable at end of year	1,671,146	\$ 9.09	1,425,698	\$ 6.06	986,807	\$6.32

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Notes to Consolidated Financial Statements — (Continued)

The fair value of each stock option granted is estimated on the date of grant using the Black-Scholes stock option valuation model with the following weighted-average assumptions for grants in 2000, 1999 and 1998: dividend yield of 0.00%; risk-free interest rates are different for each grant and range from 5.18% to 6.47%; the expected lives of options range from 5 to 6 years; and a volatility of 29.30%, 28.59% and 26.77% respectively. The weighted average fair value of options granted during the year is as follows:

	2000	1999	1998
Weighted-average fair value of options granted at a discount	n/a	n/a	\$4.71
Weighted-average fair value of options granted at-the-money	\$7.30	\$5.08	\$2.96
Weighted-average fair value of all options granted during the year	\$7.30	\$5.08	\$3.43

The following table summarizes information about stock options outstanding and exercisable at December 31, 2000:

Range of Exercise Prices	Options Outstanding			Options Exercisable	
	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
\$.20 to \$5.20	463,897	*	\$ 3.16	463,897	\$ 3.16
\$5.35 to \$11.16	810,424	5.7	8.54	739,561	8.51
\$11.72 to \$15.25	198,228	8.4	12.69	103,079	11.72
\$15.38 to \$20.19	1,133,364	9.1	17.74	364,609	17.07
\$20.20 to \$36.63	24,700	9.6	28.82	—	n/a
\$.20 to \$36.63	2,630,613	*	\$12.06	1,671,146	\$ 9.09

* All options, with an exercise price between \$.20 to \$5.20, are exercisable while the employee remains an employee at the Company and cease to be exercisable three months after termination of employment.

If the fair value based method of accounting under SFAS 123 had been applied, the Company's net income available for common shareholders and earnings per common share would have been reduced to the pro forma amounts indicated below (assuming that the fair value of options granted during the year are amortized over the vesting period):

	Year Ended December 31,		
	2000	1999	1998
Net income			
As reported	\$43,461	\$31,963	\$29,018
Pro forma	\$41,812	\$30,695	\$27,967
Basic earnings per common share			
As reported	\$ 1.34	\$ 1.01	\$ 0.97
Pro forma	\$ 1.29	\$ 0.97	\$ 0.94
Diluted earnings per common share			
As reported	\$ 1.29	\$ 0.97	\$ 0.91
Pro forma	\$ 1.24	\$ 0.93	\$ 0.88

The effects of applying SFAS 123 in the above pro forma disclosure are not indicative of future amounts. The Company anticipates making awards in the future under its stock-based compensation plans.

Benefit Plans

The Company has adopted a contributory profit sharing plan pursuant to Internal Revenue Code Section 401(k) covering substantially all employees (the "401-K Plan"). Each year the Company determines, at its discretion, the amount of matching contributions. The Company presently matches 100% of the employee contributions not to exceed

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Notes to Consolidated Financial Statements — (Continued)

5.0% of the employee's annual compensation. Total plan expense charged to the Company's operations for the years ended December 31, 2000, 1999 and 1998 was \$1,744, \$1,374 and \$972, respectively.

The 401-K Plan allows for the Company to contribute up to 500,000 shares of common stock of the Company (valued at the approximate fair market value on the date of contribution) instead of cash. A total of 4,431 shares at \$16.58 were issued to the 401-K Plan during the year ended December 31, 1999. No shares were issued to the 401-K Plan in 2000 and 1998.

Prior to December 31, 2000, Citizens had a defined benefit pension plan covering substantially all of their employees. The benefits under the plan were based on years of service and the employee's final average monthly compensation. Effective December 31, 2000, the Company curtailed the defined benefit pension plan. Pursuant to the curtailment, no further benefits will be accrued under the plan from and after December 31, 2000 and no individual who is not currently a participant in the plan shall be eligible to become a participant in the plan. Each participant who is an employee at December 31, 2000 became 100% vested in their accrued benefit on December 31, 2000.

The three wholly-owned subsidiary banks of Citizens had a profit sharing plan covering substantially all of their employees. The profit sharing plan was funded on an annual basis as determined by the Banks' Boards of Directors. Contributions to the profit sharing plan were \$573, \$681 and \$655 for the years ended December 31, 2000, 1999 and 1998, respectively. Effective October 1, 2000, the profit sharing plan was converted to a 401(k) plan.

11. Earnings Per Common Share:

Earnings per common share is computed as follows:

	Year Ended December 31,		
	2000	1999	1998
Net income	\$43,461	\$31,963	\$29,018
Interest on 8% convertible debentures, net of tax	—	—	516
Minority interest in net income of Mitchell, net of tax	—	—	246
Net income, adjusted	\$43,461	\$31,963	\$29,780
Divided by average common shares and common share equivalents:			
Average common shares	32,397	31,743	29,794
Average common shares issuable under the stock option plan	1,232	1,200	1,300
Average common shares issuable with the conversion of the 8% convertible debentures	—	—	1,351
Average common shares issuable with the conversion of the minority interest of Mitchell	—	—	296
Total average common shares and common share equivalents	33,629	32,943	32,741
Basic earnings per common share	\$ 1.34	\$ 1.01	\$ 0.97
Diluted earnings per common share	\$ 1.29	\$ 0.97	\$ 0.91

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Notes to Consolidated Financial Statements — (Continued)

12. Commitments and Contingencies:

Litigation

The Company is involved in various litigation that arise in the normal course of business. In the opinion of management of the Company, after consultation with its legal counsel, such litigation will not have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows.

Leases

At December 31, 2000, the Company has certain noncancelable operating leases which cover the Company's premises with approximate future minimum annual rental payments as follows:

2001	\$ 5,196
2002	4,910
2003	4,664
2004	4,564
2005	4,494
Thereafter	9,934
	<hr/>
	\$33,762

Rent expense was \$4,672, \$3,937 and \$3,057 for the years ended December 31, 2000, 1999 and 1998, respectively.

13. Regulatory Capital Compliance:

The Company and the Bank are subject to regulatory risk-based capital requirements that assign risk factors to all assets, including off-balance sheet items such as loan commitments and standby letters of credit. Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional discretionary, actions by regulators that, if undertaken, could have a direct material effect on the Company's consolidated financial statements. Capital is separated into two categories, Tier 1 and Tier 2, which combine for total capital. At December 31, 2000, the Company's and Bank's Tier 1 capital consists of their respective shareholders' equity adjusted for minority interest in equity accounts of consolidated subsidiaries, goodwill, and various other intangibles and Tier 2 consists of the allowance for loan losses subject to certain limitations. The guidelines require total capital of 8% of risk-weighted assets.

In conjunction with risk-based capital guidelines, the regulators have issued capital leverage guidelines. The leverage ratio consists of Tier 1 capital as a percent of average assets. The minimum leverage ratio for all banks is 3%, with a higher minimum ratio dependent upon the condition of the individual bank. The 3% minimum was established to make certain that all banks have a minimum capital level to support their assets, regardless of risk profile.

As of December 31, 2000, the most recent notification from the regulators categorized the Bank and the Company as "well capitalized" under the regulatory framework for prompt corrective action. There are no conditions or events since that notification that management believes have changed the category.

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Notes to Consolidated Financial Statements — (Continued)

The following table compares the Company's and the Bank's leverage and risk-weighted capital ratios as of December 31, 2000 and 1999 to the minimum regulatory standards:

	Actual		Minimum Capital Requirements		Minimum To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2000						
Total Capital (to Risk Weighted Assets):						
The Company	\$318,039	10.49%	\$242,590	8.00%	\$303,238	10.00%
The Bank	332,092	11.03%	240,954	8.00%	301,193	10.00%
Tier I Capital (to Risk Weighted Assets):						
The Company	289,889	9.56%	121,295	4.00%	242,590	8.00%
The Bank	303,616	10.08%	120,477	4.00%	240,954	8.00%
Tier I Capital (to Average Assets):						
The Company	289,889	7.71%	112,867	3.00%	188,111	5.00%
The Bank	303,616	8.12%	112,199	3.00%	186,998	5.00%
As of December 31, 1999						
Total Capital (to Risk Weighted Assets):						
The Company	267,837	10.61%	201,968	8.00%	252,460	10.00%
The Bank	270,426	10.71%	201,956	8.00%	252,445	10.00%
Tier I Capital (to Risk Weighted Assets):						
The Company	245,401	9.72%	100,984	4.00%	201,968	8.00%
The Bank	248,485	9.84%	100,978	4.00%	201,956	8.00%
Tier I Capital (to Average Assets):						
The Company	245,401	7.81%	94,208	3.00%	157,013	5.00%
The Bank	248,485	7.88%	94,606	3.00%	157,677	5.00%

The Company and the Bank are also subject to certain restrictions on the amount of dividends that they may declare without prior regulatory approval.

14. Financial Instruments with Off-Balance Sheet Risk and Concentrations of Credit Risk:

The Company is party to financial instruments with off-balance sheet risk in the normal course of business in order to meet the financing needs of its customers. These financial instruments, which are for purposes other than trading, include loan commitments, letters of credit, commitments to sell mortgage loans to permanent investors, purchased option contracts and financial guarantees on GNMA mortgage-backed securities administered. These financial instruments involve, to varying degrees, elements of credit risk in excess of the amounts recognized in the financial statements.

The Company's exposure to credit loss in the event of nonperformance by the other party to the loan commitments and letters of credit is limited to the contractual amount of those instruments. The Company uses the same credit policies in evaluating loan commitments and letters of credit as it does for on-balance sheet instruments. In order to control the credit risk associated with entering into commitments, the Company subjects such activity to the same credit quality and monitoring controls as its lending activities. For commitments to sell mortgage loans to permanent investors, the contract amounts do not represent exposure to credit loss. For purchased put options, the Company's exposure is limited to the option premium paid, not the notional amount of the option. For GNMA mortgage-backed securities administered, the contract amount administered exceeds the Company's exposure to credit loss.

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Notes to Consolidated Financial Statements — (Continued)

The approximate amounts of financial instruments with off-balance sheet risk are as follows:

	December 31, 2000 Contract Amount	December 31, 1999 Contract Amount
Loan commitments including unfunded lines of credit	\$1,140,589	\$1,033,780
Standby letters of credit	100,420	72,391
Commercial letters of credit	4,839	2,357
Commitments to sell mortgage loans	5,991	1,671
Option contracts	2,000	1,000
Guarantees on GNMA securities administered	90,656	101,596

Loan commitments are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee.

Since many of the loan commitments and letters of credit may expire without being drawn upon, the total commitment amount does not necessarily represent future cash requirements. Standby letters of credit are conditional commitments by the Company to guarantee the performance of a customer to a third party.

The Company evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation of the counterparty. Collateral held varies but may include certificates of deposit, accounts receivable, inventory, property, plant and equipment, and real property.

Commitments to sell mortgage loans to permanent investors are contracts in which the Company agrees to deliver mortgage loans at specific future dates at specified prices or yields. Risks arise from the possible inability of counterparties to meet the terms of their contracts and from movements in interest rates.

The Company purchases option contracts on FNMA or FHLMC guaranteed mortgage backed securities to reduce the Company's exposure to the effects of fluctuations in interest rates on the Company's lending and secondary marketing activities. The time value portion of option premiums paid is recorded in other assets and is amortized to expense over the term of the option. Changes in the intrinsic value of options are deferred and recognized as the related mortgage loans are sold.

The Company administers GNMA mortgage-backed securities on which it guarantees payment of monthly principal and interest to the security holders. The underlying loans are supported by FHA and VA mortgage insurance and are collateralized by real estate. In the event of mortgagor default, losses may arise from principal, interest or other costs which may exceed reimbursement limitations established by FHA or VA.

The Company originates real estate, commercial, construction and consumer loans primarily to customers in the greater Houston, Texas area. Although the Company has a diversified loan portfolio, a substantial portion of its customers' ability to honor their contracts is dependent upon the local Houston economy and the real estate market.

The Company maintains funds on deposit at correspondent banks which at times exceed the federally insured limits. Management of the Company monitors the balance in these accounts and periodically assesses the financial condition of correspondent banks.

15. Fair Values of Financial Instruments:

The fair value of financial instruments provided below represents estimates of fair values at a point in time. Significant estimates regarding economic conditions, loss experience, risk characteristics associated with particular financial instruments and other factors were used for the purposes of this disclosure. These estimates are subjective in

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Notes to Consolidated Financial Statements — (Continued)

nature and involve matters of judgment. Therefore, they cannot be determined with precision. Changes in the assumptions could have a material impact on the amounts estimated.

While the estimated fair value amounts are designed to represent estimates of the amounts at which these instruments could be exchanged in a current transaction between willing parties, many of the Company's financial instruments lack an available trading market as characterized by willing parties engaging in an exchange transaction. In addition, it is the Company's intent to hold most of its financial instruments to maturity and, therefore, it is not probable that the fair values shown will be realized in a current transaction.

The estimated fair values disclosed do not reflect the value of assets and liabilities that are not considered financial instruments. In addition, the value of long-term relationships with depositors (core deposit intangibles) and other customers is not reflected. The value of these items is significant.

Because of the wide range of valuation techniques and the numerous estimates which must be made, it may be difficult to make reasonable comparisons of the Company's fair value information to that of other financial institutions. It is important that the many uncertainties discussed above be considered when using the estimated fair value disclosures and to realize that because of these uncertainties, the aggregate fair value amount should in no way be construed as representative of the underlying value of the Company.

The following methods and assumptions were used by the Company in estimating its fair value disclosures for financial instruments:

Cash and Cash Equivalents: The carrying amounts for cash and cash equivalents approximate their fair values.

Securities: Fair values for investment securities are based on quoted market prices. The fair value of stock in the Federal Home Loan Bank of Dallas and the Federal Reserve Bank Stock is estimated to be equal to its carrying amount given it is not a publicly traded equity security, it has an adjustable dividend rate, and transactions in the stock are executed at the stated par value.

Loans Held for Sale: Fair values of loans held for sale are estimated based on outstanding commitments from investors or current market prices for similar loans.

Loans and Accrued Interest Receivable: For variable-rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values. The fair value of all other loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Fair values for impaired loans are estimated using discounted cash flow analyses or underlying collateral values, where applicable. The carrying amount of accrued interest approximates its fair value.

Off-Balance-Sheet Instruments: The fair values of the Company's lending commitments, letters of credit, commitments to sell loans and guarantees are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing. The fair value of the Company's option contracts are based on the estimated amounts the Company would receive from terminating the contracts at the reporting date.

Deposit Liabilities and Accrued Interest Payable: The fair values disclosed for demand deposits (e.g., interest and noninterest checking and money market accounts) are, by definition, equal to the amount payable on demand at the reporting date. Fair values for fixed-rate time deposits are estimated using a discounted cash flow analysis, using interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits. The carrying amount of accrued interest approximates its fair value.

Borrowings: The carrying amounts of federal funds purchased, securities sold under repurchase agreements, and other borrowings approximate their fair values.

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Notes to Consolidated Financial Statements — (Continued)

The following table summarizes the carrying values and estimated fair values of financial instruments (all of which are held for purposes other than trading):

	December 31, 2000		December 31, 1999	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Assets				
Cash and due from banks	\$ 331,965	\$ 331,965	\$ 188,432	\$ 188,432
Fed funds sold and other cash equivalents	79,341	79,341	25,642	25,642
Securities available for sale	848,164	848,164	831,425	831,425
Securities held to maturity	—	—	58,944	57,941
Loans held for sale	85,939	86,855	77,047	77,047
Loans held for investment, net	2,397,348	2,476,656	1,935,859	1,871,059
Accrued interest receivable	27,334	27,334	20,492	20,492
Liabilities				
Deposits	3,093,870	2,924,330	2,531,633	2,527,488
Securities sold under repurchase agreements	211,800	211,800	216,838	216,838
Other borrowings	305,961	305,961	267,140	267,140
Accrued interest payable	5,505	5,505	4,072	4,072

The fair value of the Company's off-balance sheet instruments was immaterial at December 31, 2000 and 1999.

16. Supplemental Cash Flow Information:

The supplemental cash flow information for the years ended December 31, 2000, 1999, and 1998 is as follows:

	December 31,		
	2000	1999	1998
Cash paid for interest	\$120,229	\$85,847	\$71,114
Cash paid for income taxes	21,400	18,691	12,450
Non-cash investing and financing activities:			
Tax benefit related to the exercise of certain stock options	5,075	967	1,800
Subordinated debentures converted to common stock	—	—	10,857
Loans transferred to foreclosed real estate	411	1,326	61
Dividends declared but unpaid	—	782	587
Issuance of common stock to Fort Bend Retirement Retention Plan	—	—	58
Reduction of debt in prior Fort Bend Employee Stock Option Plan	—	—	79
Issuance of common stock in exchange for 49% ownership interest in Mitchell	—	2,575	—
Transfer of securities from held to maturity to available for sale	55,800	57,800	—

REPORT OF INDEPENDENT ACCOUNTANTS ON FINANCIAL STATEMENT SCHEDULE

To the Board of Directors and Shareholders
Southwest Bancorporation of Texas, Inc.:

Our audits of the consolidated financial statements referred to in our report dated February 23, 2001 of Southwest Bancorporation of Texas, Inc. and Subsidiaries included on page F-2 of this Form 10-K also included an audit of the financial statement schedule listed in the index on page F-1 of this Form 10-K. In our opinion, this financial statement schedule presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements.

PricewaterhouseCoopers LLP

Houston, Texas
February 23, 2001

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Schedule I — Parent Company Condensed Financial Statements
Condensed Balance Sheet
(in thousands, except share amounts)

	December 31,	
	2000	1999
ASSETS		
Cash and cash equivalents	\$ 4,126	\$ 4,527
Securities — available for sale	1,189	406
Investment in subsidiary	300,875	227,010
Other assets	4,935	1,941
Total assets	\$311,125	\$233,884
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities:		
Other borrowings	\$ 13,000	\$ —
Other liabilities	—	808
Total liabilities	13,000	808
Shareholders' equity:		
Common stock — \$1 par value, 75,000,000 shares authorized; 32,705,909 issued and 32,704,877 outstanding at December 31, 2000 and 32,877,395 issued and 32,028,726 outstanding at December 31, 1999	32,706	32,877
Additional paid-in capital	69,735	62,229
Retained earnings	198,835	157,716
Accumulated other comprehensive loss	(3,107)	(15,770)
Treasury stock, at cost — 1,032 shares and 848,669 shares, respectively	(44)	(3,976)
Total shareholders' equity	298,125	233,076
Total liabilities and shareholders' equity	\$311,125	\$233,884

These condensed financial statements should be read in conjunction with the Consolidated Financial Statements and Notes thereto of Southwest Bancorporation of Texas, Inc. and Subsidiaries included herein.

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Schedule I — Parent Company Condensed Financial Statements (Continued)
Condensed Statement of Income and Comprehensive Income
(in thousands)

	Year Ended December 31,		
	2000	1999	1998
Interest income:			
Loans	\$ —	\$ —	\$ 76
Securities	103	63	26
Total interest income	103	63	102
Interest expense on borrowings	760	120	717
Net interest income (expense)	(657)	(57)	(615)
Other operating income	15	7	14
Operating expenses	705	632	1,002
Equity in income of subsidiary	44,380	32,423	30,084
Income before income taxes	43,033	31,741	28,481
Income tax benefit	(428)	(222)	(537)
Net income	43,461	31,963	29,018
Other comprehensive income, net of tax:			
Net unrealized appreciation (depreciation) on securities available for sale	12,633	(18,707)	2,540
Comprehensive income	\$56,094	\$ 13,256	\$31,558

These condensed financial statements should be read in conjunction with the
Consolidated Financial Statements and Notes thereto of
Southwest Bancorporation of Texas, Inc. and Subsidiaries included herein.

Southwest Bancorporation of Texas, Inc. and Subsidiaries
Schedule I — Parent Company Condensed Financial Statements (Continued)
Condensed Statement of Cash Flows
(in thousands)

	Year Ended December 31,		
	2000	1999	1998
Cash flows from operating activities:			
Net income	\$ 43,461	\$ 31,963	\$ 29,018
Adjustments to reconcile net income to net cash provided by operating activities:			
Equity in undistributed income of subsidiary	(40,680)	(28,120)	(24,502)
Depreciation and amortization	32	33	32
Decrease in accrued interest receivable, prepaid expenses and other assets	2,994	585	566
Decrease in accrued interest payable and other liabilities	(808)	(14)	(262)
Other, net	778	57	—
Adjustment to conform reporting periods	—	—	100
Net cash provided by operating activities	5,777	4,504	4,952
Cash flows from investing activities:			
Proceeds from maturity of securities available for sale	—	—	500
Purchase of securities available for sale	(3,473)	(24,567)	—
Sales of securities available for sale	2,690	24,161	—
Investments in subsidiaries	(18,840)	(39,000)	(1,800)
Return of capital from subsidiaries	—	25,500	—
Net cash used in investing activities	(19,623)	(13,906)	(1,300)
Cash flows from financing activities:			
Net change in other borrowings	13,000	—	—
Payments of dividends on common stock by Fort Bend Holding Corp.	—	(277)	(723)
Payments of dividends on common stock by Citizens Bankers, Inc.	(3,124)	(2,739)	(3,132)
Net proceeds from issuance of common stock	3,685	1,236	2,370
Purchase of treasury stock	(116)	—	(55)
Other, net	—	(59)	—
Adjustment to conform reporting periods	—	—	143
Net cash provided by (used in) financing activities	13,445	(1,839)	(1,397)
Net increase (decrease) in cash and cash equivalents	(401)	(11,241)	2,255
Cash and cash equivalents at beginning of period	4,527	15,768	13,513
Cash and cash equivalents at end of period	\$ 4,126	\$ 4,527	\$ 15,768

These condensed financial statements should be read in conjunction with the Consolidated Financial Statements and Notes thereto of Southwest Bancorporation of Texas, Inc. and Subsidiaries included herein.

CONSENT OF INDEPENDENT ACCOUNTANTS

We hereby consent to the incorporation by reference in the Registration Statements on Form S-8 (File Nos. 333-21619, 333-27891, 333-33533, 333-55685 and 333-76269) of Southwest Bancorporation of Texas, Inc. of our reports, dated February 23, 2001, relating to the consolidated financial statements and financial statement schedule, which appear in this Form 10-K.

We hereby consent to the incorporation by reference in the Registration Statements on Form S-3 (File Nos. 333-53162 and 333-80603) of Southwest Bancorporation of Texas, Inc. of our reports dated February 23, 2001, relating to the consolidated financial statements and financial statement schedule, which appear in this Form 10-K. We also consent to the reference to us under the heading "Experts" in such Registration Statements.

PricewaterhouseCoopers LLP

Houston, Texas

March 1, 2001

Southwest Bancorporation of Texas, Inc.
Post Office Box 27459
Houston, Texas 77227-7459