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COMMODITIES

As Oil Price Drops, Texas Lenders Watch for Fallout

Small Banks Brace for Hit to Local Businesses of Any Cutback in Crude Production

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As Oil Price Drops, Texas Lenders Watch for Fallout- WSJ



Banker Hugh B. "Trip" Ruckman III hasn't lent large sums to the drillers dotting the Texas landscape near Karnes City. But his bank has lent to small hotels that rely on oilworkers for much of their business. *PHOTO: BEN SKLAR FOR THE WALL STREET JOURNAL*

KARNES CITY, Texas- Hugh B. "Trip" Ruckman III's family ties to the Karnes County National Bank date to 1901 when it started making loans to cattle ranchers and farmers in this rural community in South Texas.

The mobile-home camps and sandstone-colored motels along Highway 181, where some rooms regularly cost more than high-rise hotel rooms in Houston and San Antonio, are newer additions to the local economy. So are the IS-wheelers that race down the streets and the mud-splattered pickup trucks that fill the Dairy Queen parking lot at lunchtime, their sides dotted with energy-company logos.

Mr. Ruckman's community bank doesn't lend much to the energy companies whose drilling sites dot the local landscape, tapping the Eagle Ford Shale oil deposits of South Texas-but he still has reason to be concerned about the recent slump in oil prices. Some 10% of Karnes County National Bank's loans are held by small hotels, many of whose prospects are tied to the energy boom.

For now, he says, occupancy rates remain high and there are few indications that oil-field workers are packing up and moving out. "I hope I don't eat my words," said Mr. Ruckman, 70 years old, who is president of the bank.

Oil and natural gas are old hat in Texas, of course, but the shale revolution brought new prosperity to parts of the state-and the country-that haven't experienced an energy bust in all its gory details.

Oil prices have dropped by roughly half since last summer, pressured by a glut that is outstripping demand. That has created an unfamiliar anxiety for many bankers with loans tied to the energy boom, even if indirectly.

The

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drilling boom that lasted most of the last decade was financed largely by private-equity firms and bond deals-not the local and regional banks that typically provided money to independent exploration firms in generations past. Yet analysts say a sustained price drop creates vulnerability for small and midsize lenders whose customers provide a range of ancillary services, from the carwashes that scrub the trucks to the hotels that

house the workers.

The impact of the energy swoon on those businesses is in many ways more difficult to predict. So far, many energy bankers say, the mood is cautiously optimistic that a catastrophe isn't looming.

"Obviously, it's not a bed of roses, but it's not as bad as people think," said Randy Gartz, a longtime energy banker at the Mutual of Omaha Bank in Houston.

Mr. Gartz is among the veteran bankers with acute memories of the late 1980s, when about 700 banks and thrifts failed in Texas after oil prices dropped more than 50%. He and his partner, Mike Turner, say they are making more frequent calls to their customers in the oil-field services business to check on the status of their contracts and get updated business projections.

Bankers have already started warning customers that credit lines may be reduced in coming months, especially if prices slide further. And they are lowering their own internal projections for oil prices to see how their portfolios will perform in a worst-case scenario.

At Atwood Oceanics Inc., a Houston-based company that has delayed delivery of two rigs because of the price slide, the firm's longtime bankers recently called on Mark Mey, the company's chief financial officer, when they were in town on an unrelated matter. Over sushi at a Houston restaurant, they peppered Mr. Mey with questions about the industry and his competitors.

"They were seeking intelligence," said Mr. Mey of the five bankers, whom he declined to identify other than saying they work for a European bank.

At Cadence Bank in Houston, clients that bankers used to call twice a year are hearing from the bank every six weeks. "Clients know that credit lines are coming down, but they want to know by how much," said Paul Murphy, chairman of the regional bank, which has more than \$7 billion in assets.

Mr. Murphy and his energy bankers say they are keeping close tabs on six or seven clients that could run into trouble. "We recognize that risk is elevated, but we're not panicked," Mr. Murphy said.

Regulators are also paying close attention. The Office of the Comptroller of the Currency, which regulates the largest U.S. banks and about 1,400 smaller financial

institutions, conducted two reviews of banks' exposure to energy prices in 2014 and has zeroed in on about 10 that have significant exposure to the oil and gas sector.



Mr. Ruckman near a hotel project that his bank has helped fund. The bank's hotel loans are gold-plated," he says, but "as we go forward, we're keeping a real close eye on them." PHOTO: BEN SKLAR FOR THE WALL STREET JOURNAL

At the same time, the Texas Department of Banking is monitoring the state's 15 banks that have assets below \$1 billion and which are believed to be heavily focused on the energy industry. The department, which oversees 273 banks, so far has focused on

three for closer scrutiny.

Charles Cooper, commissioner of the Texas regulatory agency, said in an interview that his office is "not pushing the panic button by any means."

In Karnes County, many residents have collected royalty checks that reached into the six and seven figures, helping Karnes County National's deposits explode to \$351 million from \$80 million in 2010.

"They bought new cars, fixed their fences, maybe redid the kitchen and then brought the rest of the money to the bank," said Mr. Ruckman, the bank president.

Even Karnes County National gets royalty checks, amounting to several thousand dollars a month, because two of its branches sit on top of the Eagle Ford Shale.

Houston developer Bob Keener and his partners borrowed some money from Karnes County National Bank to build a 48-room hotel, the Kenedy Lodge, in March 2013 just as production was exploding. After reaching as high as \$169 a night, prices and occupancy levels are down somewhat lately, Mr. Keener said.

He isn't worried about having trouble paying back his loan, saying "everything is fine as far as that goes." He declined to say how much he borrowed but said about 40% of the loan remains outstanding.

His banker, Mr. Ruckman, is hopeful that everything stays fine. The bank's hotel loans are "gold-plated," he said, but "as we go forward, we're keeping a real close eye on them."

-Ryan Tracy contributed to this article.

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