

TRB | SHAREHOLDER REPORT

Vol. 7 Issue 2



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Strong asset growth has become a hallmark of Texas Regional Bank and continued in 2016. By year-end, assets will exceed the \$600 million mark; loans will settle in about \$340 million. Most impressively, Texas Regional Bank is on course to outperform prior year earnings by more than 60%. After five years of record growth and investment in building the company's infrastructure, we worked diligently to refine operations, flatline expenses, and improve revenue in all areas. The end result is after-tax revenue of approximately \$3.5 million for 2016, \$1.3 million ahead of 2015.

In 2016, Texas Regional Bank continued to expand client services. The Trust and Wealth Management Division established many new relationships during the year and outperformed its peers in every regard. TRB Mortgage launched in September and, much like Wealth Management, will be a tremendous complement to core banking. The group closed its first loan in October and has built a solid closing pipeline for the months ahead.

Several new locations are on the horizon. We are close in negotiations on a second Edinburg location and are looking for an additional site in Brownsville as well. We anticipate breaking ground on our Harlingen Main facility at the Expressway and Stuart Place Road in the first quarter of 2017, with completion in early 2018. We believe TRB is ready to expand outside the region and continually assess opportunities in markets that would complement our Valley operations and provide geographic diversification.

Great people have made Texas Regional Bank what it is today and will continue to be the foundation of our success. We are proud to have assembled an exceptional team and grateful for the many contributions of our shareholders.

Thank you for your continued enthusiasm for and support of Texas Regional Bank.

MICHAEL SCAIEF
CHAIRMAN

We take pride in sharing with community members and business partners the exciting and exceptional growth Texas Regional Bank (TRB) is experiencing.

In 2016, the TRB team worked particularly hard to expand our presence within the business community. Our new ConnectBanking program included visiting employers and introducing them to the many customized and convenient TRB products and services designed to meet specific industry needs. A first-of-its-kind Sales Campaign launched in mid-August involved staff at all levels in selling the bank, resulting in 400 new accounts over a five-week span.

The 2016 Sales Campaign was a success on many levels. Aside from increasing deposits and the loan-prospect pipeline, it provided staff in all of our markets with a greater understanding of TRB products and services, and experience developing and reaching self-set goals. Our sales team played a pivotal role in guiding each market on best practices, outreach and follow-up, enabling all to reach their highest selling potential.

TRB's rising trajectory is due to our strong commitment to the business industry and the people we serve. We continue to gain exposure within our communities by offering our time and energy to various non-profit organizations that help our area in so many ways. You can learn more about our dedication to specific organizations on page 14.

Our momentum is great and already we are planning toward a successful 2017.

PAUL MOXLEY
CEO/PRESIDENT

The lending team at Texas Regional Bank has succeeded at almost all we set out to accomplish. Our objective has been steady growth of the loan base and 2016 proved to be another great year. With the support of an excellent loan operations and credit team, we expanded our presence in the newest TRB markets, while deepening roots in our original locations.

In 2016, as we expanded roles and capacity within the Texas Regional Bank team, the lending team's wealth of knowledge and years of experience were critical to creating a more efficient system with many customer benefits. One example is the Business Loan Advantage, a new product that was rolled out in the second quarter. By streamlining the small business loan process, it has enabled us to deliver timely credit decisions to borrowers.

The Texas Regional Bank lending team will continue to cultivate strong, long-lasting relationships with our customers. Partnering with our front-line staff and sales team, we are committed to delivering a robust portfolio of innovative products and services.



BRENT BALDREE
CHIEF LENDING OFFICER

In 2016, Texas Regional Bank Operations continued to focus on improving efficiency and service, developing products, and utilizing the technology expected in today's financial sector. Our priority is to consistently improve delivery of service by whatever means our customers prefer. Whether via remote access or face-to-face with a full-service, universal banker, we remain committed to helping our clients succeed.

Cyber security continues to have our undivided attention. We have taken a pro-active approach to strengthen TRB defenses against cyber attacks and to educate our team, our customers, and our community to be mindful of the risks and vulnerabilities we face daily.

As the bank experiences growth in every column, we are highly motivated to maintain the trust of all we serve and continually strive to outperform our own expectations, those of our customers, and those of our shareholders.



MICHAEL LAMON
CHIEF OPERATIONS OFFICER

In 2016, Texas Regional Bank focused on building its core assets and creating long-term shareholder value. As we expanded the TRB footprint, we invested in building infrastructure to support a sound organization and meaningful customer relationships.

Growing the loan portfolio with quality assets is important for our continued success. Loans continue to be the highest yielding investment for Texas Regional Bank. Through the first three quarters of 2016 we have had excellent growth with the loan portfolio reaching \$330 million.

We are on track to record net income and are excited to report our 2016 figures very soon. The improved earnings are a direct result of the strong loan growth, the redeployment of very liquid and low-yielding investments into higher-yielding securities, and better control of operating expenses.



MARK RAMIREZ
CHIEF FINANCIAL OFFICER

The people you know.

Could This Be the End of the Texas Slump?

Regional economic activity appears to be improving, and the oil-driven slump may be nearing an end.

Texas job growth continues to accelerate, rising an annualized 2.1 percent in September and lifting year-to-date growth to an annualized 1.4 percent. After incorporating the second-quarter early benchmark, the Dallas Fed revised its forecast for 2016 employment growth up to 1.5 percent (December/December), which, if it comes to fruition, would surpass last year's 1.3 percent increase. If there are additional downward revisions to state employment data, like those in the first half of the year, third-quarter growth could come in weaker than the current 2.6 percent increase.

Job losses in the oil and manufacturing sectors have started to slow, and the Texas Manufacturing Outlook Survey (TMOS) production index has remained in positive territory for the past four months, suggesting that the manufacturing sector may soon see a turnaround.

The unemployment rate moved up again, to 4.8 percent in September, 0.5 percentage points above its low of 4.3 percent in March but still below the U.S. rate. The most recent increase reflects people entering the workforce, perhaps because hiring conditions have recently improved.

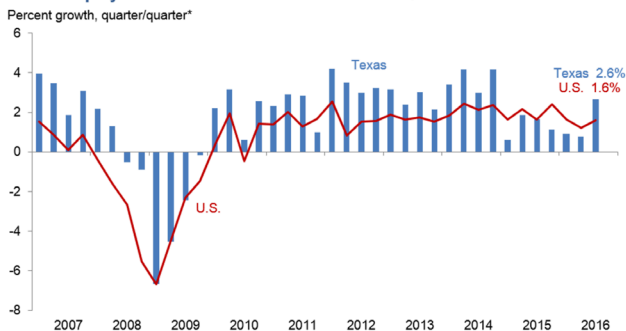
Texas Employment Growth Rallies in Third Quarter

The pace of Texas job growth more than tripled in the third quarter, reaching an annualized 2.6 percent and outpacing the nation by a percentage point (Chart 1). Third-quarter growth was a substantial improvement over first- and second-quarter growth at 0.9 percent and 0.8 percent, respectively.

Most major Texas metros saw a pickup in employment growth in the third quarter compared with the first half of the year. The largest gains were in Dallas at 5.0 percent and Fort Worth at 4.3 percent (annualized). Houston saw a stark turnaround; employment expanded 1.9 percent in the third quarter after contracting an annualized 1.0 percent through June.

Incorporating the second-quarter early benchmark revision into Texas employment data wiped out gains the energy sector had previously posted in the preliminary August data. While the energy and manufacturing sectors continue to shed jobs, the pace of losses slowed in the third quarter. Construction, along with most of the service sectors, saw strong job growth in the quarter.

Chart 1
Texas Employment Growth Races Ahead in Third Quarter



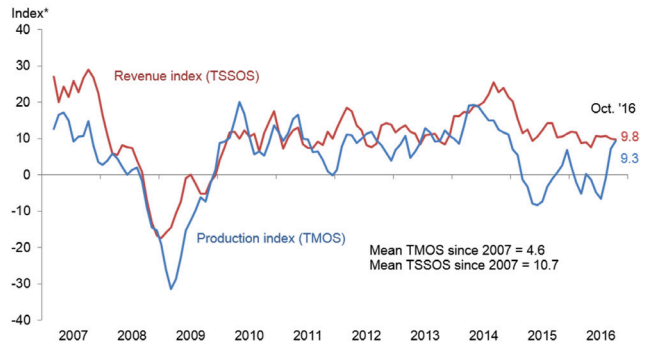
*Seasonally adjusted, annualized rate.
NOTES: Quarterly data are the last month of the quarter; average annual growth since 1990: U.S. 1.1 percent, Texas 2.1 percent.
SOURCES: Bureau of Labor Statistics; Texas Workforce Commission; seasonal and other adjustments by the Federal Reserve Bank of Dallas.

Dallas Fed Surveys Show Possible Manufacturing Turnaround

Headline indexes from the Dallas Fed's Texas Business Outlook Survey show continued strength in the service sector and accelerating growth in manufacturing activity in October (Chart 2). This is potentially good news for the state's manufacturing sector, which contracted through most of 2015 and the first half of 2016.

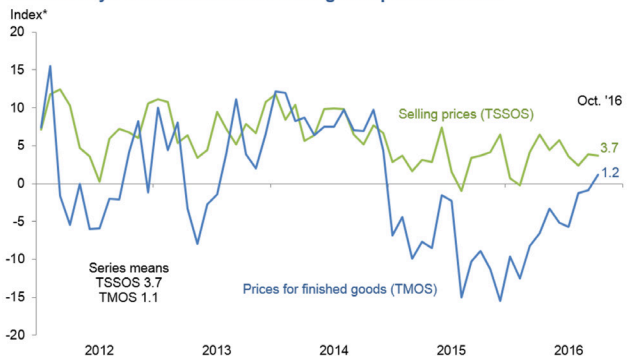
Another positive sign is that deflationary pressures that have plagued manufacturers since early 2015 may be dissipating, according to TMOS (Chart 3). October was the first month since December 2014 that the TMOS index of prices received for finished goods was positive. Selling prices in the service sector have continued to increase at an average pace.

Chart 2
Survey Indexes Show Manufacturing Rebounding, Services Still Growing



*Seasonally adjusted; three-month moving average.
SOURCE: Federal Reserve Bank of Dallas' Texas Manufacturing Outlook Survey (TMOS) and Texas Service Sector Outlook Survey (TSSOS).

Chart 3
Deflationary Pressures in Manufacturing Dissipate in October



*Seasonally adjusted.
SOURCE: Federal Reserve Bank of Dallas' Texas Manufacturing Outlook Survey (TMOS) and Texas Service Sector Outlook Survey (TSSOS).



Home Prices, Apartment Rents Continue to Rise

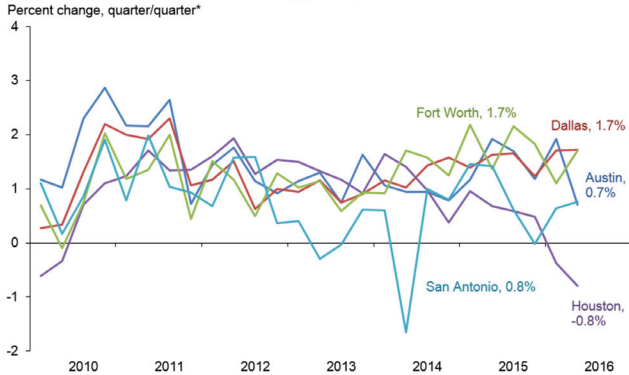
Despite the state's energy woes the past two years, housing markets remain robust, with the possible exception of Houston's. The Texas median single-family home price rose 6.1 percent year over year in September, faster than the nation's 4.2 percent increase. Inventories remained low at 3.7 months of supply. Tight inventories and strong demand for single-family homes have led to the rapid price appreciation over the past four years.

Prices are rising in part due to the shift in composition of homes sold, according to a new article from the Texas A&M Real Estate Center, produced jointly with the Dallas Fed.[1]

Sales of entry-level homes—those priced under \$200,000—dropped from 69 percent of total sales in 2011 to 47 percent this year. This drop is even more exaggerated across most of the major Texas metros, with Austin by far seeing the greatest shift away from homes sold in the entry-level range.

The Texas apartment market has seen increases in rents, but unlike single-family construction, multifamily construction has been robust during the recovery from the Great Recession. Despite a near-record number of units coming online, both Dallas and Fort Worth posted 1.7 percent growth in apartment rents in the second quarter over the first (Chart 4). Houston, however, has seen declining rents and occupancy rates.

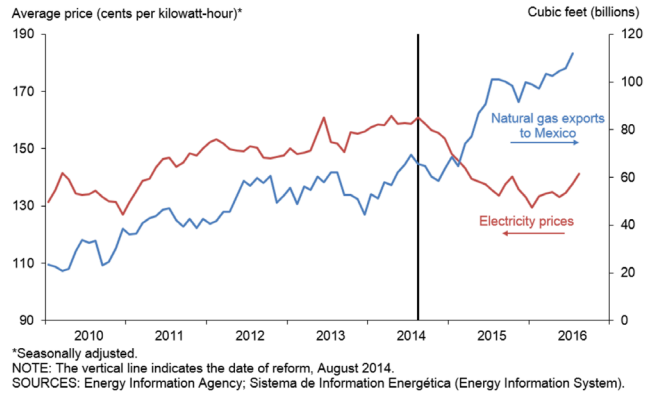
Chart 4
Apartment Rents Continue Climbing, Except in Houston



Texas Exporting 15 Percent of Its Natural Gas Production to Mexico

Texas is exporting an increasing volume of natural gas to Mexico. These exports now account for about 15 percent of the state's natural gas production. With the completion of new pipelines and the deregulation of Mexico's electricity markets in mid-2014, U.S. natural gas exports to Mexico have increased 71 percent; over the same period, average electricity prices in Mexico have fallen 12 percent, from 161 to 141 cents per kilowatt-hour (Chart 5). About 78 percent of U.S. exports were from Texas in July.

Chart 5
Mexico's Energy Reform Leads to Electricity Price Declines, Rising Natural Gas Imports from the U.S.



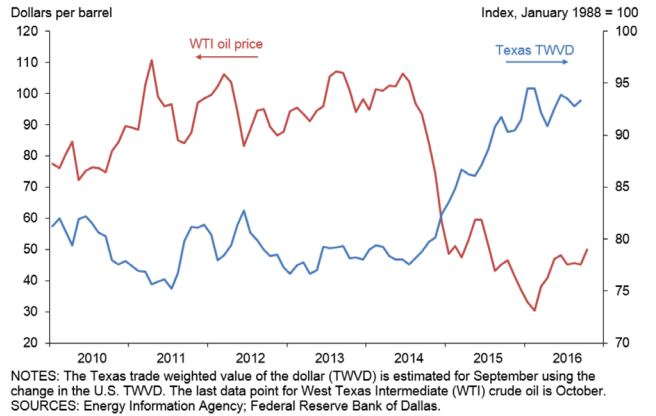
Are Headwinds of Strong Dollar, Low Oil Prices Dissipating?

Risks to the outlook include low oil prices and an unusually strong Texas trade-weighted value of the dollar (TWVD). Low oil prices led to the collapse of drilling activity in the state in 2015, and an expensive dollar has hurt manufacturing exports. Those headwinds seem to be waning somewhat, with West Texas Intermediate oil prices hovering in the \$40- to \$50-per-barrel range—up from their brief dip into the \$20 range earlier in the year—and the Texas TWVD stabilizing this year after seeing large increases in 2014 and 2015 (Chart 6).

According to the third-quarter Dallas Fed Energy Survey, most Texas oil producers need stable oil prices above \$55 to profitably expand drilling activity in areas where they are active. The Texas rig count increased to 256 for the week ending Oct. 28, its highest level since February. For manufacturers who have struggled to remain globally competitive with the rising dollar, the recent stabilization may bring a sigh of relief.

—Sarah Greer, Amy Jordan and Pia Orrenius

Chart 6
Are Economic Headwinds Dissipating?



About the Authors

Gullo is a research assistant, Jordan is an assistant economist and Orrenius is a vice president and senior economist in the Research Department at the Federal Reserve Bank of Dallas.



*“The most important thing about an investment philosophy is to have **one** that you follow.”*

At TRB Wealth Management, our goal is to provide you the financial freedom you’ve worked hard to earn. We act as fiduciaries and always put your interests first. Many studies show the majority of active wealth managers underperform the market over time. Active managers often ignore the hidden impact of expenses from trades and taxes, reducing portfolio returns. TRB approaches wealth management differently, guided by over 50 years of academic research.

Our philosophy is simple yet effective: let the markets work for you. We believe it is best to be and stay fully invested in a proper asset allocation for your age and circumstances. Our investment portfolios are designed to reduce risk through global diversification, keep fees low, and be extremely tax efficient. Each and every portfolio is designed strategically to meet specific financial needs and goals. At the end of the day, we want our clients to be comfortable financially so they can spend more time doing what they love.

John Tippit

Assistant Vice President
Investment Advisor

John Tippit recently joined the Trust & Wealth Management Division as an Investment Advisor. John was born and raised in McAllen and is a graduate of McAllen Memorial High School. He earned his BBA in Finance, focusing on investment management, from the University of Texas at Austin.

After graduation, he moved to Houston and started his career as a financial analyst in private wealth management at Credit Suisse. There he helped manage over \$1 billion in client assets. John is happy to be home, helping families throughout the Rio Grande Valley achieve their financial goals.



Rick Garcia

Wealth Management Advisor

Rick Garcia joined the Trust & Wealth Management team earlier this year. He was born in Mexico and moved to the Rio Grande Valley in 1997 at the age of 15. After graduating from McAllen Memorial High School, he earned a BBA in Business Administration from the University of Texas Pan-American.

Rick’s career as a financial advisor includes two years as a registered representative with JPMorgan Chase and four years as an investment and insurance representative with BBVA Compass. His expertise on brokerage and insurance products will help the TRB Wealth Management team maximize customer returns.

COMMUNITY GIVING YOU CAN BANK ON



Success and growth of a corporation can be measured in many ways. One metric important to Texas Regional Bank is support of local non-profit and civic organizations, which has increased year after year.

TRB support is both through financial contributions and thousands of volunteer hours. Our team loves to roll up their sleeves and lend their time and talents to make our communities strong.

This year the TRB team logged over 6,000 volunteer hours across the Rio Grande Valley. Projects ranged from building a house with Habitat for Humanity to helping raise funds for PAWS Animal Center. "We are extremely proud of our team," said Paul Moxley, CEO. "Relationship banking means being actively involved in the community. Our employees love to lend a helping hand."

TRB team members also serve on boards and committees that guide local non-profits, civic groups and faith-based organizations. Their leadership and commitment to service helps to enhance economic development and overall quality of life in the region.



TOP 10 VOLUNTEERS

Elida Anes
Ana Briones
Claudia Cabrera
Briana Cantu
Blanca Cerda

Rita Garcia
Diana Garza
Cynthia Quintanilla
Alma Soto
Norma Trevino





L to R: Michael Fallek, Bobby Farris, Bill Elliff, Tudor Uhlhorn, Michael Scaief, Brad Wolfe, Paul Moxley, Mark Richards, Carlos Varela

Senior Executive Team

- Michael Scaief – Chairman of the Board
- Paul Moxley – President & Chief Executive Officer
- Brent Baldree – Chief Lending Officer
- Michael Lamon – Chief Operations Officer
- Mark Ramirez – Chief Financial Officer

Trust & Wealth Management

- Bobby Farris – Chairman/Investment Advisor
- David L. Estes -Executive Trust Officer

Operations

Executive Vice President

- Rolando Carrasco – Chief Compliance Officer
- Ronda Johnson – Chief Information Officer

Senior Vice President

- Rutha Drawe – Finance & Regulatory Reporting Officer
- Jane Jansen – Compliance
- Sylvia Shives – Regional Branch Manager
- Beverly Speer- Branch Development & Special Projects

Lending

Executive Vice President

- Randy McLelland – Chief Credit Officer

Senior Vice President

- Fred L. Garza – Edinburg Market President
- Joel A. Gonzalez – Loan Officer
- Margie Karst – Loan Administration
- Anabel Navarro – Falfurrias Market President
- Michele Robinson – Harlingen Market President
- Carlos A. Rodriguez – Brownsville Market President
- Cesar Suarez – Mission Market President
- Lincoln Talbert – Weslaco Market President
- Jamie D. Whittemore – Loan Officer
- Mario Ysaguirre – Loan Officer

