

Is Texas Overbanked?

By Kory Killgo

A good way to answer that question is to compare the availability of banking services in Texas with availability in other parts of the country.

Texas taking to the roads are almost guaranteed to come across three things: a place to eat, a place to buy gas and a place to bank. Seemingly ubiquitous in the modern Texas landscape, banks are both a source and a sign of the state's robust economy. In small towns and large cities, community banks compete for business with each other, with savings banks and credit unions and with the largest commercial banks in the world.

Banks competing to offer the best service at the best price is essential to the health of local economies. With too little competition, monopoly characteristics can creep into banking markets, driving up costs for consumers. On the other hand, too many banks in a market may mean some institutions don't have enough business to support their overhead, making them less efficient.

So where do Texas banks and banking markets fall on this spectrum? A good way to answer that question is to compare the availability of banking services in Texas with availability in other parts of the country.

Bankers sometimes worry Texas is overbanked. The concept is somewhat

subjective, so finding a conclusive empirical answer can be problematic. However, data show that Texas ranks among the relatively less banked states, based on several measures, although it generally has greater banking services availability than California, a similarly sized state. The same conclusion holds when Texas metropolitan areas are compared with like-sized regions in other states.

How States Compare

When quantifying an area's banking infrastructure, several measures provide a yardstick of institutional presence, including total deposits, the number of different banks and the number of branches.

Branch number is probably the best gauge of availability from industry participants' perspective. A community banker with a single location surrounded by 10 branches of other institutions would most likely deem each a competitive force, regardless of the size of the branches' deposits or whether they were owned by two, three or 10 different institutions.

Since industry participants usually consider the broadest range of competitors,

Table 1
Banking Services Availability

	Texas	California	U.S. average
Population per institution (rank)	19,234 (35)	43,515 (50)	17,549
Population per branch (rank)	3,290 (42)	4,848 (51)	2,880
GDP per institution (rank)	\$872 (35)	\$2,039 (51)	\$767
GDP per branch (rank)	\$149 (42)	\$227 (49)	\$126
Personal income per institution (rank)	\$721 (35)	\$1,786 (51)	\$675
Personal income per branch (rank)	\$123 (39)	\$199 (51)	\$111
Deposits per institution (rank)	\$399 (34)	\$999 (47)	\$416
Deposits per branch (rank)	\$68 (37)	\$111 (46)	\$68
Square miles per branch (rank)	37 (33)	21 (21)	34

NOTES: All dollar values are in millions. Population data are 2007 Census estimates. Gross domestic product estimates as of calendar year 2006. Personal income data as of second quarter 2007. Banking structure data as of June 30, 2007.

SOURCES: Population and geographic data, Census Bureau; GDP and personal income, Bureau of Economic Analysis; institution branch structure and deposit data, SNL Financial.

Table 2
Big Banks Gaining Ground in Texas

	HHI (rank)		Median HHI for all states
	Texas	California	
2002	385 (9)	711 (32)	640
2003	401 (9)	764 (34)	647
2004	360 (9)	746 (32)	647
2005	540 (19)	777 (35)	686
2006	527 (16)	674 (29)	648
2007	545 (16)	672 (30)	646

SOURCE: SNL Financial.

we look at all financial institutions with reported, insured deposits: commercial banks, savings banks, thrifts and credit unions.¹ To compensate for differences in state size, the measures take the form of ratios—for example, population per number of institutions.

The data allow us to derive nine measures of banking services availability in Texas, California and the nation in 2007 (Table 1). The values in parentheses show the states' rank relative to the 50 states and the District of Columbia.

For each measure, the state ranked first is the "most banked"—the state with the lowest size measure (e.g., population) relative to its banking activity measure (e.g., number of branches), suggesting the most competition. The state ranked 51st is the "least banked"—the state with the highest size factor relative to its availability factor, suggesting the least competition. On the population-per-institution measure, for example, California is the 50th, or second-least-banked, state in the U.S.

The rankings indicate that Texas is less banked than the majority of the other states on all the measures. However, it's more banked than California by most of them.

In general, Texas falls on the less-banked side of the U.S. averages. For example, it has 3,290 people per branch, compared with 2,880 for the nation. When it comes to deposits per institution, however, the state's \$399 million falls slightly below the nation's \$416 million.

These simple availability measures don't tell us as much as we'd like about competition. A more sophisticated approach involves the Herfindahl-Hirschman Index (HHI), a widely used measure of the degree of competition in a market. It starts with the percentage of the market's deposits held by each institution. These shares are squared

and summed to arrive at the HHI.

Relatively high or increasing HHI values indicate a market's biggest institutions have a large or growing market share, which is consistent with low or decreasing competition.

For banking, the HHI has some limitations—such as the inability to reflect the impact of the number of locations each institution operates in a market. However, it's the principal measure used by the Federal Reserve System and the U.S. Department of Justice for anticompetitive analysis.

Statewide HHI values and related rankings for Texas and California, as well as the median HHI for all states, seem at odds with previous concentration measures that put Texas on the less-banked side of the U.S. average. The HHI data indicate that Texas is more competitive and more banked than both California and the rest of the nation (Table 2).

The HHI analysis suggests a slight lessening of competition in Texas over the past five years, but the state still ranked 16th on banking services availability in 2007. California was 30th.

Using a simple HHI to measure concentration can be misleading, however, because it rests on the assumption that the entire state acts as a single market. The shortcomings of that approach are obvious—especially in a state the size of Texas. It would be hard to see how a community bank with several branches in the Panhandle would compete for loans and deposits with a savings bank in the Valley or a credit union in Tyler.

A weighted HHI for each state addresses this problem by calculating an HHI value for each market within a state, using Census

The rankings indicate that Texas is less banked than the majority of the other states on all the measures.

Table 3
Banking Competition Weakens in Texas

	Weighted HHI (rank)		Weighted median HHI for all states
	Texas	California	
2002	1,277 (21)	939 (10)	1,396
2003	1,316 (21)	1,007 (12)	1,404
2004	1,218 (20)	1,170 (16)	1,377
2005	1,516 (32)	1,362 (25)	1,436
2006	1,486 (28)	842 (6) *	1,416
2007	1,602 (35)	846 (4)	1,415

*The decrease in California's HHI in 2006 is caused by a decrease of approximately \$50 billion in the deposits of a single branch.

SOURCE: SNL Financial.

core based statistical areas (CBSAs) and rural counties as markets and weighting each one's contribution to state HHI by the ratio of its deposits to the state's total (Table 3).²

By weighted HHI, California was the fourth most competitive, or most banked, state in 2007, with Texas falling on the less-banked side of the median value of 1,415 for all states. The time series also shows that, by this measure, Texas has become moderately less competitive, or relatively less banked, over the past five years, with the state's weighted HHI value increasing from 1,277 to 1,602.

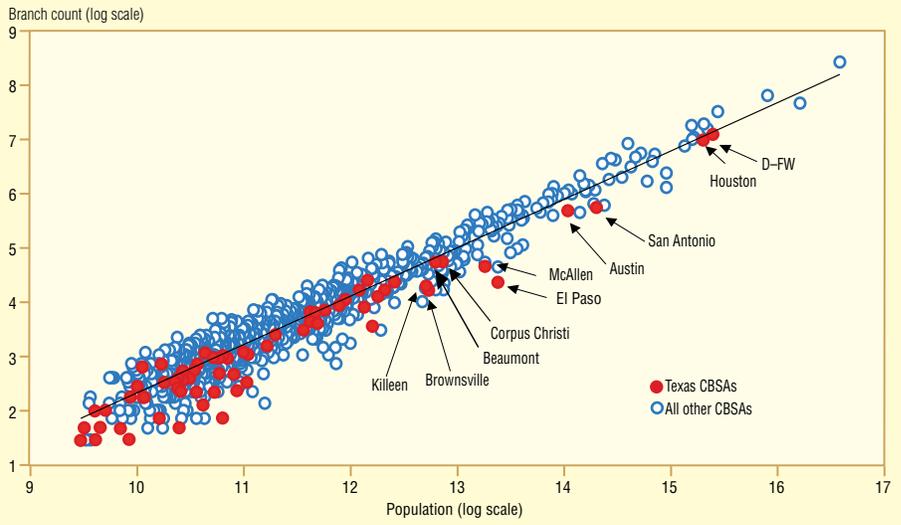
This confirms the conclusion based on the availability measures in Table 1—that Texas is among the relatively less banked states. Moreover, by the weighted HHI analysis, Texas is less banked than California.

How Metros Compare

A state as big and diverse as Texas shows significant regional differences in

Banking services do vary from place to place, but availability in Texas CBSAs tends to be slightly low when compared with similarly sized areas in other states.

Chart 1
In 2002, Most Texas Metros Are Less Banked Than Peers Elsewhere



SOURCE: SNL Financial.

many economic measures. Banking services do vary from place to place, but availability in Texas CBSAs tends to be slightly low when compared with similarly sized areas in other states.

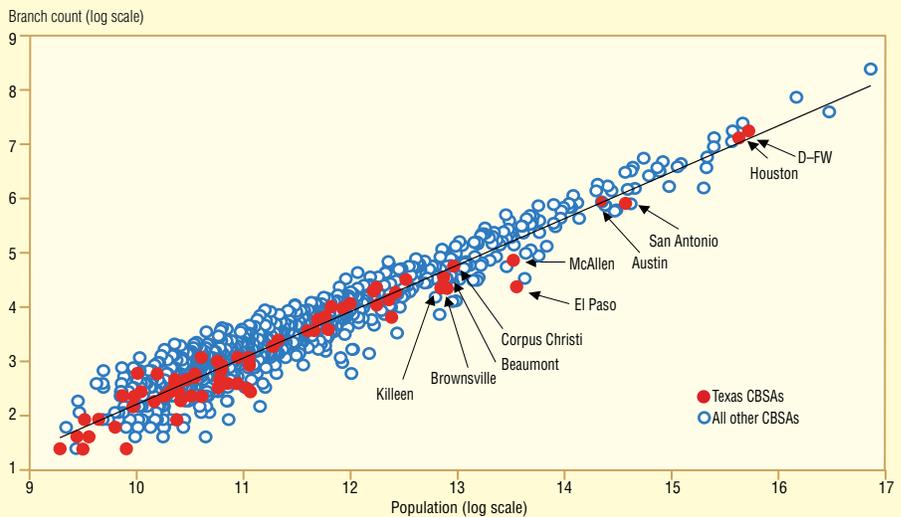
Let's first look at the ratio of population to branches in each U.S. CBSA in 2002 (*Chart 1*).³ The trend line represents central values for the entire sample: areas above the line are relatively more banked; those below the line are relatively less banked.

The 10 Texas metro areas with the largest

population were under the trend line in 2002, suggesting some degree of being less banked compared with CBSAs nationwide. El Paso was the most noticeably less banked of Texas' large CBSAs.

Now, let's look at the most recent CBSA data (*Chart 2*). In 2007 the Dallas-Fort Worth and Houston CBSAs are above the trend line, indicating their availability of bank branches relative to all CBSAs increased since 2002. The Austin and San Antonio areas' relative availability also rose over

Chart 2
By 2007, Large Texas Metros Become More Banked But Still Trail Peers



SOURCE: SNL Financial.

Table 4
Projections Based on Peer Areas Show State's Most Populous Areas Are Less Banked

Census statistical area	As of year	Branch count	Projected branch count	Difference
Dallas–Fort Worth	2002	1,311	1,484	-173
	2007	1,817	1,873	-56
Houston	2002	1,175	1,338	-163
	2007	1,587	1,723	-136
San Antonio	2002	327	531	-204
	2007	451	628	-177
Austin	2002	308	435	-127
	2007	465	532	-67
El Paso	2002	80	223	-143
	2007	91	236	-145
McAllen	2002	107	215	-108
	2007	149	242	-93
Corpus Christi	2002	117	119	-2
	2007	135	131	+4
Beaumont	2002	115	127	-12
	2007	110	133	-23
Brownsville	2002	67	107	-40
	2007	88	135	-47
Killeen	2002	75	100	-25
	2007	88	126	-38

SOURCE: SNL Financial.

the five-year period—but they, like the six other largest Texas CBSAs, remain below the trend line and less banked.

Comparing Texas' 10 largest CBSAs with defined peer groups from other states brings the changes between 2002 and 2007 into greater focus. Made up of the five next largest and five next smallest CBSAs, these peer groups are the basis for projections that we can compare with actual branch counts in Texas metropolitan areas.⁴

In 2002, the peer-based projections call for 1,484 branches in Dallas–Fort Worth; the area had 1,311, a deficit of 173. In 2007, however, the deficit had dropped to 56 branches (*Table 4*).

From 2002 to 2007, the general trend is consistent with the largest Texas CBSAs becoming more like other similarly sized areas in terms of banking services availability. Take San Antonio as an example. In 2002, the market had 204 fewer branches than we would expect based on peer areas. In 2007, the market had 177 fewer branches than we would expect based on peer areas, a relative gain of 27 branches.

The El Paso, Beaumont, Brownsville and Killeen areas trended the opposite way and became less banked relative to the peer average over those five years. With the exception of Corpus Christi, the state's largest

CBSAs are still less banked than their similarly sized peers nationwide.

Texas Not More Banked

Is Texas overbanked? The question can't be answered precisely, but we can determine how Texas compares with other states. Various measures suggest Texas isn't among the states with the most intense competition in banking services, and weighted HHI analysis implies at least some decreasing competition in recent years.

Branch analysis of the largest metropolitan areas detects increasing competition in some places. Even so, Texas' major metropolitan areas are either near or below the number of branches that would be expected based on similarly sized markets outside the state.

Is Texas more banked than other states? By objective measures, it seems the answer is no. The state's major urban centers are more banked than they were just five years ago, but overall, current banking availability is at or below levels seen elsewhere in the U.S.

Killgo is a financial industry analyst in the Financial Industry Studies Department of the Federal Reserve Bank of Dallas.

Notes

¹ Credit unions don't report branch-level data. Instead, they report all share balances at the institution's head office.

² Core based statistical areas are composed of metropolitan statistical areas, centered on a core urban area of at least 50,000 people, and micropolitan statistical areas, which are centered on a core urban area of between 10,000 and 50,000 people.

³ Charts 1 and 2 show branch data as of June 30 and population estimates as of July 1.

⁴ Dallas–Fort Worth was the fifth and fourth largest CBSA in the nation ranked by population in 2002 and 2007, respectively, and Houston was ranked fifth in 2007 (excluding Dallas). Their peer groups are adjusted accordingly. For example, in 2002 Dallas–Fort Worth's peer group consists of the four next largest and four next smallest CBSAs outside Texas.