TEXAS CAPITAL BANCSHARES INC/TX
Form 424B4
August 13, 2003

Filed Pursuant to Rule 424(b)(4)
Registration No. 333-97915

PROSPECTUS

6,000,000 Shares

Common Stock

This is our initial public offering of our common stock. We are offering 3,000,000 shares of our common stock and the selling stockholders named in this prospectus are offering 3,000,000 shares of our common stock. No public market for our common stock currently exists. We will not receive any proceeds from the sale of our shares by the selling stockholders.

Our common stock has been approved for listing on the Nasdaq National Market under the symbol TCBI.

Investing in our common stock involves risks. See Risk Factors beginning on page 10.

	Per Share	Total
Public offering price	$11.00	$66,000,000
Underwriting discounts and commissions	$ 0.77	$ 4,620,000
Proceeds, before expenses, to Texas Capital Bancshares	$10.23	$30,690,000
Proceeds, before expenses, to the selling stockholders	$10.23	$30,690,000

We and certain of the selling stockholders have granted the underwriters a 30-day option to purchase up to 900,000 additional shares to cover over-allotments.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or passed upon the adequacy or accuracy of this prospectus. Any representation to the contrary is a criminal offense.

These securities are not deposits or savings accounts and are not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency.

Lehman Brothers, on behalf of the underwriters, expects to deliver the shares on or about August 18, 2003.

LEHMAN BROTHERS

U.S. BANCORP PIPER JAFFRAY

SUNTRUST ROBINSON HUMPHREY

SANDLER O NEILL & PARTNERS, L.P.

August 13, 2003

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ABOUT THIS PROSPECTUS

You should rely only on the information contained in this document or any other document to which we refer you. We have not authorized anyone to provide you with information that is different. This document may only be used where it is legal to sell these securities. The information contained in this document is current only as of its date, regardless of the time of delivery of this prospectus or of any sales of shares of common stock.

Unless otherwise indicated, the information in this prospectus:

reflects the conversion of the 1,057,142 shares of preferred stock outstanding as of July 31, 2003 into 2,114,284 shares of common stock, which we expect will automatically occur upon the consummation of the offering.

PROSPECTUS SUMMARY

This summary highlights selected information about us and the offering that is contained elsewhere in this prospectus. You should read this summary together with the entire prospectus, including the more detailed information in our consolidated financial statements and related notes appearing elsewhere in this prospectus, as well as the other documents to which we refer you. Except as otherwise indicated by the context, references in this prospectus to we, our, the issuer or TCBI are to the combined business of Texas Capital Bancshares, Inc. and its wholly-owned subsidiary, Texas Capital Bank, N.A.

THE COMPANY

Through our bank, Texas Capital Bank, we provide a wide range of banking services, primarily to the middle market business and high net worth individual segments of the Texas economy. Since we commenced operations in December 1998, our bank has demonstrated substantial growth in assets, deposits and profitability. As of June 30, 2003, we had approximately $2.0 billion in assets, $1.3 billion in total loans, $1.3 billion in deposits and $132 million in stockholders equity. We currently operate eight banking centers in our core markets, which are the greater Dallas/ Fort Worth, Austin and San Antonio metropolitan areas. We anticipate opening a new banking center to support and expand our operations in the Houston metropolitan area in September 2003. In addition, we also operate BankDirect, an Internet banking division of our bank, to attract consumer deposits for funding purposes and to provide our BankDirect customers with access to banking services on a 24 hours-a-day/ 7 days-a-week basis.

Background

In March 1998, our founders organized TCBI to serve as a new holding company for an independent bank oriented to the needs of the Texas marketplace. Our founders have extensive Texas banking experience and strong community and business relationships in our core markets. Based on their assessment of the Texas banking environment, our founders determined that middle market businesses (which we generally define as businesses with annual revenues between $5 million and $250 million) and high net worth individuals (which we generally define as individuals with net worth in excess of $1 million) were not being well-served by the banks that emerged from the Texas banking crisis of the late 1980s. They concluded that there was an opportunity to reestablish an independent, Texas-headquartered, -managed and -focused bank with sufficient capital and other resources and expertise to serve these clients.

We commenced banking operations under the Texas Capital Bank name in December 1998. Our predecessor bank, Resource Bank N.A., had commenced limited operations in October 1997. At the time of our acquisition of Resource Bank, we raised approximately $80 million in initial equity capital in a private offering, which we believe is the largest amount of start-up capital ever raised by a national bank. We believed this capital was necessary to service our target markets, particularly by allowing us to originate and retain loans of a size and type that would appeal to our targeted market segment. We also began recruiting a team of senior executives with extensive experience in the Texas banking industry and expanding our operations in our targeted core markets. We also focused on developing a broader range of funding sources, including raising deposits through BankDirect and attracting cost-effective, stable deposits from our commercial banking customers.

We have grown substantially in both asset size and profitability since our formation. Our assets increased at annual rates of 357%, 122%, 28% and 54% in 1999, 2000, 2001 and 2002, respectively. Our total loans increased at annual rates of 1,952%, 176%, 44% and 24% in 1999, 2000, 2001 and 2002, respectively. Over the same period, our operating results have improved from a net loss of $9.3 million and $16.5 million in 1999 and 2000, respectively, reflecting in large part our start-up and expansion costs, to profits of $5.8 million and $7.3 million in 2001 and 2002, respectively, and $6.9 million for the first six months of 2003. The growth in our profitability is based largely on our success in developing a portfolio with an increasing amount of higher yielding commercial loans to local businesses and individuals, while managing our funding costs and non-interest expenses.

The Texas Market

We believe that a key factor in our ability to achieve our business strategy and financial goals and to create stockholder value is the attractiveness of the Texas market. We believe the Texas market has favorable demographic and economic characteristics. In addition, we believe that the changes in the Texas banking market since the late 1980s have created an underserved market of Texas-based middle market businesses and high net worth individuals that we can successfully target.

Texas is the second most populous state in the country with an estimated population in 2002 of approximately 21.6 million. In terms of population, Texas is expected to be among the ten fastest growing states in the U.S. over the period from 2002 to 2007, and the third fastest growing state of the ten most populous states over that period. In addition, average 2002 per capita income of $27,069 in our target markets (the five largest metropolitan markets in the state of Texas) was above the U.S. average and is expected to grow faster than any of the ten largest metropolitan statistical areas in the U.S. (excluding Dallas and Houston, which are two of our target markets and are among the ten largest metropolitan statistical areas in the U.S.) for the period 2002 to 2007. The Texas banking markets have grown over the past five years, with statewide deposits increasing from $194.3 billion in 1997 to $256.6 billion in 2002. The Texas economy has become substantially less dependent upon energy-related businesses than it was prior to the energy industry crisis of the late 1980s and includes a greater diversification among industries such as services, technology and manufacturing. Accordingly, we expect that the local Texas markets will grow faster than most in the U.S. with less volatility than experienced in the past, providing opportunities for above-average growth and potential profitability for us. Although current estimates of future economic and demographic data may indicate a favorable trend, there is no assurance that the actual results will follow these trends, especially as the Texas market may be subject to unexpected economic downturns.

The Texas banking market is currently characterized by the dominance of large out-of-state banking organizations that entered the state following the economic crisis that affected Texas during the 1980s. Today, Texas five largest banking organizations by deposits are headquartered outside of Texas and approximately 55% of the total deposits in the state are controlled by out-of-state organizations. We believe that many middle market companies and high net worth individuals are interested in banking with a company headquartered in, and with decision-making authority based in, Texas and with established Texas bankers who have the expertise to act as trusted advisors. These customers are attractive to us because we believe that, if we serve them properly, we will be able to establish long-term relationships and provide multiple products to them, enhancing our overall profitability. Our banking centers have been built around experienced bankers with lending expertise in the specific industries found in their market areas, allowing for responsive, personalized service.

Our Management

We have assembled an executive management team with extensive experience in the Texas banking industry.

Joseph M. (Jody) Grant (64) Mr. Grant has been our Chairman of the Board and Chief Executive Officer since we commenced operations in 1998. In addition, he currently serves as the Chairman of the Board of our bank. Prior to co-founding our company, Mr. Grant served as Executive Vice President, Chief Financial Officer and a member of the board of directors of Electronic Data Systems Corporation from 1990 to March 1998. From 1986 to 1989, Mr. Grant had served as the Chairman and Chief Executive Officer of Texas American Bancshares, Inc.

George F. Jones, Jr. (59) Mr. Jones has served as the Chief Executive Officer and President of our bank since its inception in December 1998. Mr. Jones was also a founder of Resource Bank, our predecessor bank. From 1993 until 1995, Mr. Jones served as an Executive Vice President of Comerica Bank, which acquired NorthPark National Bank in 1993. From 1986 until Comerica s acquisition of NorthPark in 1993, Mr. Jones served as either NorthPark s President or President and Chief Executive Officer.

C. Keith Cargill (50) Mr. Cargill has served as an Executive Vice President and the Chief Lending Officer of our bank since its inception in December 1998. Mr. Cargill has more than 20 years of banking experience. He began his banking career at Texas American Bank in 1977, where he was the manager of the national corporate lending division of the flagship bank in Fort Worth. In 1985, Mr. Cargill became President and Chief Executive Officer of Texas American Bank/ Riverside, Ft. Worth. In 1989, Mr. Cargill joined NorthPark National Bank as an Executive Vice President and Chief Lending Officer. When NorthPark was acquired by Comerica Bank in 1993, Mr. Cargill joined Comerica as Senior Vice President and middle market banking manager.

In addition to these three executive officers, we have attracted a number of other experienced Texas bankers to help build and grow our company. It is an integral component of our ongoing strategy to attract high quality, experienced bankers with long track records of serving middle market and private banking clientele in our targeted banking markets in Texas.

Chief Financial Officer

In July 2003, Peter B. Bartholow agreed to become our Chief Financial Officer. We expect that he will begin serving in that capacity on October 6, 2003. Mr. Bartholow most recently served as a Managing Partner of Hat Creek Partners, a Dallas, Texas private equity firm. Prior to joining Hat Creek Partners, he was Vice President of Corporate Finance for EDS and also served on A.T. Kearney s Board of Directors during that time.

Strategy

Our main objective is to take advantage of expansion opportunities while operating efficiently, providing individualized customer service and maximizing profitability. To achieve this, we seek to implement the following strategies:

Target the attractive middle market business and high net worth individual market segments;

Focus our business development efforts on the key major metropolitan markets in Texas;

Grow our loan and deposit base in our existing markets by hiring additional experienced Texas bankers and opening select, strategically-located banking centers;

Improve our financial performance through the efficient management of our infrastructure and capital base;

Continue to use BankDirect as a way to diversify our funding sources by attracting retail deposits on a nationwide basis; and

Expand our geographic reach and business mix by hiring qualified local bankers, establishing select banking locations and completing selective acquisitions in new markets.

Expansion in Houston Market

In September 2003, we anticipate that we will open a new banking center in Houston. We believe this new banking center will allow us to significantly expand our current operations in Houston. To assist our expansion in Houston, we have also hired several senior, experienced bankers who we believe will significantly expand our relationships in important sectors of the Houston marketplace. In addition, we intend to hire sufficient support personnel to offer a complete range of banking services.

THE OFFERING

Common stock offered by us	3,000,000 shares
Common stock offered by the selling stockholders	3,000,000 shares
Total shares of common stock offered	6,000,000 shares
Common stock outstanding after the offering	24,426,449 shares
Use of proceeds received by us	General corporate purposes, including to finance the growth of our business. A portion of the proceeds may be used for acquisitions or for the opening of select banking locations, although currently we have no understandings, agreements or definitive plans with respect to any acquisitions or openings of banking locations, other than the anticipated opening of our banking center in Houston in September 2003. We will not receive any proceeds from the shares sold by our selling stockholders.
Nasdaq National Market trading symbol	TCBI

Unless otherwise indicated, the share information in the table above and in this prospectus excludes up to 900,000 shares that may be purchased by the underwriters from us and certain of the selling stockholders to cover over-allotments.

The outstanding share information is based upon 21,426,449 shares of our common stock that were outstanding as of July 31, 2003, as adjusted for the conversion of the 1,057,142 shares of preferred stock outstanding as of July 31, 2003 into 2,114,284 shares of common stock, which we expect will automatically occur upon the consummation of the offering. Unless otherwise indicated, information contained in this prospectus regarding the number of outstanding shares of common stock does not include or reflect the following:

- 2,368,888 shares of common stock issuable upon the exercise of outstanding stock options as of June 30, 2003; and

- an aggregate of 129,861 shares of common stock reserved for future issuance as of June 30, 2003 under our 1999 Omnibus Stock Plan and 2000 Employee Stock Purchase Plan.

OUR CORPORATE INFORMATION

We are incorporated under the laws of Delaware. Our corporate headquarters is located at 2100 McKinney Avenue, Suite 900, Dallas, Texas 75201. Our telephone number is (214) 932-6600. Our web site addresses are www.texascapitalbank.com and www.bankdirect.com. The information on our web sites does not constitute part of this prospectus.

SUMMARY CONSOLIDATED FINANCIAL INFORMATION

The following table provides our summary consolidated financial data for the periods ended and as of the dates indicated. You should read the summary consolidated financial data set forth below in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations and with our consolidated financial statements and related notes appearing elsewhere in this prospectus.

	At or for the Six Months Ended June 30,		At or for the Year Ended December 31,		
	2003	2002	2002	2001	2000
	(Unaudited)				
	(In thousands, except per share, average share and percentage data)				
Consolidated Statement of Operations Data(1)					
Interest income	$ 41,499	$ 32,013	$ 70,142	$ 70,594	$ 55,769
Interest expense	17,093	12,405	27,896	35,539	32,930
Net interest income	24,406	19,608	42,246	35,055	22,839
Provision for loan losses	2,850	1,979	5,629	5,762	6,135
Net interest income after provision for loan losses	21,556	17,629	36,617	29,293	16,704
Non-interest income	6,145	3,656	8,625	5,983	1,957
Non-interest expense	26,279	16,780	35,370	29,432	35,158
Income (loss) before taxes	1,422	4,505	9,872	5,844	(16,497)
Income tax expense (benefit)	(5,466)	1,128	2,529		
Net income (loss)	6,888(2)	3,377(2)	7,343	5,844	(16,497)
Consolidated Balance Sheet Data(1)					
Total assets	2,003,198	1,260,774	1,793,282	1,164,779	908,428
Loans	1,251,794	944,731	1,122,506	903,979	629,109
Securities available for sale	649,522	270,085	553,169	206,365	184,952
Securities held to maturity					28,366
Deposits	1,340,322	980,297	1,196,535	886,077	794,857
Federal funds purchased	156,194	52,087	83,629	76,699	11,525
Other borrowings	346,773	102,442	365,831	86,899	7,061
Long-term debt	20,000		10,000		
Stockholders equity	132,168	118,043	124,976	106,359	86,197
Other Financial Data					
Income (loss) per share:					
Basic	$ 0.33(2)	$ 0.15	$ 0.33(2)	$ 0.31	$ (0.95)
Diluted	0.32(2)	0.15	0.32(2)	0.30	(0.95)
Tangible book value per share(3)	6.11	5.48	5.80	5.08	4.46
Book value per share(3)	6.18	5.55	5.87	5.15	4.54
Weighted average shares:					
Basic	19,202,699	19,135,782	19,145,255	18,957,652	17,436,628
Diluted	21,554,892	19,338,906	19,344,874	19,177,204	17,436,628
Selected Financial Ratios:					
Performance Ratios(6)					
Return on average assets	0.74%	0.56%	0.54%	0.58%	(2.42)%
Return on average equity	10.87%	6.02%	6.27%	6.44%	(20.02)%
Net interest margin	2.81%	3.47%	3.28%	3.62%	3.51%
Efficiency ratio	86.02%(4)	72.13%	69.53%(4)	71.72%	141.79%
Non-interest expense to average assets	2.81%(5)	2.79%	2.59%(5)	2.90%	5.15%

Asset Quality Ratios(6):					
Net charge-offs to average loans	0.02%	0.56%	0.38%	0.26%	
Allowance for loan losses to total loans	1.38%	1.28%	1.30%	1.39%	1.42%
Allowance for loan losses to non-performing and renegotiated loans	136.12%	178.88%	499.42%	110.23%	1,557.69%
Non-performing and renegotiated loans to total loans	1.01%	0.72%	.26%	1.26%	.09%
Capital and Liquidity Ratios					
Total capital ratio	11.50%	11.99%	11.32%	11.73%	10.98%
Tier 1 capital ratio	10.27%	10.83%	10.16%	10.48%	9.94%
Tier 1 leverage ratio	7.43%	9.27%	7.66%	9.46%	9.62%
Average equity/average assets	6.78%	9.34%	8.57%	8.93%	12.07%
Tangible equity/assets	6.52%	9.24%	6.89%	9.00%	9.31%
Average net loans/average deposits	92.91%	96.08%	96.31%	95.54%	72.92%

(1) The consolidated statement of operations data and consolidated balance sheet data presented above for the six month period ended June 30, 2002 and for the three most recent fiscal years ended December 31 have been derived from our audited consolidated financial statements, which have been audited by Ernst & Young LLP, independent auditors. The historical results are not necessarily indicative of the results to be expected in any future period. The unaudited operating results for the six month period ended June 30, 2003 are not necessarily indicative of the results to be achieved for the full year. Interim results reflect all adjustments necessary for a fair statement of the results of operations and balances for the interim periods presented. Such adjustments are of a normal recurring nature.

(2) During the six months ended June 30, 2003, net income included the impact of reversing our deferred tax asset valuation allowance of $5.9 million, $6.3 million in penalties related to unwinding repurchase agreements prior to maturity and approximately $250,000 in separation expense related to the resignation of a senior officer. For the six months ended June 30, 2003, income per share excluding the impact of reversing the valuation allowance, unwinding penalties and separation expense would have been $0.25, on a basic basis, and $0.25, on a diluted basis. During the year ended December 31, 2002, net income included $1.2 million in IPO expenses recognized as our offering was postponed. For the year ended December 31, 2002, income per share excluding these IPO expenses would have been $0.37, on a basic basis, and $0.36, on a diluted basis. Income per share excluding the impact of reversing the valuation allowance, unwinding penalties and separation expense for the six months ended June 30, 2003 and income per share excluding IPO expenses for the year ended December 31, 2002 are non-GAAP financial measures. See below for an explanation of why we believe these non-GAAP financial measures are useful to management and investors and a reconciliation of these non-GAAP financial measures to income per share, which is the most directly comparable financial measure presented in accordance with GAAP.

(3) Amounts for December 31, 2001 are adjusted to reflect the conversion of 753,301 shares of preferred stock outstanding on such date into 1,506,602 shares of common stock, assuming automatic conversion of the preferred stock. Amounts for June 30, 2002, December 31, 2002 and June 30, 2003 are adjusted to reflect the conversion of 1,057,142 shares of preferred stock outstanding on such date into 2,114,284 shares of common stock, assuming automatic conversion of the preferred stock.

(4) Represents non-interest expense divided by the sum of net interest income and non-interest income for the periods shown. During the six months ended June 30, 2003, non-interest expense included $6.3 million in penalties related to unwinding repurchase agreements prior to maturity and approximately $250,000 in separation expense related to the resignation of a senior officer. For the six months ended June 30, 2003, the efficiency ratio excluding the unwinding penalties and separation expense would have been 64.70%. During the year ended December 31, 2002, non-interest expense included $1.2 million in IPO expenses recognized as our offering was postponed. For the year ended December 31, 2002, the efficiency ratio excluding the IPO expenses would have been 67.19%. The efficiency ratio excluding unwinding penalties and separation expense for the six months ended June 30, 2003 and the efficiency ratio excluding IPO expenses for the year ended December 31, 2002 are non-GAAP financial measures. See below for an explanation of why we believe these non-GAAP financial measures are useful to management and investors and a reconciliation of these non-GAAP financial measures to the efficiency ratio, which is the most directly comparable financial measure presented in accordance with GAAP.

(5) During the six months ended June 30, 2003, the ratio of non-interest expense to average assets included $6.3 million in penalties related to unwinding repurchase agreements prior to maturity and approximately $250,000 in separation expense related to the resignation of a senior officer. For the six months ended June 30, 2003, the annualized ratio of non-interest expense to average assets excluding the unwinding penalties and separation expense would have been 2.11%. During the year ended December 31, 2002, the ratio of non-interest expense to average assets included $1.2 million in IPO expenses recognized as our offering was postponed. For the year ended December 31, 2002, the ratio of non-interest expense to average assets excluding the IPO expenses would have been 2.50%. The ratio of non-interest expense to average assets excluding unwinding penalties and separation expense for the six months ended June 30, 2003 and the ratio of non-interest expense to average assets excluding IPO expenses for the year ended December 31, 2002 are non-GAAP financial measures. See below for an explanation of why we believe these non-GAAP financial measures are useful to management and investors and a reconciliation of these non-GAAP financial measures to the ratio of non-interest expense to average assets, which is the most directly comparable financial measure presented in accordance with GAAP.

(6) Interim period ratios are annualized.

* Not meaningful.

Non-GAAP Financial Measures

The footnotes to the Summary Consolidated Financial Information presented above, the footnotes to the Selected Consolidated Financial Data, and portions of Management s Discussion and Analysis of Financial Condition and Results of Operations include non-GAAP financial measures. These non-GAAP financial measures are:

for the six months ended June 30, 2003:

income per share (basic and diluted) excluding the impact of reversing the valuation allowance, unwinding penalties and separation expense;

efficiency ratio excluding unwinding penalties and separation expense; and

ratio of non-interest expense to average assets excluding unwinding penalties and separation expense;

for the year ended December 31, 2002:

income per share (basic and diluted) excluding IPO expenses;

efficiency ratio excluding IPO expenses; and

ratio of non-interest expense to average assets excluding IPO expenses.

The impact of reversing the valuation allowance reflects the reversal of our deferred tax asset valuation allowance of $5.9 million. The unwinding penalties reflect $6.3 million in penalties related to unwinding repurchase agreements prior to maturity. The separation expense reflects approximately $250,000 in separation expense related to the resignation of a senior officer. The IPO expenses reflect $1.2 million in IPO expenses recognized as our offering was postponed.

Management believes that these non-GAAP financial measures are useful to investors and to management because they provide additional information that more closely reflects our intrinsic operating performance and growth. Reversal of the entire valuation allowance was based on our assessment of our ability to generate earnings to allow the deferred tax assets to be realized which is supported by our current earnings trends. We unwound certain repurchase agreements, incurring the unwinding penalties, in order to take advantage of historical lows in interest rates, which had decreased on similar repurchase agreements by approximately 1.4% since the time we entered into the original repurchase agreements. Although we have experienced employee separations in the past, this was the first separation with an executive who had entered into an employee agreement with us. We currently have only three other employees with employment agreements. Since we have not had any reversals of valuation allowances, unwinding penalties or separation expenses related to employees who have employment agreements in our operating history, and because expenses related to the initial public offering will not recur once the offering is completed, we believe that these non-GAAP financial measures are useful to investors and to management to understand the development of our income per share results, efficiency ratio and ratio of non-interest expense to average assets since our founding and to help in comparing our intrinsic operating performance in different periods. Management also uses these measures internally to evaluate our performance and manage our operations. These measurements should not be regarded as a replacement for corresponding GAAP measures.

The following tables reconcile each of the non-GAAP financial measures described above to the most directly comparable financial measure presented in accordance with GAAP.

Reconciliation of GAAP to income per share, excluding the impact of reversing the valuation allowance, unwinding penalties, separation expense and to income per share excluding IPO expenses.

	Six Months Ended June 30, 2003	Year Ended December 31, 2002
	(Unaudited)	
	(In thousands except share data)	
Net income	$ 6,888	$ 7,343
Repurchase agreement unwinding penalties	6,262	
Executive separation	250	
Tax effect of repurchase agreement unwinding penalties and separation costs	(2,120)	
Impact of reversing deferred tax asset valuation allowance	(5,929)	
IPO expenses		1,190
Tax effect of IPO expenses		(417)
Income excluding the impact of reversing the valuation allowance, unwinding penalties, and separation expense (for six months ended June 30, 2003), and income excluding IPO expenses (for year ended December 31, 2002)	5,351	8,116
Preferred stock dividends	(550)	(1,097)
Numerator used to calculate basic income per share excluding the impact of reversing the valuation allowance, unwinding penalties, and separation expense (for six months ended June 30, 2003) and numerator for basic income for share excluding IPO expenses (for year ended December 31, 2002)	4,801	7,019
Effect of dilutive securities (*)	550	
Numerator used to calculate diluted income per share excluding the impact of reversing the valuation allowance, unwinding penalties, and separation expense (for six months ended June 30, 2003) and numerator for diluted income per share excluding IPO expenses (for year ended December 31, 2002)	$ 5,351	$ 7,019
Denominator used for GAAP and basic income per share excluding the impact of reversing the valuation allowance, unwinding penalties, and separation expense (for six months ended June 30, 2003) and denominator for GAAP and basic income per share excluding IPO expenses (for year ended December 31, 2002)	19,202,699	19,145,255
Denominator used for GAAP and diluted income per share excluding the impact of reversing the valuation allowance, unwinding penalties, and separation expense (for six months ended June 30, 2003) and denominator for GAAP and diluted income per share excluding IPO expenses (for year ended December 31, 2002)	21,554,892	19,344,874
Basic income per share excluding the impact of reversing the valuation allowance, unwinding penalties, and separation expense (for six months ended June 30, 2003) and basic income per share excluding IPO expenses (for year ended December 31, 2002)	$ .25	$ .37
Diluted income per share excluding the impact of reversing the valuation allowance, unwinding penalties, and separation expense (for six months ended June 30, 2003) and diluted income per share excluding IPO expenses (for year ended December 31, 2002)	$ .25	$ .36

* Effects of Series A convertible preferred stock are anti-dilutive in 2002 and are not included.

Reconciliation of GAAP to Efficiency Ratio and Ratio of Non-interest Expense to Average Assets excluding Unwinding Penalties and Separation Expense, and Efficiency Ratio and Ratio of Non-interest Expense to Average Assets excluding IPO expenses.

	Six Months Ended June 30, 2003	Year Ended December 31, 2002
	(Unaudited)	
	(In thousands)	
Non-interest expense	$ 26,279	$ 35,370
Repurchase agreement unwinding penalties	(6,262)	
Executive separation	(250)	
IPO expenses		(1,190)
Numerator used to calculate efficiency ratio excluding unwinding penalties and separation expense and ratio of non-interest expense to average assets excluding unwinding penalties and separation expense (for six months ended June 30, 2003) and numerator for efficiency ratio excluding IPO expenses and ratio of non-interest expense to average assets excluding IPO expenses (for year ended December 31, 2002)	$ 19,767	$ 34,180
Denominator used for GAAP and efficiency ratio excluding unwinding penalties and separation expense (for six months ended June 30, 2003) and denominator used for GAAP and efficiency ratio excluding IPO expenses (for year ended December 31, 2002)		
Net interest income	$ 24,406	$ 42,246
Non-interest income	6,145	8,625
	$ 30,551	$ 50,871
Efficiency ratio excluding unwinding penalties and separation expense (for six months ended June 30, 2003) and efficiency ratio excluding IPO expenses (for year ended December 31, 2002)	64.70%	67.19%
Denominator used for GAAP and ratio of non-interest expense to average assets excluding unwinding penalties and separation expense (for six months ended June 30, 2003 (annualized)) and denominator used for GAAP and ratio of non-interest expense to average assets excluding IPO expenses (for year ended December 31, 2002)		
Average assets	$ 1,886,142	$ 1,365,722
Ratio of Non-interest expense to average assets excluding unwinding penalties and separation expense (for six months ended June 30, 2003 (annualized)) and ratio of non-interest expense to average assets excluding IPO expenses (for year ended December 31, 2002)	2.11%	2.50%

RISK FACTORS

Before you invest in our common stock, you should understand the high degree of risk involved. You should consider carefully the following risks and other information in this prospectus, including our financial statements and related notes, before you decide to purchase shares of our common stock. The following risks and uncertainties are not the only ones we face. There may be additional risks that we do not currently know of or that we currently deem immaterial based on the information available to us. If any of these risks actually occur, our business, financial condition and operating results could be adversely affected. As a result, the trading price of our common stock could decline, perhaps significantly and you could lose part or all of your investment.

Risks Related to Our Business

Our business strategy includes significant growth plans, and if we fail to manage our growth effectively as we pursue our expansion strategy, it could negatively affect our operations

We intend to develop our business by pursuing a significant growth strategy. Our prospects must be considered in light of the risks, expenses and difficulties frequently encountered by companies in significant growth stages of development. In order to execute our growth strategy successfully, we must, among other things:

- identify and expand into suitable markets;
- build our customer base;
- maintain credit quality;
- attract sufficient deposits to fund our anticipated loan growth;
- attract and retain qualified bank management in each of our targeted markets;
- identify and pursue suitable opportunities for opening new banking locations; and
- maintain adequate regulatory capital.

Failure to manage our growth effectively could have a material adverse effect on our business, future prospects, financial condition or results of operations, and could adversely affect our ability to successfully implement our business strategy.

We have a history of net operating losses

Although we have generated operating profits for each fiscal quarter since March 2001, we incurred significant losses during our initial years of operations and cannot guarantee that we will be able to sustain profitability. Our losses were attributable in large part to expenses incurred in forming our business, establishing our operations and growing our business, which were funded with equity capital. We cannot assure you that our revenues will continue to be sufficient to cover our expenses or that capital will be available to us on satisfactory terms, or at all, to fund any shortfall between these costs and revenues. Consequently, if we are unable to generate profits on a consistent basis, our ability to compete effectively could be adversely affected.

We have a limited operating history and as a result our financial performance to date may not be a reliable indicator of whether our business strategy will be successful

We did not commence significant operations with our current management and begin implementing our current strategy until December 1998, and our operations prior to that date were very limited. We have a very limited historical basis upon which to rely for gauging our business performance under normalized operations. Our prospects are subject to the risks and uncertainties frequently encountered by companies in their early stages of development, including the risk that we will not be able to implement our business plan or that our business plan will prove to be unprofitable. Accordingly, our financial performance to date may not be

representative of our long-term future performance or indicative of whether our business strategy will be successful.

We may not be able to find suitable acquisition candidates

We intend to make acquisitions that will complement or expand our business. However, we believe that there are a limited number of banks that will meet our acquisition criteria and, consequently, we cannot assure you that we will be able to identify suitable candidates for acquisitions. In addition, even if suitable candidates are identified, we expect to compete with other potential bidders for such businesses, many of which may have greater financial resources than we have. Our failure to find suitable acquisition candidates, or successfully bid against other competitors for acquisitions, could adversely affect our ability to successfully implement our business strategy.

We may be unable to manage our growth due to acquisitions, which could have an adverse effect on our financial condition or results of operations

We believe that a portion of our growth will come from acquisitions of banks and other financial institutions. Such acquisitions involve risks of changes in results of operations or cash flows, unforeseen liabilities relating to the acquired institution or arising out of the acquisition, asset quality problems of the acquired entity and other conditions not within our control, such as adverse personnel relations, loss of customers because of change of identity, deterioration in local economic conditions and other risks affecting the acquired institution. In addition, the process of integrating acquired entities will divert significant management time and resources. We cannot assure you that we will be able to integrate successfully or operate profitably any financial institutions we may acquire. We may experience disruption and incur unexpected expenses in integrating acquisitions. There can be no assurance that any such acquisitions will enhance our business, results of operations, cash flows or financial condition, and such acquisitions may have an adverse effect on our results of operations, particularly during periods in which the acquisitions are being integrated into our operations.

We are dependent upon key personnel

Our success depends to a significant extent upon the performance of certain key employees, the loss of whom could have an adverse effect on our business. Our key employees include Joseph M. Grant, our Chairman of the Board of Directors and Chief Executive Officer, George F. Jones, Jr., the President and Chief Executive Officer of our bank, and C. Keith Cargill, our bank s Executive Vice President and Chief Lending Officer. Although we have entered into employment agreements with these employees, we cannot assure you that we will be successful in retaining these key employees.

Our operations are significantly affected by interest rate levels

Our profitability is dependent to a large extent on our net interest income, which is the difference between interest income we earn as a result of interest paid to us on loans and investments and interest we pay to third parties such as our depositors and those from whom we borrow funds. Like most financial institutions, we are affected by changes in general interest rate levels, which are currently at relatively low levels, and by other economic factors beyond our control. Interest rate risk can result from mismatches between the dollar amount of repricing or maturing assets and liabilities and from mismatches in the timing and rate at which our assets and liabilities reprice. Although we have implemented strategies which we believe reduce the potential effects of changes in interest rates on our results of operations, these strategies may not always be successful. In addition, any substantial and prolonged increase in market interest rates could reduce our customers desire to borrow money from us or adversely affect their ability to repay their outstanding loans by increasing their credit costs since most of our loans have adjustable interest rates that reset periodically. Any of these events could adversely affect our results of operations or financial condition.

We must effectively manage our credit risk

There are risks inherent in making any loan, including risks with respect to the period of time over which the loan may be repaid, risks resulting from changes in economic and industry conditions, risks inherent in dealing with individual borrowers and risks resulting from uncertainties as to the future value of collateral. The risk of nonpayment of loans is inherent in commercial banking. Although we attempt to minimize our credit risk by carefully monitoring the concentration of our loans within specific industries and through prudent loan application approval procedures, we cannot assure you that such monitoring and approval procedures will reduce these lending risks. Moreover, as we expand our operations into new geographic markets, our credit administration and loan underwriting policies will need to be adapted to the local lending and economic environments of these new markets. We cannot assure you that our credit administration personnel, policies and procedures will adequately adapt to any new geographic markets.

There are material risks involved in commercial lending that could adversely affect our business

We generally invest a greater proportion of our assets in commercial loans than other banking institutions of our size, which typically invest a greater proportion of their assets in loans secured by single-family residences. Commercial loans generally involve a higher degree of credit risk than residential mortgage loans due, in part, to their larger average size and generally less readily-marketable collateral. Due to their size and the nature of their collateral, losses incurred on a small number of commercial loans could have a material adverse impact on our financial condition and results of operations. In addition, unlike residential mortgage loans, commercial loans generally depend on the cash flow of the borrower s business to service the debt. Furthermore, a significant portion of our loans is dependent for repayment largely on the liquidation of assets securing the loan, such as inventory and accounts receivable. These loans carry incrementally higher risk, since their repayment is often dependent solely on the financial performance of the borrower s business. Our business plan calls for continued efforts to increase our assets invested in commercial loans. An increase in non-performing loans could cause operating losses, impaired liquidity and the erosion of our capital, and could have a material adverse effect on our business, financial condition or results of operations.

If the value of real estate in our core Texas markets were to decline materially, a significant portion of our loan portfolio could become under-collateralized, which would have a material adverse effect on us

The market value of real estate, particularly real estate held for investment, can fluctuate significantly in a short period of time as a result of market conditions in the geographic area in which the real estate is located. If the value of the real estate serving as collateral for our loan portfolio were to decline materially, a significant part of our loan portfolio could become under-collateralized. As of June 30, 2003, approximately 41% of the collateral for the loans in our portfolio consisted of real estate. Of the real estate that collateralizes the loans in our portfolio, approximately one-third of the properties are real estate owned and occupied by businesses to which we have extended loans and the remaining two-thirds is real estate held for investment by the borrower. If the loans that are collateralized by real estate become troubled during a time when market conditions are declining or have declined, then we may not be able to realize the amount of security that we anticipated at the time of originating the loan, which could have a material adverse effect on our provision for loan losses and our operating results and financial condition.

We may be responsible for environmental claims and other related costs of property we acquire through foreclosure, which could adversely affect our profitability

A significant portion of our loan portfolio is secured by real property. In the course of our business, we may acquire properties that secure loans as a result of foreclosure. There is a risk that hazardous or toxic waste could be found on such properties. In such event, we could be held responsible for the cost of cleaning up or removing such waste, and such cost could significantly exceed the value of the underlying properties and adversely affect our profitability. To date, we have not been required to perform any investigation or clean up activities with respect to, nor have we been subject to any environmental claims on, any loans held in our loan portfolio or other properties we acquired. Although we have a policy that requires us to perform an environmental review before initiating any foreclosure action on real property, there can be no assurance that this will be sufficient to detect all potential environmental hazards.

Our financial condition and results of operations would be adversely affected if our allowance for loan losses is not sufficient to absorb actual losses

Experience in the banking industry indicates that a portion of our loans will become delinquent, some of which may only be partially repaid or may never be repaid at all. Despite our underwriting criteria, we experience losses for reasons beyond our control, such as general economic conditions. Although we believe that our allowance for loan losses is maintained at a level adequate to absorb any inherent losses in our loan portfolio, these estimates of loan losses are inherently subjective and their accuracy depends on the outcome of future events. We may need to make significant and unanticipated increases in our loss allowances in the future, which would materially affect our results of operations in that period.

Bank regulators may require us to increase our allowance for loan losses, which could have a negative effect on our financial condition and results of operations

Federal regulators, as an integral part of their respective supervisory functions, periodically review our allowance for loan losses. The regulatory agencies may require us to increase our provision for loan losses or to recognize further loan charge-offs based upon their judgments, which may be different from ours. Any increase in the allowance for loan losses required by these regulatory agencies could have a negative effect on our financial condition and results of operations.

Lack of seasoning of our loan portfolio may increase the risk of credit defaults in the future

Most of the loans in our loan portfolio were originated within the past four years, and approximately 49% were originated within the past 18 months. In general, loans do not begin to show signs of credit deterioration or default until they have been outstanding for some period of time, a process referred to as seasoning. As a result, a portfolio of older loans will usually behave more predictably than a newer portfolio. Because our loan portfolio is relatively new, the current level of delinquencies and defaults may not be representative of the level that will prevail when the portfolio becomes more seasoned, which is likely to be somewhat higher than current levels.

Until our portfolio becomes more seasoned, we must rely in part on the historical loan loss experience of other financial institutions and the experience of our management in determining our allowance for loan losses, and this may not be comparable to our loan portfolio

Because most of our loans in our loan portfolio were originated relatively recently, our loan portfolio does not provide an adequate history of loan losses for our management to rely upon in establishing our allowance for loan losses. We therefore rely to a significant extent upon other financial institutions histories of loan losses and their allowance for loan losses, as well as our management s estimates based on their experience in the banking industry, when determining our allowance for loan losses. There is no assurance that the history of loan losses and the reserving policies of other financial institutions and our management s judgment will result in reserving policies that will be adequate for our business and operations or applicable to our loan portfolio.

Our business faces unpredictable economic conditions

General economic conditions impact the banking industry. The credit quality of our loan portfolio necessarily reflects, among other things, the general economic conditions in the areas in which we conduct our business. Our continued financial success depends somewhat on factors beyond our control, including:

- national and local economic conditions;

- the supply and demand for investable funds;

interest rates; and

federal, state and local laws affecting these matters.

Any substantial deterioration in any of the foregoing conditions could have a material adverse effect on our financial condition and results of operations, which would likely adversely affect the market price of our common stock. Further, with the exception of our BankDirect customers which comprised 19% of our total deposits as of June 30, 2003, our bank s customer base is primarily commercial in nature, and our bank does not have a significant branch network or retail deposit base. In periods of economic downturn, business and commercial deposits may tend to be more volatile than traditional retail consumer deposits and, therefore, during these periods our financial condition and results of operations could be adversely affected to a greater degree than those competitors that have a larger retail customer base.

Our business is concentrated in Texas and a downturn in the economy of Texas may adversely affect our business

Substantially all of our business is located in Texas. As a result, our financial condition and results of operations may be affected by changes in the Texas economy. A prolonged period of economic recession or other adverse economic conditions in Texas may result in an increase in nonpayment of loans and a decrease in collateral value.

We compete with many larger financial institutions which have substantially greater financial resources than we have

Competition among financial institutions in Texas is intense. We compete with other bank holding companies, state and national commercial banks, savings and loan associations, consumer finance companies, credit unions, securities brokerages, insurance companies, mortgage banking companies, money market mutual funds, asset-based non-bank lenders and other financial institutions. Many of these competitors have substantially greater financial resources, lending limits and larger branch networks than we do, and are able to offer a broader range of products and services than we can. Failure to compete effectively for deposit, loan and other banking customers in our markets could cause us to lose market share, slow our growth rate and may have an adverse effect on our financial condition and results of operations.

Our future profitability depends, to a significant extent, upon revenue we receive from our middle market business customers and their ability to meet their loan obligations

At June 30, 2003, a substantial majority of our loan portfolio was comprised of loans to our middle market business customers. For the six month period ended June 30, 2003, a significant portion of our total interest and non-interest income was derived from middle market business customers. We expect that our future profitability will depend, to a significant extent, upon revenue we receive from middle market business customers, and their ability to continue to meet existing loan obligations. As a result, adverse economic conditions or other factors adversely affecting this market segment may have a greater adverse effect on us than on other financial institutions that have a more diversified customer base.

We compete in an industry that continually experiences technological change, and we may have fewer resources than many of our competitors to continue to invest in technological improvements

The financial services industry is undergoing rapid technological changes, with frequent introductions of new technology-driven products and services. In addition to improving the ability to serve customers, the effective use of technology increases efficiency and enables financial institutions to reduce costs. Our future success will depend, in part, upon our ability to address the needs of our customers by using technology to provide products and services that will satisfy customer demands for convenience, as well as to create additional efficiencies in our operations. Many of our competitors have substantially greater resources to invest in technological improvements. We may not be able to effectively implement new technology-driven products and services or be successful in marketing these products and services to our customers.

System failure or breaches of our network security could subject us to increased operating costs as well as litigation and other liabilities

The computer systems and network infrastructure we use could be vulnerable to unforeseen problems. Our operations are dependent upon our ability to protect our computer equipment against damage from fire, power loss, telecommunications failure or a similar catastrophic event. Any damage or failure that causes an interruption in our operations could have an adverse effect on our financial condition and results of operations. In addition, our operations are dependent upon our ability to protect the computer systems and network infrastructure utilized by us against damage from physical break-ins, security breaches and other disruptive problems caused by the Internet or other users. Such computer break-ins and other disruptions would jeopardize the security of information stored in and transmitted through our computer systems and network infrastructure, which may result in significant liability to us and deter potential customers. Although we, with the help of third-party service providers, intend to continue to implement security technology and establish operational procedures to prevent such damage, there can be no assurance that these security measures will be successful. In addition, advances in computer capabilities, new discoveries in the field of cryptography or other developments could result in a compromise or breach of the algorithms we and our third-party service providers use to protect customer transaction data. A failure of such security measures could have an adverse effect on our financial condition and results of operations.

Our success in the Internet banking market will largely depend on our ability to implement services competitive with similar services offered by other financial institutions

The success of our Internet banking products and services will depend in large part on our ability to implement and maintain the appropriate technology. This includes our ability to provide services competitive with banks that are already using the Internet. If we are unable to implement and maintain the appropriate technology efficiently, it could affect our results of operations and our ability to compete with financial institutions.

Our success in attracting and retaining retail consumer deposits depends on our ability to offer competitive rates and services

As of June 30, 2003, approximately 19% of our total deposits came from retail consumer customers through BankDirect, our Internet banking facility. The market for Internet banking is extremely competitive and allows retail consumer customers to access financial products and compare interest rates from numerous financial institutions located across the U.S. As a result, Internet retail consumers are more sensitive to interest rate levels than retail consumers who bank at a branch office. Our future success in retaining and attracting retail consumer customers depends, in part, on our ability to offer competitive rates and services.

We could be adversely affected by changes in the regulation of the Internet

Our ability to conduct, and the cost of conducting, business may also be adversely affected by a number of legislative and regulatory proposals concerning the Internet, which are currently under consideration by federal, state, local and foreign governmental organizations. These proposals include, but are not limited to, the following matters:

- on-line content;
- user privacy;
- taxation;
- access charges;
- liability for third-party activities; and
- regulatory and supervisory authority.

Moreover, it is uncertain how existing laws relating to these issues will be applied to the Internet. The adoption of new laws or the application of existing laws could decrease the growth in the use of the Internet, which could in turn decrease the demand for our services, increase our cost of doing business or otherwise have an adverse effect on our business, financial condition and results of operations. Furthermore, government restrictions on Internet content could slow the growth of Internet use and decrease acceptance of the Internet as a communications and commercial medium and thereby have an adverse effect on our financial condition and results of operations.

Risks Related to Our Industry

We are subject to significant government regulation

We operate in a highly regulated environment and are subject to supervision and regulation by a number of governmental regulatory agencies, including the Federal Reserve System, or Federal Reserve, the Office of the Comptroller of the Currency, or OCC, and the Federal Deposit Insurance Corporation, or FDIC. Regulations adopted by these agencies, which are generally intended to provide protection for depositors and customers rather than for the benefit of stockholders, govern a comprehensive range of matters relating to ownership and control of our shares, our acquisition of other companies and businesses, permissible activities for us to engage in, maintenance of adequate capital levels and other aspects of our operations. The bank regulatory agencies possess broad authority to prevent or remedy unsafe or unsound practices or violations of law. In addition, future legislation and government policy, including with respect to bank deregulation and interstate expansion, could adversely affect the banking industry as a whole, including our results of operations. For example, new legislation or regulation may limit the manner in which we may conduct our business, including our ability to offer new products, obtain financing, attract deposits, make loans and achieve satisfactory interest spreads.

Recent legislation will change the way financial institutions conduct their business; we cannot predict the effect it will have upon us

The Gramm-Leach-Bliley Financial Modernization Act was signed into law on November 12, 1999. Among other things, the Modernization Act repeals restrictions on banks affiliating with securities firms and insurance companies. It also permits bank holding companies that become financial holding companies to engage in additional financial activities, including insurance and securities underwriting and agency activities, merchant banking and insurance company portfolio investment activities. The Modernization Act may have the result of increasing the competition we face from larger banks and other companies. It is not possible to predict the full effect that the Modernization Act will have on us.

Risks Related to an Investment in Our Common Stock

Our offering price may not be indicative of the fair market value of the common stock, and the future trading price of our stock may fluctuate

The public offering price may not indicate the market price for the common stock after this offering. We determined the public offering price based on a variety of factors, including:

- prevailing market conditions;
- our historical performance and capital structure;
- estimates of our business potential and earnings prospects;
- an overall assessment of our management; and
- the consideration of these factors in relation to market valuation of companies in related businesses.

The offering price and aggregate number of shares being offered were determined through our negotiations with the underwriters. No assurance can be given that you will be able to resell your shares at a price equal to or greater than the offering price or that the offering price necessarily indicates the fair market value of our common stock.

The market price of our common stock may also be subject to significant fluctuations in response to our future operating results and other factors, including market conditions. In recent years, the stock market has experienced extreme price and volume fluctuations that have often been unrelated or disproportionate to the operating performances and prospects of individual companies.

If a market for our common stock does not develop, you may not be able to sell your shares at or above the offering price

Prior to this offering, a public market for our common stock did not exist. Although our common stock has been approved for listing on the Nasdaq National Market, there can be no assurance that an active trading market will develop or that purchasers of our common stock will be able to resell their common stock at prices equal to or greater than the initial public offering price. The development of a public market having the desirable characteristics of depth, liquidity and orderliness depends upon the presence of a sufficient number of willing buyers and sellers at any given time, over which neither we nor any market maker has any control. Accordingly, there can be no assurance that an established and liquid market for the common stock will develop or be maintained.

Future sales of our common stock could depress the price of our common stock

Sales of a substantial number of shares of our common stock in the public market by our stockholders after this offering, or the perception that these sales are likely to occur, could cause the market price of our common stock to decline. Upon completion of this offering, we will have 24,426,449 outstanding shares of our common stock. Of these shares, approximately 10.5 million shares, including the shares sold in this offering, may be traded, without restriction, in the public market immediately after this offering is completed. Upon the expiration of lock-up agreements entered into by our directors, officers, the selling stockholders and certain other significant stockholders in connection with the offering, which will occur 180 days from the date of this prospectus, approximately 13.0 million additional shares will be eligible for sale in the public market, subject, in the case of our affiliates, to the volume restrictions of Rule 144.

As a new investor, you will incur substantial book value dilution as a result of this offering and future equity issuances could result in further dilution, which could cause our stock price to decline

The initial public offering price is substantially higher than the current net tangible book value of our outstanding common stock. As a result, investors purchasing common stock in this offering will incur immediate dilution of $4.34 per share. This dilution is due in large part to earlier investors in our company having paid substantially less than the initial public offering price when they purchased their shares. The exercise of outstanding options and future equity issuances, including any additional shares issued in connection with acquisitions, could result in further dilution to investors.

Our existing management will maintain significant control over us following the offering

Immediately following this offering, our current executive officers and directors will beneficially own approximately 14.8% of the outstanding shares of our common stock, or approximately 13.9% if the underwriters exercise their over-allotment option in full. These percentages may increase to the extent that the executive officers and directors elect to purchase shares in connection with this offering. Accordingly, our current executive officers and directors will be able to influence, to a significant extent, the outcome of all matters required to be submitted to our stockholders for approval (including decisions relating to the election of directors), the determination of day-to-day corporate and management policies and other significant corporate activities.

We have not historically paid, and do not presently intend to pay, cash dividends

We have not paid any cash dividends on our common stock to date and do not intend to pay cash dividends on our common stock in the foreseeable future. We intend to retain earnings to finance operations and the expansion of our business. Therefore, any gains from your investment in our common stock must come from an increase in its market price.

We will be restricted in our ability to pay dividends to our stockholders

We are a holding company with no independent sources of revenue and would likely rely upon cash dividends and other payments from our bank to fund the payment of future cash dividends, if any, to our stockholders. Payment of dividends by the bank to us would be subject to the prior approval of the OCC if the total of all dividends declared by the bank in any calendar year exceeds the sum of the bank s net profits for that year and its retained net profits for the preceding two calendar years, less any required transfers to surplus. In addition, federal law also prohibits a national bank from paying dividends if it is, or such dividend payments would cause it to become, undercapitalized. At June 30, 2003, our bank was prohibited by these laws from paying any dividends to us without the OCC s prior approval. If the bank is restricted from paying cash dividends to us, we would likely not be able to pay cash dividends to our stockholders.

Anti-takeover provisions of our certificate of incorporation, bylaws and Delaware law may make it more difficult for you to receive a change in control premium

Certain provisions of our certificate of incorporation and bylaws could make a merger, tender offer or proxy contest more difficult, even if such events were perceived by many of our stockholders as beneficial to their interests. These provisions include advance notice for nominations of directors and stockholders proposals. In addition, our certificate of incorporation authorizes the issuance of blank check preferred stock with such designations, rights and preferences as may be determined from time to time by our board of directors. Accordingly, our board of directors is empowered, without stockholder approval (unless otherwise required by the rules of any stock exchange on which our common stock is then listed), to issue preferred stock with dividend, liquidation, conversion, voting or other rights which could adversely affect the voting power or other rights of the holders of our common stock. In the event of such issuance, the preferred stock could be utilized, under certain circumstances, as a method of discouraging, delaying or preventing a change in control. Although we have no present intention to issue any shares of our preferred stock, there can be no assurance that we will not do so in the future. In addition, as a Delaware corporation, we are subject to Section 203 of the Delaware General Corporation Law which, in general, prevents an interested stockholder, defined generally as a person owning 15% or more of a corporation s outstanding voting stock, from engaging in a business combination with our company for three years following the date that person became an interested stockholder unless certain specified conditions are satisfied.

There are substantial regulatory limitations on changes of control

With certain limited exceptions, federal regulations prohibit a person or company or a group of persons deemed to be acting in concert from, directly or indirectly, acquiring more than 10% (5% if the acquiror is a bank holding company) of any class of our voting stock or obtaining the ability to control in any manner the election of a majority of our directors or otherwise direct the management or policies of our company without prior notice or application to and the approval of the Federal Reserve. Accordingly, prospective investors need to be aware of and comply with these requirements, if applicable, in connection with any purchase of shares of our common stock in this offering.

We have broad discretion to use the proceeds of this offering

We expect to use the net proceeds from this offering for the broadening of business lines, potential acquisitions in the financial and financial services industries and other general corporate purposes. Accordingly, we will have broad discretion as to the application of such proceeds. You will not have an opportunity to evaluate the economic, financial or other information on which we base our decisions on how to use these net proceeds. Our failure to use these funds effectively could have an adverse effect on our financial condition and results of operations.

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This prospectus includes forward-looking statements based on our current expectations, assumptions, estimates and projections about our business and our industry. They include, but are not limited to, statements relating to:

- future revenues, expenses and profitability; and

- the future development and expected growth of our business.

You can identify forward-looking statements by the use of words such as may, should, will, could, estimates, predicts, potential, aims, anticipates, believes, plans, expects, future and intends and similar expressions. This information does not guarantee future perfo and is subject to risks, uncertainties and other factors, some of which are beyond our control and difficult to predict and could cause actual results to differ materially from those expressed or forecasted in the forward-looking statements. In evaluating forward-looking statements, you should carefully consider the risks and uncertainties described in Risk Factors and elsewhere in this prospectus. The forward-looking statements reflect our view only as of the date of this prospectus, and we do not assume any obligation to update or correct these forward-looking statements except to the extent we are required to do so by applicable law. All forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the cautionary statements and risk factors contained throughout this prospectus.

USE OF PROCEEDS

We expect to receive net proceeds of approximately $30.2 million from this offering after deducting the underwriting discount and estimated offering expenses. We will not receive any proceeds from shares of our common stock sold by the selling stockholders in this offering.

We intend to use the net proceeds for general corporate purposes, including to finance the growth of our business. We may also use a portion of the proceeds for acquisitions or for the opening of select banking locations. However, we have no present understanding, agreement or definitive plans relating to any specific acquisitions or openings of any banking locations, other than the anticipated opening of our banking center in Houston in September 2003.

The principal purposes of this offering are to raise capital, create a public market for our common stock, enhance our ability to acquire other businesses, products and technologies and facilitate future access to public securities markets.

We have not yet determined the amount of net proceeds to be used specifically for each of the foregoing purposes mentioned above. Accordingly, our management will have significant flexibility in applying the net proceeds of the offering. Pending their use as described above, we may invest the net proceeds of this offering in interest-bearing investment-grade instruments or bank deposits.

DIVIDEND POLICY

We have never declared or paid any cash dividends on our common stock. We do not anticipate paying any cash dividends on our common stock in the foreseeable future. We currently intend to retain future earnings, if any, to finance operations and the expansion of our business.

In addition, we are a holding company and our principal source of funds to pay dividends, if any, in the future and make other payments will be the payment of dividends by our bank to us. As a national bank, our bank is subject to various restrictions under federal law on its ability to pay dividends and make other distributions and payments to us. These are described under Regulation and Supervision.

Any future determination to pay cash dividends will be at the discretion of our board of directors and will be dependent upon our financial condition, operating results, capital requirements, federal banking regulations, Delaware law, and other factors that our board of directors deems relevant.

CAPITALIZATION

The following table presents our capitalization as of June 30, 2003. Our capitalization is presented:

- on an actual basis (which does not reflect the conversion of the 1,057,142 shares of preferred stock into shares of common stock); and
- on a pro forma basis to reflect:
  - our receipt of the estimated net proceeds of approximately $30.2 million from the sale of 3,000,000 shares of common stock by us in this offering, after deducting the estimated underwriting discounts and commissions, and estimated offering expenses;
  - the conversion of the 1,057,142 shares of preferred stock outstanding into 2,114,284 shares of common stock, which we expect will automatically occur upon the consummation of the offering; and
  - the conversion of a sufficient number of shares of Series A-1 Nonvoting common stock, all of which is held by one of our stockholders, into an equal number of shares of voting common stock so that, after the offering, the holder s beneficial ownership of voting common stock equals 4.9% of the outstanding shares of voting common stock.

You should read this table in conjunction with the consolidated financial statements and related notes that are included in this prospectus.

	As of June 30, 2003	
	Actual	Pro Forma
	(In thousands, except share data)	
Liabilities		
Deposits		
Non-interest bearing	$ 330,015	$ 330,015
Interest bearing	1,010,307	1,010,307
Total deposits	1,340,322	1,340,322
Accrued interest payable	3,393	3,393
Other liabilities	4,348	4,348
Federal funds purchased	156,194	156,294
Repurchase agreements	293,272	293,172
Other borrowings	53,501	53,501
Long-term debt	20,000	20,000
Total liabilities	1,871,030	1,871,030
Stockholders equity:		
Preferred stock, $.01 par value		
Authorized shares 10,000,000		
Issued shares 1,057,142 convertible preferred stock, nonvoting, $.01 par value, 6% (actual); 0 (pro forma)	11	
Common stock, $.01 par value:		
Authorized shares 100,000,000		
Voting common stock:		
Issued shares 18,577,704 (actual); 24,056,863 (pro forma)	185	241
Series A-1 non-voting common stock, $.01 par value:		
Issued shares 691,733 (actual); 326,858 (pro forma)	7	3
Additional paid-in capital	131,801	161,954
Accumulated deficit	(6,459)	(6,459)
Treasury stock (shares at cost: 97,246 (actual); 97,246 (pro forma))	(668)	(668)
Deferred compensation	573	573

Accumulated other comprehensive income	6,718	6,718
Total stockholders equity	132,168	162,362
Total capitalization	$2,003,198	$2,033,392

SELECTED CONSOLIDATED FINANCIAL DATA

You should read the selected consolidated financial data presented below in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and the related notes appearing elsewhere in this prospectus.

We formed our wholly-owned subsidiary bank through the acquisition of Resource Bank, N.A. on December 18, 1998. Our bank s financial statements include the operations of our bank from December 18, 1998. The operations of Resource Bank, N.A. prior to December 18, 1998 are shown separately as predecessor financial statements.

	At or for the Six Months Ended June 30,		At or for the Year Ended December 31,				March 1, 1998 (Inception) through December 31,
	2003	2002	2002	2001	2000	1999	1998
	(Unaudited)		(In thousands, except per share, average share and percentage data)				
Consolidated Statement of Operations(1)							
Interest income	$ 41,499	$ 32,013	$ 70,142	$ 70,594	$ 55,769	$ 14,414	$ 213
Interest expense	17,093	12,405	27,896	35,539	32,930	6,166	32
Net interest income	24,406	19,608	42,246	35,055	22,839	8,248	181
Provision for loan losses	2,850	1,979	5,629	5,762	6,135	2,687	1
Net interest income after provision for loan losses	21,556	17,629	36,617	29,293	16,704	5,561	180
Non-interest income	6,145	3,656	8,625	5,983	1,957	358	4
Non-interest expense	26,279	16,780	35,370	29,432	35,158	15,217	923
Income (loss) before taxes	1,422	4,505	9,872	5,844	(16,497)	(9,298)	(739)
Income tax expense (benefit)	(5,466)	1,128	2,529				
Net income (loss)	6,888(2)	3,377(2)	7,343	5,844	(16,497)	(9,298)	(739)
Consolidated Balance Sheet Data(1)							
Total assets	2,003,198	1,260,774	1,793,282	1,164,779	908,428	408,579	89,311
Loans	1,251,794	944,731	1,122,506	903,979	629,109	227,600	11,092
Securities available for sale	649,522	270,085	553,169	206,365	184,952	164,409	3,171
Securities held to maturity					28,366		
Deposits	1,340,322	980,297	1,196,535	886,077	794,857	287,068	16,018
Federal funds purchased	156,194	52,087	83,629	76,699	11,525		
Other borrowings	346,773	102,442	365,831	86,899	7,061	46,267	
Long-term debt	20,000		10,000				
Stockholders equity	132,168	118,043	124,976	106,359	86,197	72,912	73,186
Other Financial Data							
Income (loss) per share:							
Basic	$ 0.33(2)	$ 0.15	$ 0.33(2)	$ 0.31	$ (0.95)	$ (0.61)	$ *
Diluted	0.32(2)	0.15	0.32(2)	0.30	(0.95)	(0.61)	*
Tangible book value per share(3)	6.11	5.48	5.80	5.08	4.46	4.67	5.37
Book value per share(3)	6.18	5.55	5.87	5.15	4.54	4.79	5.51

Weighted average shares:							
Basic	19,202,699	19,135,782	19,145,255	18,957,652	17,436,628	15,132,496	*
Diluted	21,554,892	19,338,906	19,344,874	19,177,204	17,436,628	15,132,496	*
Selected Financial Ratios:							
Performance Ratios(6)							
Return on average assets	0.74%	0.56%	0.54%	0.58%	(2.42)%	(4.45)%	(5.83)%(7)
Return on average equity	10.87%	6.02%	6.27%	6.44%	(20.02)%	(12.13)%	(12.52)%(7)
Net interest margin	2.81%	3.47%	3.28%	3.62%	3.51%	4.12%	5.65%(7)
Efficiency ratio	86.02%(4)	72.13%	69.53%(4)	71.72%	141.79%	176.82%	205.18%(7)
Non-interest expense to average assets	2.81%(5)	2.79%	2.59%(5)	2.90%	5.15%	7.28%	10.64%(7)
Asset Quality Ratios(6):							
Net charge-offs to average loans	0.02%	0.56%	0.38%	0.26%		0.01%	
Allowance for loan losses to total loans	1.38%	1.28%	1.30%	1.39%	1.42%	1.22%	0.90%
Allowance for loan losses to non-performing and renegotiated loans	136.12%	178.88%	499.42%	110.23%	1,557.69%		666.67%
Non-performing and renegotiated loans to total loans	1.01%	0.72%	.26%	1.26%	0.09%		0.14%

	At or for the Six Months Ended June 30,		At or for the Year Ended December 31,				March 1, 1998 (Inception) through December 31,
	2003	2002	2002	2001	2000	1999	1998
	(Unaudited)						
	(In thousands, except per share, average share and percentage data)						
Capital and Liquidity Ratios							
Total capital ratio	11.50%	11.99%	11.32%	11.73%	10.98%	23.84%	267.01%
Tier 1 capital ratio	10.27%	10.83%	10.16%	10.48%	9.94%	22.98%	266.64%
Tier 1 leverage ratio	7.43%	9.27%	7.66%	9.46%	9.62%	21.32%	397.86%
Average equity/average assets	6.78%	9.34%	8.57%	8.93%	12.07%	36.67%	46.58%(7)
Tangible equity/assets	6.52%	9.24%	6.89%	9.00%	9.31%	17.42%	79.85%
Average loans/average deposits	92.91%	96.08%	96.31%	95.54%	72.92%	81.12%	68.36%(7)

(1) The consolidated statement of operations data and consolidated balance sheet data presented above for the six month period ended June 30, 2002 and for the four most recent fiscal years ended December 31 have been derived from our audited consolidated financial statements, which have been audited by Ernst & Young LLP, independent auditors. The historical results are not necessarily indicative of the results to be expected in any future period. The unaudited operating results for the six month period ended June 30, 2003 are not necessarily indicative of the results to be achieved for the full year. Interim results reflect all adjustments necessary for a fair statement of the results of operations and balances for the interim periods presented. Such adjustments are of a normal recurring nature.

(2) During the six months ended June 30, 2003, net income included the impact of reversing our deferred tax asset valuation allowance of $5.9 million, $6.3 million in penalties related to unwinding repurchase agreements prior to maturity and approximately $250,000 in separation expense related to the resignation of a senior officer. For the six months ended June 30, 2003, income per share excluding the impact of reversing the valuation allowance, unwinding penalties and separation expense would have been $0.25, on a basic basis, and $0.25, on a diluted basis. During the year ended December 31, 2002, net income included $1.2 million in IPO expenses recognized as our offering was postponed. For the year ended December 31, 2002, income per share excluding these IPO expenses would have been $0.37, on a basic basis, and $0.36, on a diluted basis. Income per share excluding the impact of reversing the valuation allowance, unwinding penalties and separation expense for the six months ended June 30, 2003 and income per share excluding IPO expenses for the year ended December 31, 2002 are non-GAAP financial measures. See discussion of non-GAAP financial measures on page 7 and reconciliation of GAAP to non-GAAP measures beginning on page 8.

(3) Amounts for December 31, 2001 are adjusted to reflect the conversion of 753,301 shares of preferred stock outstanding on such date into 1,506,602 shares of common stock, assuming automatic conversion of the preferred stock. Amounts for June 30, 2002, December 31, 2002 and June 30, 2003 are adjusted to reflect the conversion of 1,057,142 shares of preferred stock outstanding on such date into 2,114,284 shares of common stock, assuming automatic conversion of the preferred stock.

(4) Represents non-interest expense divided by the sum of net interest income and non-interest income for the periods shown. During the six months ended June 30, 2003, non-interest expense included $6.3 million in penalties related to unwinding repurchase agreements prior to maturity and approximately $250,000 in separation expense related to the resignation of a senior officer. For the six months ended June 30, 2003, the efficiency ratio excluding the penalties and separation expense would have been 64.70%. During the year ended December 31, 2002, non-interest expense included $1.2 million in IPO expenses recognized as our offering was postponed. For the year ended December 31, 2002, the efficiency ratio excluding the IPO expenses would have been 67.19%. The efficiency ratio excluding unwinding penalties and separation expense for the six months ended June 30, 2003 and the efficiency ratio excluding IPO expenses for the year ended December 31, 2002 are non-GAAP financial measures. See discussion of non-GAAP financial measures on page 7 and reconciliation of GAAP to non-GAAP measures beginning on page 8.

(5) During the six months ended June 30, 2003, the non-interest expense to average assets ratio included $6.3 million in penalties related to unwinding repurchase agreements prior to maturity and approximately $250,000 in separation expense related to the resignation of a senior officer. For the six months ended June 30, 2003, the annualized ratio of non-interest expense to average assets excluding the penalties and separation expense would have been 2.11%. During the year ended December 31, 2002, the non-interest expense to average assets ratio included $1.2 million in IPO expenses recognized as our offering was postponed. For the year ended December 31, 2002, the ratio of non-interest expense to average assets excluding the IPO expenses would have been 2.50%. The ratio of non-interest expense to average assets excluding unwinding penalties and separation expense for the six months ended June 30, 2003 and the ratio of non-interest expense to average assets excluding IPO expenses for the year ended December 31, 2002 are non-GAAP financial measures. See discussion of

non-GAAP financial measures on page 7 and reconciliation of GAAP to non-GAAP measures beginning on page 8.

(6) Interim period ratios are annualized.

(7) Percentage is calculated using the combined results of Resource Bank and TCBI for 1998.

* Not meaningful.

Non-GAAP Financial Measures

The footnotes to the Selected Consolidated Financial Information presented above include non-GAAP financial measures. See discussion of non-GAAP financial measures on page 7 and reconciliation of GAAP to non-GAAP measures beginning on page 8.

Predecessor Financial Statements

	Resource Bank	
	January 1 through December 18, 1998	October 3, 1997 (Inception) through December 31, 1997
	(In thousands)	
Selected Operating Data		
Interest income	$ 1,097	$ 86
Interest expense	377	10
Net interest income	720	76
Provision for loan losses	69	30
Net interest income after provision for loan losses	651	46
Non-interest income	60	3
Non-interest expense	1,057	271
Loss before taxes	(346)	(222)
Income tax expense		
Net loss	(346)	(222)
Selected Balance Sheet Data		
Total assets	19,605	8,060
Loans	11,102	1,532
Securities available for sale	3,175	
Deposits	15,166	3,386
Federal funds purchased		
Other borrowings		
Stockholders equity	4,292	4,638

MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview of Our Operating Results

Our bank was formed through the acquisition of Resource Bank, N.A., which itself had been organized in 1997. Upon completion of our $80 million private equity offering and acquisition of our predecessor bank, we commenced operations in December 1998. The amount of capital we raised, which we believe is the largest amount of start-up capital ever raised for a national bank, was intended to support a significant level of near-term growth and permit us to originate and retain loans of a size and type that our targeted customers, middle market businesses and high net worth individuals, would find attractive. Our large initial capitalization has resulted in reduced levels of return on equity to date. However, as we build our loan and investment portfolio we expect our return on equity to increase to normalized levels.

An important aspect of our growth strategy is the ability to service and effectively manage a large number of loans and deposit accounts in multiple markets in Texas. Accordingly, we created an operations infrastructure sufficient to support state-wide lending and banking operations. We believe that our existing infrastructure will allow us to grow our business over the next two to three years both geographically and with respect to the size and number of loan and deposit accounts without substantial additional capital expenditures.

During 1999 and 2000, we established a total of seven banking centers in key metropolitan markets in Texas. We also invested resources in hiring experienced bankers, which required a significant period of time for both recruiting and transitioning them from their previous employers. In conjunction with our roll-out of operations in 1999, we undertook a significant advertising and marketing campaign to increase brand name recognition of the traditional banking activities of our bank and of BankDirect, particularly in the Dallas/ Fort Worth business community. Once we had achieved our initial goals, we were able to significantly reduce our advertising expenses (from $2.3 million (which excludes approximately $1.9 million in expenses attributable to American Airlines AAdvantage® minimum mile requirements and co-branded advertising) in 2000 to $278,000 in 2001) and place more emphasis on targeted marketing to, and relationship-building efforts with, selected business groups, charities and communities. As we enter new market areas, we intend to evaluate the efficiency of selected advertising to brand our name and increase our recognition in those markets.

Our historical financial results reflect the development of our company in its early stages, notably in connection with initial start-up costs and the raising and retention of excess capital to fund our planned growth. In 1999 and 2000, we incurred significant non-interest expenses for the start-up and infrastructure costs described above, while revenue items gradually increased as we began to source and originate loans and other earning assets. In 2001, 2002 and the first half of 2003, we achieved improved levels of profitability as these costs have been spread over a larger asset base.

Our historical results also reflect the evolving role of BankDirect, the Internet banking division of our bank, in our business. When we launched BankDirect in 1999, we aimed to quickly establish a significant market position and establish a significant deposit base with which to fund our growth. Accordingly, we committed substantial resources to advertising for BankDirect and offered its deposit products at very attractive rates. Our efforts were successful, and BankDirect grew to account for approximately $369.7 million in deposits by the end of 2000, providing much of the liquidity we required to increase our lending activities during 2000. By early 2001, however, deposits at our traditional bank had grown to an amount sufficient to fund a much larger portion of our ongoing lending activities. As a result, we decided to reorient the focus of BankDirect towards higher balance depositors to reduce our management requirements and expenses. To this end, we restructured the account fees charged by BankDirect and lowered the rates on deposit products. This reorientation toward customers with higher deposit balances allowed us to significantly reduce our expenses related to BankDirect (from $6.8 million in 2000 (which excludes approximately $1.9 million in expenses attributable to American Airlines AAdvantage® minimum mile requirements and co-branded advertising) to $3.0 million in 2001, a decrease of over 56%), while substantially increasing the average balance held in our BankDirect accounts and lowering the total number of accounts serviced by BankDirect. As of June 30, 2003, BankDirect provided a significant, but not primary, source of funding for us, accounting for approximately 19% of our deposits.

Our operating results have improved significantly over the past several years as we moved into full operations. The table below shows the annual growth rate of our net interest income, net income, assets, loans and deposits:

	At or for December 31, 2002	Annual Growth Rate(1)	At or for December 31, 2001	Annual Growth Rate(1)	At or for December 31, 2000	Annual Growth Rate(1)	At or for December 31, 1999	Annual Growth Rate(1)
				(In thousands)				
Net interest income	$ 42,246	21%	$ 35,055	53%	$ 22,839	177%	$ 8,248	815%
Net income (loss)	7,343	26%	5,844	135%	(16,497)	*	(9,298)	*
Assets	1,793,282	54%	1,164,779	28%	908,428	122%	408,579	357%
Loans	1,122,506	24%	903,979	44%	629,109	176%	227,600	1,952%
Deposits	1,196,535	35%	886,077	11%	794,857	177%	287,068	1,692%

(1) The annual growth rate with respect to period data is the percentage growth of the item in the period shown compared to the most recently completed prior period. For purposes of calculating the 1999 annual growth rate, results of our bank and Resource Bank, our predecessor bank, for 1998 have been combined. The annual growth rate with respect to data as of a particular date is the percentage growth of the item at the date shown compared to the most recent prior date.

* Not meaningful.

The growth in our profitability is based on several key factors:

- we have successfully grown our asset base significantly each year;
- we have been able to maintain stable and diverse funding sources, resulting in increased net interest income from 2000 onward, despite a falling interest rate environment and the fact that most of our loans have floating interest rates;
- the growth in our asset base has resulted in annual growth of 815%, 177%, 53% and 21% in our principal earnings source, net interest income, in 1999, 2000, 2001 and 2002, respectively; and
- since the completion of our initial advertising and marketing campaigns and the reorientation of BankDirect, we have been able to tightly control non-interest expenses; this has contributed to a substantial improvement of our efficiency ratio from 176.8% in 1999 to 69.5% in 2002.

Six Months Ended June 30, 2003 Compared to the Six Months Ended June 30, 2002

We recorded net income of $6.9 million for the six months ended June 30, 2003 compared to $3.4 million for the same period in 2002. Diluted income per common share was $0.32 for 2003 and $0.15 for the same period in 2002. Returns on average assets and average equity were 0.74% and 10.87%, respectively, for the six months ended June 30, 2003, compared to 0.56% and 6.02%, respectively, for the same period in 2002.

The increase in net income for the six months ended June 30, 2003 over the same period of 2002 was primarily due to an increase in net interest income and non-interest income and the impact of reversing the deferred tax valuation allowance of $5.9 million, offset by an increase in non-interest expense. Net interest income increased by $4.8 million, or 24.5%, to $24.4 million for the six months ended June 30, 2003 compared to $19.6 million for the same period in 2002. The increase in net interest income was primarily due to an increase of $613.7 million in average earning assets, offset by a 66 basis point decrease in the net interest margin. Non-interest expense for the six months ended June 30, 2003 included approximately $250,000 in separation expense related to the resignation of a senior officer and $6.3 million in penalties related to unwinding repurchase agreements in June 2003 prior to maturity to lower funding costs. We unwound approximately $139 million of repurchase agreements and entered into new repurchase agreements with respect to a significant portion of that amount, with the remainder replaced with overnight funds. A significant portion of these overnight funds were replaced with deposits when we completed our acquisition of the outstanding deposit accounts of Bluebonnet Savings Bank FSB, which occurred on August 8, 2003. See Business Acquisition of Bluebonnet Savings Deposits. The impact on net interest income of these transactions was not material for the six-month period ended June 30, 2003, as these transactions occurred in June. Assuming a flat interest rate environment, we expect that these transactions will significantly lower our cost of funding through the remainder of 2003 and in 2004.

Excluding the impact of reversing the valuation allowance, unwinding penalties and separation expense, diluted income per share would have been $0.25. Income per share excluding the impact of reversing the valuation allowance, unwinding penalties and separation expense is a non-GAAP financial measure. Please see the discussion of non-GAAP financial measures beginning on page 7 for an explanation of why we believe this non-GAAP financial measure is useful to management and investors and the table beginning on page 8 for a reconciliation of diluted income per share excluding impact of reversing the valuation allowance, unwinding penalties and separation expense to diluted income per share, which is the most directly comparable financial measure presented in accordance with GAAP.

Non-interest income increased by $2.4 million, or 68.1%, during the six month period ended June 30, 2003 to $6.1 million, compared to $3.7 million during the same period in 2002. The increase was in part due to an overall increase in non-interest bearing deposits for 2003, which resulted in more service charges on deposit accounts. Also, our trust income increased by $95,000 to $587,000 during the six month period ended June 30, 2003 compared to $492,000 for the same period in 2002, due to continued growth in trust assets. During the six month period ended June 30, 2003, we had a gain on sale of securities of $686,000 due to our ability to realize substantial profits from sales of fixed-rate debt securities as a result of rapid declines in overall interest rates. Mortgage warehouse fees increased by $448,000 to $703,000 during the six month period ended June 30, 2003 from $255,000 in the same period in 2002. Also, we had bank owned life insurance (BOLI) income of $842,000 during the six month period ended June 30, 2003.

Non-interest expense increased by $9.5 million, or 56.6%, to $26.3 million during the six months ended June 30, 2003 compared to $16.8 million during the same period in 2002. This increase is primarily due to the incurrence of $6.3 million in penalties related to unwinding repurchase agreements prior to maturity in order to take advantage of historical lows in interest rates, which had decreased on similar repurchase agreements by approximately 1.4% since the time we entered into the original repurchase agreements. Salaries and employee benefits increased by $2.9 million due in part to an increase in total full-time employees from 201 at June 30, 2002 to 237 at June 30, 2003. The increase in salaries and employee benefits also included separation expenses of approximately $250,000 related to the resignation of a senior officer. In addition, we experienced losses related to forged checks of approximately $278,000 in the first half of 2003. We have taken steps to attempt to reduce these types of losses in the future. Occupancy expense decreased by $167,000 to $2.4 million during the six months ended June 30, 2003 compared to the same period in 2002 primarily related to a decrease in depreciation as many of our fixed assets are becoming fully depreciated. Advertising expense decreased $170,000 to $392,000 during the six months ended June 30, 2003 from $562,000 during the same period in 2002.

Year Ended December 31, 2002 Compared to Year Ended December 31, 2001

We recorded net income of $7.3 million for 2002 compared to $5.8 million for 2001. Diluted income per common share was $0.32 for 2002 and $0.30 for 2001. Returns on average assets and average equity were 0.54% and 6.27%, respectively, for 2002 compared to 0.58% and 6.44%, respectively, for 2001.

The increase in net income for 2002 was due to an increase in both net interest income and non-interest income partially offset by an increase in non-interest expenses. Net interest income increased by $7.2 million, or 20.5%, to $42.3 million for 2002 compared to $35.1 million for 2001. The increase in net interest income was primarily due to an increase of $319.5 million in average earning assets, offset by a 34 basis point decrease in the net interest margin. Non-interest expense included $1.2 million of IPO expenses recognized as our offering was postponed in October 2002 due to unfavorable market conditions. Excluding the IPO expenses, diluted income per share would have been $0.36. Income per share excluding IPO expenses is a non-GAAP financial measure. Please see discussion of non-GAAP financial measures beginning on page 7 for an explanation of why we believe this non-GAAP financial measure is useful to management and investors and the table beginning on page 8 for a reconciliation of diluted income per share excluding IPO expenses to diluted income per share, which is the most directly comparable financial measure presented in accordance with GAAP.

Non-interest income increased by $2.6 million in 2002 to $8.6 million, compared to $6.0 million in 2001. The increase was in part due to an overall increase in deposits for 2002, which resulted in more service charges on deposit accounts. Also, our trust income increased by $161,000, to $987,000 for 2002 compared to $826,000 for 2001, due to continued growth in trust assets. Mortgage warehouse fees increased by $402,000 to $693,000 for 2002 from $291,000 in 2001. Income from bank owned life insurance, or BOLI, policies that we purchased during 2002 totaled $660,000. Gain on sale of securities in 2002 was $1.4 million compared to $1.9 million in 2001.

Non-interest expense increased by $6.0 million in 2002 to $35.4 million compared to $29.4 million in 2001. The increase was due, in part, to an increase in total full-time employees from 198 at December 31, 2001 to 215 at December 31, 2002. IPO expenses of $1.2 million were recognized as our offering was postponed in October 2002 due to unfavorable market conditions. Advertising expenses increased to $1.2 million in 2002 compared to $278,000 in 2001. 2002 advertising expenses included direct marketing and branding for the traditional banking activities of our bank of $586,000 and for BankDirect of $12,000, as well as American Airlines AAdvantage® minimum mile requirements of $630,000 and co-branded advertising with American Airlines AAdvantage® of $8,000. BankDirect has been a member of American Airlines AAdvantage® travel benefits program since May 2000, offering AAdvantage awards to AAdvantage® members who open and maintain accounts with BankDirect. We did not purchase any miles in 2001 because the miles that we were contractually required to purchase in 2000 were sufficient to cover our mileage rewards to customers in 2001.

Year Ended December 31, 2001 Compared to Year Ended December 31, 2000

We recorded net income of $5.8 million for 2001 compared to a net loss of $16.5 million for 2000. Diluted income (loss) per common share was $0.30 for 2001 and $(0.95) for 2000. Returns on average assets and average equity were 0.58% and 6.44%, respectively, for 2001 compared to (2.42)% and (20.02)%, respectively, for 2000.

The increase in net income for 2001 was due to an increase in both net interest income and non-interest income and a substantial decrease in non-interest expenses. Net interest income increased by $12.2 million, or 53.5%, to $35.1 million for 2001 compared to $22.8 million for 2000. The increase in net interest income was primarily due to an increase of $317.0 million in average earning assets, combined with an 11 basis point increase in the net interest margin.

Non-interest income increased by $4.0 million in 2001 to $6.0 million, compared to $2.0 million in 2000. The increase was in part due to an overall increase in deposits for 2001, which resulted in more service charges on deposit accounts. Also, our trust income increased by $252,000, to $826,000 for 2001 compared to $574,000 for 2000, due to continued growth in trust assets. Mortgage warehouse fees increased by $287,000 to $291,000 in 2001 from $4,000 in 2000. Other non-interest income increased by $234,000 in 2001 to $1.1 million from $873,000 in 2000, primarily related to letter of credit fees, investment fees, rental income, and gain on sale of leases. Gain on sale of securities in 2001 was $1.9 million compared to $19,000 in 2000, due to our ability to realize substantial profits from sales of fixed-rate debt securities as a result of rapid declines in overall interest rates.

Non-interest expense decreased by $5.8 million in 2001 to $29.4 million compared to $35.2 million in 2000. The decrease was due, in part, to a reduction in total full-time employees from 234 at December 31, 2000 to 198 at December 31, 2001. 75% of this decrease in full-time employees from 2000 to 2001 was attributable to a reduction in BankDirect employees from 40 to 13. Also, we reduced advertising expenses to $278,000 in 2001 compared to $4.2 million in 2000. 2000 advertising expenses included direct marketing and branding for the traditional banking activities of our bank of $724,000 and for BankDirect of $1.6 million, as well as American Airlines AAdvantage® minimum mile requirements of $1.1 million and co-branded advertising with American Airlines AAdvantage® of $752,000. BankDirect has been a member of the American Airlines AAdvantage® travel benefits program since May 2000, offering AAdvantage® awards to AAdvantage® members who open and maintain accounts with BankDirect. We did not purchase any miles in 2001 because the miles that we were contractually required to purchase in 2000 were sufficient to cover our mileage rewards to customers in 2001. Also, a reduction in other non-interest expense was due to the accrual in 2000 of a $1.8 million contingent liability related to an agreement to provide merchant card processing for a customer who ceased operations and filed for bankruptcy in December 2000. Approximately $300,000 of this liability was reversed in 2001.

Net Interest Income

Net interest income was $24.4 million for the six months ended June 30, 2003 compared to $19.6 million for the same period of 2002. The increase was primarily due to an increase in average earning assets of $613.7 million for the six months ended June 30, 2003 compared to the same period in 2002. The increase in average earning assets from the six months ended June 30, 2002 included a $270.3 million increase in average net loans, which represented 65.5% of average earning assets for the six months ended June 30, 2003 compared to 77.0% for the same period in 2002. The decrease reflected management s decision to tighten lending standards during 2002 pending clearer signs of improvement in the U.S. economy. While we continue to apply conservative lending standards, loan growth in the second quarter of 2003 continued as net loans increased to $1.23 billion. Securities increased to 33.3% of average earning assets for the six months ended June 30, 2003 compared to 21.1% for the same period in 2002. We used additional securities in 2003 to increase our earnings by taking advantage of market spreads between returns on assets and the cost of funding these assets.

Average interest bearing liabilities increased $560.2 million for the six months ended June 30, 2003 compared to the same period in 2002, due, in part, to a $226.2 million increase in interest bearing deposits and a $319.5 million increase in other borrowings. Average borrowings were 26.3% of average total assets for the six months ended June 30, 2003 compared to 14.6% for the same period in 2002. The increase in average borrowings was primarily related to an increase in federal funds purchased and securities sold under repurchase agreements, and was used to supplement deposits in funding loan growth and securities purchases. The average cost of interest bearing liabilities decreased from 2.62% for the six months ended June 30, 2002 to 2.27% for the same period in 2003, reflecting the continuing decline in market interest rates and a $95.9 million increase in non-interest bearing deposits.

Net interest income was $42.3 million for the year ended December 31, 2002 compared to $35.1 million for the same period of 2001. The increase was primarily due to an increase in average earning assets of $319.5 million for 2002 as compared to 2001. The increase in average earning assets from 2002 included a $176.2 million increase in average net loans, which represented 74.0% of average earning assets for the year ended December 31, 2002 compared to 80.3% for 2001. The decrease reflected management s decision to tighten lending standards during 2002 pending clearer signs of improvement in the U.S. economy. Securities increased to 24.8% of average earning assets in 2002 compared to 18.2% in 2001.

Average interest bearing liabilities increased $268.0 million in 2002 compared to 2001, due, in part, to a $120.7 million increase in interest bearing deposits and a $146.2 million increase in other borrowings. Average borrowings were 18.2% of average total assets for 2002 compared to 10.1% in 2001. The increase in average borrowings was primarily related to an increase in federal funds purchased and securities sold under repurchase agreements, and was used to supplement deposits in funding loan growth and securities purchases. The average cost of interest bearing liabilities decreased from 4.35% for the year ended December 31, 2001 to 2.57% in 2002, reflecting the continuing decline in market interest rates and a $55.8 million increase in non-interest bearing deposits.

Net interest income increased by $12.2 million, or 53.5%, in 2001 to $35.1 million compared to $22.8 million in 2000. The increase in net interest income was primarily due to a significant increase in average earning assets. Average earning assets increased by $317.0 million during 2001, primarily due to continued growth in our lending portfolio. Additionally, the mix of earning assets improved during 2001. Average loans, which generally have higher yields than other types of earning assets, increased to 80.3% of average earning assets in 2001 compared to 64.5% of average earning assets in 2000.

Average interest bearing liabilities also increased by $269.9 million during 2001 compared to 2000. Of this amount, interest bearing deposits increased $186.6 million and borrowings increased $83.3 million. Average borrowings were 10.1% of average total assets for 2001 compared to 2.9% for 2000. The increase in borrowings was used to supplement deposits in funding the growth in loans. The average cost of interest bearing liabilities decreased in 2001 to 4.35% from 6.02% in 2000. The decrease was mainly due to the overall decline in market interest rates, as well as the additional lowering of rates on BankDirect deposits and a $51.0 million increase in non-interest bearing deposits.

Volume/ Rate Analysis

	Six Months Ended June 30,			Years Ended December 31,					
	2003/2002			2002/2001			2001/2000		
		Change Due to(1)			Change Due to(1)			Change Due to(1)	
	Change	Volume	Yield/Rate	Change	Volume	Yield/Rate	Change	Volume	Yield/Rate
					(In thousands)				
Interest income:									
Securities	$4,180	$ 9,231	$(5,051)	$ 4,724	$ 8,740	$ (4,016)	$ (2,848)	$ (1,811)	$ (1,037)
Loans	5,351	7,755	(2,404)	(4,849)	13,464	(18,313)	18,954	34,432	(15,478)
Federal funds sold	(49)	4	(53)	(337)	7	(344)	(1,198)	(846)	(352)
Deposits in other banks	4	15	(11)	10	11	(1)	(83)	1	(84)
	9,486	17,005	(7,519)	(452)	22,222	(22,674)	14,825	31,776	(16,951)
Interest expense:									
Transaction deposits	(10)	60	(70)	(414)	255	(669)	383	584	(201)
Savings deposits	168	552	(384)	(7,214)	(452)	(6,762)	(2,621)	4,497	(7,118)
Time deposits	788	2,612	(1,824)	(2,908)	6,558	(9,466)	2,294	5,734	(3,440)
Borrowed funds	3,742	4,487	(745)	2,893	5,416	(2,523)	2,553	5,218	(2,665)
	4,688	7,711	(3,023)	(7,643)	11,777	(19,420)	2,609	16,033	(13,424)
Net interest income	$4,798	$ 9,294	$(4,496)	$ 7,191	$10,445	$ (3,254)	$12,216	$15,743	$ (3,527)

(1) Changes attributable to both volume and yield/rate are allocated to both volume and yield/rate on an equal basis.

Net interest margin, the ratio of net interest income to average earning assets, decreased from 3.47% for the six months ended June 30, 2002 to 2.81% for the same period in 2003. This decrease was due primarily to the falling rate environment in which our balance sheet was asset sensitive, which means we had more loans repricing than deposits over the year. In addition, a larger portion of our assets were invested in securities, which generally have a lower yield than loans. The cost of interest bearing liabilities decreased by 35 basis points during the six months ended June 30, 2003, primarily due to overall lower market interest rates, and an increase in non-interest bearing deposits.

Net interest margin decreased from 3.62% in 2001 to 3.28% in 2002. This decrease was due primarily to the falling rate environment in which our balance sheet was asset sensitive, which means we had more loans repricing than deposits over the year. The cost of interest bearing liabilities decreased by 178 basis points in 2002, primarily due to overall lower market interest rates, and an increase in non-interest bearing deposits.

Net interest margin increased from 3.51% in 2000 to 3.62% in 2001. This increase was due primarily to lower cost of funds and continued strong asset yields in a falling rate environment. The cost of interest bearing liabilities decreased by 167 basis points in 2001, primarily due to lower interest rates offered as a result of a reorientation of BankDirect, overall lower market interest rates, and an increase in non-interest bearing deposits.

Consolidated Daily Average Balances, Average Yields and Rates

	Six Months Ended June 30,					
	2003			2002		
	Average Balance	Revenue/ Expense(1)	Yield/ Rate	Average Balance	Revenue/ Expense(1)	Yield/ Rate
	(In thousands, except percentage data)					
Assets						
Taxable securities	$ 583,384	$ 10,685	3.69%	$ 241,165	$ 6,505	5.44%
Federal funds sold	21,262	130	1.23%	20,850	179	1.73%
Deposits in other banks	951	7	1.48%	161	3	3.76%
Loans	1,163,993	30,677	5.31%	891,126	25,326	5.73%
Less reserve for loan losses	15,525			12,919		
Loans, net	1,148,468	30,677	5.39%	878,207	25,326	5.82%
Total earning assets	1,754,065	41,499	4.77%	1,140,383	32,013	5.66%
Cash and other assets	132,077			70,312		
Total assets	$ 1,886,142			$ 1,210,695		
Liabilities and Stockholders Equity						
Transaction deposits	$ 61,038	$ 233	0.77%	$ 49,007	$ 243	1.00%
Savings deposits	394,404	3,269	1.67%	334,780	3,101	1.87%
Time deposits	550,114	7,477	2.74%	395,618	6,689	3.41%
Total interest bearing deposits	1,005,556	10,979	2.20%	779,405	10,033	2.60%
Other borrowings	496,061	5,734	2.33%	176,578	2,372	2.71%
Long-term debt	14,530	380	5.27%			
Total interest bearing liabilities	1,516,147	17,093	2.27%	955,983	12,405	2.62%
Demand deposits	230,497			134,597		
Other liabilities	11,702			7,012		
Stockholders equity	127,796			113,103		
Total liabilities and stockholders equity	$ 1,886,142			$ 1,210,695		
Net interest income		$ 24,406			$ 19,608	
Net interest income to average earning assets (net interest margin)			2.81%			3.47%
Net interest spread			2.50%			3.04%

(1) The loan averages include loans on which the accrual of interest has been discontinued and are stated net of unearned income.

	Year Ended December 31,								
	2002			2001			2000		
	Average Balance	Revenue/ Expense(1)	Yield/ Rate	Average Balance	Revenue/ Expense(1)	Yield/ Rate	Average Balance	Revenue/ Expense(1)(2)	Yield/ Rate
	(In thousands, except percentage data)								
Assets									
Taxable securities	$ 318,864	$15,484	4.86%	$ 175,945	$10,760	6.12%	$202,955	$13,608	6.70%
Federal funds sold	14,874	243	1.63%	14,688	580	3.95%	28,025	1,778	6.34%
Deposits in other banks	558	28	5.02%	351	18	5.13%	348	101	29.02%
Loans	966,964	54,387	5.62%	787,879	59,236	7.52%	424,782	40,282	9.48%
Less reserve for loan losses	13,226			10,335			4,619		
Loans, net	953,738	54,387	5.70%	777,544	59,236	7.62%	420,163	40,282	9.59%
Total earning assets	1,288,034	70,142	5.45%	968,528	70,594	7.29%	651,491	55,769	8.56%
Cash and other assets	77,688			47,789			31,023		
Total assets	$1,365,722			$1,016,317			$682,514		
Liabilities and Stockholders Equity									
Transaction deposits	$ 52,155	$ 491	0.94%	$ 40,673	$ 905	2.23%	$ 19,198	$ 522	2.72%
Savings deposits	349,128	6,671	1.91%	360,865	13,885	3.85%	283,594	16,506	5.82%