

Bank of the Ozarks, Inc.
Conference Call – July 11, 2016
Transcript – Prepared Remarks

Note: Administrative communications of the operator and other greetings and social exchanges of no substantial import have been omitted from this transcript.

Good morning, I am Susan Blair, Executive Vice President in charge of Investor Relations for Bank of the Ozarks. The purpose of this call is to discuss the Company's results for the quarter just ended and our outlook for upcoming quarters.

Our goal is to make this call as useful as possible to you in understanding our recent operating results and outlook for the future. A transcript of today's call, including our prepared remarks and the Q&A, will be posted on bankozarks.com under the Investor Relations tab. During today's call, and in other disclosures and presentations, we may make certain forward-looking statements about our plans, goals, expectations, thoughts, beliefs, estimates and outlook, including statements about economic, competitive, real estate, credit and interest rate conditions, including expectations for further changes in monetary and interest rate policy by the Federal Reserve; revenue growth; net income and earnings per share; net interest margin; net interest income; non-interest income, including service charge income, mortgage lending income, trust income, bank owned life insurance income, other income from purchased loans, and gains on sales of foreclosed and other assets; non-interest expense, including acquisition-related, systems conversion and contract termination expenses; expenses with regard to regulatory compliance, including the impact on non-interest expense from our total assets exceeding \$10 billion; our efficiency ratio, including our long-term goal for achieving a sub-30% efficiency ratio and the impact that our pending mergers will have on our efficiency ratio; asset quality and our various asset quality ratios; our expectations for net charge-offs and our net charge-off ratios; our allowance for loan and lease losses; growth in total assets, both as a result of organic growth and acquisitions; our expectations for loan and lease growth, including growth from unfunded closed loans and growth from loans currently in the underwriting and closing processes; growth in earning assets and changes in our mix of growth in earning assets, including our expectations for growth in non-CRE asset categories; expected cash flows of our purchased loan portfolio; changes in the value and volume of our securities portfolio; deposit growth, including growth from existing offices and acquisitions; expectations regarding our cost of interest bearing deposits; the opening, relocating and closing of banking offices;

expectations regarding our pending acquisitions, including our belief that such acquisitions will enhance our community banking, loan administration and other business functions and provide capabilities in technology and innovation which will be transformational to customer experiences and operational efficiency; our goals and expectations for additional acquisitions; our expectations regarding capital adequacy and growth; and changes and growth in our staff.

You should understand that our actual results may differ materially from those projected in any forward-looking statements due to a number of risks and uncertainties, some of which we will point out during the course of this call. For a list of certain risks that may impact any of these forward-looking statements and other risks associated with our business, you should refer to the Forward-Looking Information section of our periodic public reports, the Forward-Looking Statements caption of our most recent earnings release, and the description of certain Risk Factors contained in our most recent Annual Report on Form 10-K, all as filed with the SEC. Forward-looking statements made by the Company and its management are based on estimates, projections, beliefs and assumptions of management at the time of such statements, and are not guarantees of future performance. The Company disclaims any obligation to update or revise any forward-looking statement based on the occurrence of future events, the receipt of new information or otherwise. Any references to non-GAAP financial measures are intended to provide meaningful insights and are reconciled with GAAP in our earnings press release.

Let me turn the call over to our Chairman and Chief Executive Officer, George Gleason.

George Gleason:

Thank you, Susan, and thank you all for joining our call today. I want to briefly discuss several subjects before I turn the call over to Greg and Tyler.

First, we are very pleased with our record net income for both the first and second quarters of this year. Our second quarter net income was \$54.5 million, a 21.7% increase over last year's second quarter and a 5.4% increase over this year's first quarter. Our second quarter results included quarterly records for net interest income, service charge income, mortgage income and trust income, as well as a 4.82% net interest margin, a 35.4% efficiency ratio, excellent loan growth and some record asset quality ratios.

Clearly we have continued to hit on all cylinders with our very conservative and disciplined business strategy.

Our long-standing focus on conservative underwriting standards and credit quality is a critical element of our business strategy. Since the “Great Recession,” we have focused even more than ever before on loan transactions with various combinations of four attributes: great properties, strong and capable sponsors, very low leverage and defensive loan structures. The rewards for our discipline and this focus were evident in our credit quality metrics for the quarter just ended. At June 30, 2016, excluding purchased loans, our nonperforming loans and leases as a percent of total loans and leases were just 0.09%; our nonperforming assets as a percent of total assets were just 0.25%; and our loans and leases past due 30 days or more, including past due non-accrual loans and leases, to total loans and leases, were just 0.22%. These ratios of nonperforming loans and leases and past due loans and leases are our best ever as a public company, setting new records for the second consecutive quarter. These ratios clearly reflect our pristine asset quality.

These recent ratios are a continuation of a multi-decade long commitment to excellent asset quality, which has resulted in our having asset quality consistently better than the industry as a whole. In our 19 years as a public company, our net charge-off ratio has averaged 37% of the industry’s net charge-off ratio, and we have beaten the industry’s net charge-off ratio in every single year.

During the quarter just ended, we continued to focus on originating high quality loans at very low leverage. Of course, the largest component of our loan and lease portfolio is our Real Estate Specialties Group, or RESG, portfolio which increased to 69.5% of the funded balance, and 90.5% of the unfunded balance of our total non-purchased loans and leases at June 30, 2016. At quarter-end, our average loan to cost for the RESG portfolio was a very conservative 49.1%, and our average loan to appraised value was even lower at just 42.7%. The low leverage of this portfolio exemplifies our very conservative credit culture.

Certainly these recent asset quality ratios, combined with the low leverage of so many of our loans, justify our confidence in the quality and durability of our loan and lease portfolio. This portfolio has been built to withstand another “Great Recession.” While we don’t expect another “Great

Recession,” we believe we are superbly prepared if one occurs.

Our annualized net charge-off ratio for total loans and leases for both the second quarter and the first six months of this year were just 6 basis points. While we are not changing our 5 to 20 basis points guidance for our 2016 net charge-off ratio for total loans and leases, we now think we are likely to achieve a 2016 total net charge-off ratio even better than our favorable ratios of 16 basis points in 2014 and 17 basis points in 2015.

Even considering our very conservative underwriting, our extreme discipline and our four-fold focus on great properties, strong and capable sponsors, very low leverage and defensive loan structures, we are achieving exceptionally good loan and lease growth. Clearly we are providing our borrowers a compelling value equation in which our expertise and ability to reliably execute transactions with both speed and excellence justify our borrowers accepting conservative loan structures. In the quarter just ended, our non-purchased loans and leases grew \$624 million and for the first six months of this year grew \$1.69 billion. Our excellent second quarter growth was achieved notwithstanding a large volume of loan payoffs, as anticipated. In the quarter just ended, our unfunded balance of closed loans also increased by \$968 million. During the first six months of 2016, our unfunded balance of closed loans has increased by \$1.55 billion, growing to a record \$7.35 billion at June 30, 2016.

In our January conference call, we increased our guidance for our full year 2016 growth in non-purchased loans and leases to at least \$3.0 billion. We are now further increasing our 2016 guidance for growth in non-purchased loans and leases to \$3.5 billion based on our excellent year-to-date growth, the growth in our customer base, our pipeline of transactions currently in underwriting and closing, and our largest ever unfunded balance of closed loans.

RESG, under the expert leadership of Dan Thomas, continued to be the primary driver for our loan growth in the quarter just ended, as it has been in most quarters in recent years. Dan started this team for us 13 years ago. Its priorities have always been: first on asset quality, second on profitability, and third on growth. As a result of this emphasis on quality, RESG has had only two loans result in losses in 13 years. If you total both the charge-offs and the subsequent OREO write-downs on those loans, RESG’s total credit losses since inception are \$10.4 million. That’s just a nine basis point annualized

loss ratio over the entire history of RESG. In recent years RESG has tended to be even more conservative. You can see this in the leverage ratios for the RESG portfolio. As we previously mentioned, and assuming every RESG loan is fully advanced, at June 30, 2016 RESG's average loan to cost is approximately 49.1% and average loan to appraised value is approximately 42.7%. That compares to the 2005 to 2007 time frame when our loan to cost percentage on such loans was typically in the low 70's and our loan to appraised value percentage was typically in the high 60's. Or to state it another way, our leverage today is more than 20 percentage points lower than our leverage on loans in this portfolio in the years preceding the "Great Recession." Obviously our RESG portfolio held up extremely well during the "Great Recession," with only two loans resulting in losses, and with the leverage of our current RESG portfolio more than 20 percentage points lower, there is substantial reason to believe that this current portfolio will perform equally well, or even better, if we were to incur a comparable economic downturn.

As previously mentioned, at June 30, 2016, RESG accounted for the majority, specifically 69.5%, of our total non-purchased loans and leases and an even higher 90.5% of the unfunded balance of closed loans. Given the exceptional track record of this division, the low leverage of this portfolio, and the significant diversification of the RESG portfolio by both geography and product type, you can see why we are so confident in how well our asset quality will hold up under a broad array of economic and real estate market scenarios.

Another benefit of RESG accounting for a greater percentage of our total non-purchased loans is RESG's consistency in collecting loan origination fees and the corresponding increase in our level of net deferred loan fees. As we have discussed in previous calls, in accordance with generally accepted accounting principles, we defer both loan origination fees and loan origination costs. At June 30, 2016, we had \$35.6 million in net deferred credits, meaning that we had \$35.6 million more in unamortized deferred loan origination fees than unamortized deferred loan origination costs. This net deferred credit has increased \$7.9 million from \$27.7 million at yearend 2015. This larger net deferred credit, along with the \$72.2 million valuation discount on our purchased loans at June 30, 2016, has favorable implications for future earnings.

Throughout my 37 years as Chairman and Chief Executive Officer, our focus has been on real estate lending. When bank regulators first issued their CRE concentration guidelines in 2006, our CRE ratios were well over the guidelines, just as our CRE ratios are today. We were comfortable then with our level of CRE lending, and, because of all the factors we have just discussed, we are even more comfortable with the quality of our portfolio, our exceptional rate of portfolio growth and our CRE levels today. The regulatory guidelines mandate that, if you have a CRE concentration, extra safeguards should be in place. We totally agree with that, and we have robust policies, procedures and processes in place to assure the quality of our CRE portfolio and to effectively measure, monitor and manage our CRE concentrations. Of course, our specialized expertise in CRE and the conservatism we employ in our CRE lending are among our most critical safeguards. Our track record, including our track record through the “Great Recession,” speaks for itself.

Since RESG’s loans are, on average, our best quality and lowest leverage loans, with our best sponsors and best properties, and are our best underwritten, documented and serviced loans, we are comfortable with RESG growing to be a bigger and bigger part of our portfolio. We believe RESG is where we have the greatest competitive advantage. Nevertheless, we have been working over the last several years to improve our competitive advantage in other areas. This includes, among other things, developing the government guaranteed lending capabilities we acquired in our OMNIBANK acquisition, developing the poultry lending capabilities we acquired in our Summit Bank acquisition, developing the consumer and small business lending capabilities and the indirect marine and RV consumer lending capabilities we are acquiring with the Community & Southern Bank acquisition, and expanding our proven legacy leasing and investment securities portfolio platform. While we expect our CRE lending volumes to continue to increase significantly, we expect these other areas to grow even faster. By 2018, our goal is for CRE to account for approximately 57% of our quarterly growth in earning assets and for our non-CRE asset categories, including those just mentioned, to account for approximately 43% of our quarterly growth in earning assets. You should see this evolution in the mix of earning asset growth beginning this quarter, accelerating in future quarters, and reaching our goal of a roughly 57%/43% mix sometime in 2018. Again, we are not slowing RESG’s CRE growth, and we expect RESG’s growth to accelerate. On the other hand, we have put in place various elements, which we have been working on for some time, to balance that growth with other high-quality, good-yielding earning asset elements. This should allow us to continue our excellent

growth rates in non-purchased loans and leases, while further diversifying our portfolio.

We think our two pending acquisitions, which we expect to close on the 20th and 21st of this month, are of particular strategic importance and value. Our pending acquisition of Community & Southern Bank, which we announced in October last year, will be our largest acquisition to date. Community & Southern provides us 46 strategically located and highly complementary Georgia banking offices and one Florida banking office, a large number of very talented bankers, particular expertise in both direct and indirect consumer lending and small business lending, an important loan operations group, two important loan and business analytics groups, and numerous other team members and capabilities which will enhance our community banking, loan administration and other business functions. Our pending acquisition of C1 Bank, which we announced in November last year, will provide us 33 strategically located and highly complementary Florida offices, including offices in some of Florida's highest growth and strongest economic markets. We believe that C1's unique culture and leadership in technology and innovation will be transformational in our quest to be an industry leader in best-in-class customer experiences and operational efficiency. We appreciate the work of our various regulators in approving these transactions, and we look forward to closing both transactions and completing integration of these operations in the weeks and months ahead.

While we have been working on the typical things needed to close these transactions, we have been very focused on accelerating the effective integration of these two acquired entities. For example, teams from all three banks have been working intensely for months to fully synchronize all aspects of consumer and small business lending products, pricing, policies, procedures and documentation. As a result, we have already synchronized and adopted each other's best practices in regard to consumer and small business lending in legacy Bank of the Ozarks and Community & Southern Bank, and we will roll out this platform at C1 Bank within two weeks following closing. This is just one example of many. Achieving this level of synchronization prior to closing, or shortly following closing, should greatly enhance our outcomes on both transactions.

Let me turn the call over to our Chief Financial Officer, Greg McKinney.

Greg McKinney:

We often talk about our Company's focus on three disciplines, those being net interest margin, efficiency and asset quality. George covered asset quality, so let me discuss net interest margin and efficiency.

Net interest income is traditionally our largest source of revenue and is a function of both the volume of average earning assets and net interest margin. Our second quarter 2016 net interest income was a record \$119.0 million. We enjoyed a very positive trend in net interest income in the quarter just ended as a result of excellent growth in average earning assets, namely our growth in non-purchased loans and leases. This robust growth more than offset the ten basis point reduction in our net interest margin from 4.92% in this year's first quarter to 4.82% in this year's second quarter. As a result, net interest income increased \$6.5 million in the quarter just ended compared to this year's first quarter, and that is after having increased \$6.0 million in this year's first quarter compared to last year's fourth quarter. As we have previously stated, we expect our net interest margin to decline in 2016, but, as in the first two quarters of this year, we expect substantial loan and lease growth to continue to drive significant quarter-to-quarter increases in net interest income.

Achieving a superb net interest margin continues to be one of our key goals, and, although there has been pressure on our net interest margin in recent years, at 4.82% we continue to be among the best in the industry.

In recent years we have focused on decreasing our loan-to-cost and loan-to-value on loans to reduce credit risk, and we have focused on originating more variable rate loans with floors and fewer fixed rate loans to reduce interest rate risk. While we believe these actions have given our portfolio a very favorable credit and interest rate risk profile, these actions have also lowered our average yield on new loans, but we believe being more conservatively positioned is worth giving up some margin. At June 30, we had increased variable rate loans to 81.9% of our total non-purchased loans and leases, and we had floors in 91.9% of our variable rate loans. No matter which direction interest rates move, or, if they don't move at all, we are well positioned. If interest rates increase, our high percentage of variable rate loans should result in a nice increase in our net interest income compared to our baseline scenario. If interest rates decrease, and even in an unlikely scenario where we would have negative U.S. sovereign

debt yields, our having floors in 91.9% of our variable rate loans should protect our yield on our current portfolio.

Let me switch to efficiency. Traditionally we have been among the most efficient bank holding companies in the U.S., and our 35.4% efficiency ratio in the quarter just ended and 35.5% efficiency ratio for the first six months of 2016 further enhance our excellent standing among the nation's most efficient banks.

While our efficiency ratio will vary from quarter to quarter, especially in quarters where we have significant unusual items of income and non-interest expense, we have stated in recent conference calls that we expect to see a generally improving trend in our efficiency ratio in the coming years. This is predicated upon a number of factors, including our expectation that we will ultimately utilize a large amount of the current excess capacity of our extensive branch network and our expectation that we will achieve significant efficiencies over time from our pending acquisitions, including efficiencies from the adoption of Community & Southern Bank's consumer and small business lending platform and the deployment of numerous technology applications from the C1 Labs technology and innovation group. By fully leveraging these factors, among others, we hope to achieve an improving efficiency ratio over the next several years and ultimately our goal of a sub-30% efficiency ratio. With our 35.4% efficiency ratio in the quarter just ended, ultimately reaching a sub-30% efficiency ratio seems achievable.

We will incur additional unusual items of non-interest expense in future quarters, including non-interest expense related to the closing and core systems conversions of acquisitions. As for our two pending acquisitions, Community & Southern Bank and C1 Bank, we expect acquisition-related and systems conversion expenses to be incurred in each remaining quarter of 2016. We expect both transactions will close later this month, and we anticipate core systems conversions and certain back office consolidations for Community & Southern Bank in late August and for C1 Bank in mid-October. These acquisitions will likely increase our efficiency ratio for the remainder of 2016, especially considering the acquisition-related and systems conversion expenses, but, as already noted, we believe these acquisitions will help us achieve an improving efficiency ratio longer term. Our guidance regarding an improving efficiency ratio in future years considers the impact of our having exceeded \$10 billion in total assets, our

expectations for continued organic growth and our two pending mergers, but it does not consider the potential impact of any future acquisitions.

Before I turn the call over to Tyler, I want to discuss our capital position. During the first six months of this year, our total assets grew \$2.40 billion, or 24.3%, and that number is not annualized. Obviously that is a great organic growth rate and continues a trend of outsized organic growth. While our organic growth in recent years has been notable, the much more important facts are these. First, we believe the loans we have originated in the past 2 ½ years are among the highest quality loans we have ever originated contributing to improvement in our excellent credit quality. Second, we have been able to achieve this growth while maintaining one of the best net interest margins in the industry. We have always believed that we could raise capital as needed to support high quality, good yielding organic growth. In the closing weeks of June, we successfully completed a \$225 million sub debt issuance providing Tier 2 capital to support our continued growth. This sizeable sub debt issuance follows a registered direct placement of \$110 million of common stock last December.

Even after our tremendous balance sheet growth in recent years, and including our excellent growth in the quarter just ended, we continue to be well capitalized by all applicable regulatory standards. But our internal policies for capital adequacy are well above the current regulatory requirements. Our internal policies mandate that we maintain well capitalized status in accordance with the fully phased-in 2019 Basel III standards, including the capital conservation buffer. With our recent sub debt issuance, we currently have substantial capital in excess of our self-imposed capital standards to support continued growth. We will continue to monitor our capital position in light of our significant growth opportunities. Even with our strong profitability and substantial accumulation of retained earnings, continued organic growth rates well in excess of our growth rate of retained earnings will eventually require us to add additional capital. With our focus on excellent profits and pristine asset quality, we are confident that we will continue to be able to effectively and efficiently access capital markets as needed to support our high quality, good-yielding growth.

Now, let me turn the call over to our Chief Operating Officer and Chief Banking Officer Tyler Vance.

Tyler Vance:

We have long expected that, within reasonable limits, we could accelerate deposit growth as needed to fund our loan and lease growth. In the first six months of 2016, our deposits grew \$2.22 billion, providing sufficient funds to pay off our short-term borrowings outstanding at yearend, support our excellent loan and lease growth, and accumulate surplus cash of approximately \$709 million at June 30, 2016. Currently, we have 48 offices in 31 cities in “spin-up” mode offering various deposit specials along with an enhanced level of marketing activity. Our existing branch network continues to have substantial untapped deposit capacity and we believe that capacity is sufficient to fund our expected loan and lease growth over the next two to three years. Our two pending acquisitions should provide additional deposit growth capacity to support even further growth. Additionally, possible future acquisitions or *de novo* branch additions, or a combination thereof, should provide additional deposit growth capacity as may be needed in the future.

Since 2010 we have acquired many offices through our 13 acquisitions, providing significant capacity for deposit growth. You can get some idea of the magnitude of this capacity from the FDIC’s most recent branch deposit share data as of June 30, 2015. At that time we had 4.05% of the branches in the 93 cities in the seven states, excluding New York, where we accept deposits, but we had only 0.88% of the total deposits in those 93 cities. This suggests that we have billions of dollars of deposit growth potential inherent within our existing branch network. As a result, we have opened only a few *de novo* offices in recent years where compelling opportunities arose. Today we have 177 offices in nine states, and that total should increase to over 250 offices upon completion of our two pending acquisitions, providing further capacity for deposit growth.

We consider net growth in core checking accounts as our most important deposit metric. Last year we achieved record annual growth in our number of net new core checking accounts, with approximately 12,232 net new accounts added, and that does not include the addition of accounts from acquisitions. Our core account growth accelerated in the first six months of this year with approximately 8,447 net new core checking accounts added. Our excellent checking account growth has been an important contributor to our having achieved record service charge income in 2015 and each of the first two quarters of this year.

In our January conference call, we said we expected our cost of interest-bearing deposits would increase between three and seven basis points in each quarter of 2016 due to accelerated deposit gathering activities to fund growth. In the quarter just ended, our cost of interest-bearing deposits increased seven basis points from the first quarter of this year, after having increased nine basis points in this year's first quarter compared to the fourth quarter of last year. We hope to see continued moderation in this rate of increase in future quarters. We continue to believe that, notwithstanding the higher increase in the first quarter, the average quarterly increase in our cost of interest-bearing deposits in 2016 will be in line with the previous three to seven basis points guidance, although toward the upper end of that range.

Organic growth of loans, leases and deposits continues to be our top growth priority, and we have demonstrated our ability to achieve substantial growth apart from acquisitions. With that said, M & A activity continues to be another focus for us, as we believe M & A provides significant opportunities to augment our robust organic growth. We will continue to be active in identifying and analyzing M & A opportunities, and we believe an active and disciplined M & A strategy will allow us to continue to create significant shareholder value. Our two pending transactions, which combined account for approximately \$6.4 billion in total assets, have been our primary M & A focus over the last few quarters, and will continue to be our primary focus in the current quarter. Once these two large transactions close and are successfully integrated, we expect to become more active in looking at future opportunities.

Now, let me turn the call back to George Gleason.

George Gleason:

I want to thank our very talented and hard-working team of bankers across our Company for achieving our excellent second quarter results. The quality of our Company, our assets and our financial performance has never been better, and this is because we have a championship team with the skills, discipline, work ethic and commitment we need to deliver outstanding results for our customers and our shareholders. As strong as our team is today, it only gets better with the addition of many outstanding team members from the Community & Southern Bank and C1 Bank acquisitions. We look forward to officially welcoming these new team members to the Bank of the Ozarks team.

Let me close with one final thought. We have a long tradition of executing very well while growing rapidly. From 1994 through 2009, our growth was almost all organic, as we opened *de novo* banking offices throughout Arkansas and Texas with great effect. From 2010 to the present, our growth has been a combination of strong organic growth enhanced by 13 acquisitions, soon to be 15 acquisitions. In the last three quarters, our organic growth has hit record levels with our balance sheet growing \$2.95 billion organically over those three quarters, bringing us to \$12.3 billion in total assets at June 30. In the coming quarters, we expect organic growth to continue at or near the recent pace, and we would not be surprised to see our organic growth accelerate. With the closing of our two pending transactions and our expected organic growth, our total assets could be close to, or in excess of, \$20 billion at year end with a strong organic growth trajectory in place for future years. We have been working hard in recent years, and particularly recent quarters, to put in place the enhanced infrastructure needed to effectively manage and operate as a much larger bank of \$20 billion and well beyond. This building of infrastructure has been broad-based across most aspects of our Company, including the implementation of new core operating systems in 2014, the addition of a new primary data center in 2015, and continuing with our numerous ongoing initiatives including the significant expansion of our enterprise risk management functions. We will add important additional elements of infrastructure through our pending acquisitions. We have and will continue to proactively prepare for significant growth. We believe we are well positioned to deliver great products and services to our rapidly growing customer base and great returns to our shareholders.

That concludes our prepared remarks. At this time we will entertain questions. Let me ask our operator to once again remind our listeners how to cue in for questions.

Transcript of Q & A

Tim Abrazilla – *Wells Fargo Securities*

George, maybe the first question is to just talk a little bit about the geographic diversity that you saw within the loan growth this quarter, where did much of that come from?

George Gleason:

It was very broad-based and came from pretty much across the footprint. On a net basis, I really can't tell you where that came from because we have, as we mentioned and as we had expected, a large number of loan payoffs. So on a net-net basis, I haven't really calculated that, but we originated new credits literally across the country from California or Washington, Denver to New York and Miami and pretty much all points in between, it was a broad-based origination quarter.

Tim Abrazilla:

And then maybe just more broadly speaking, can you talk about the competition and just overall markets of New York, Texas and Southern Florida, what kind of incremental information have you picked up over the last three months and just general trends there?

George Gleason:

A lot of our competitors tend to move as a pack and are heavily driven by headline risk and headline perceptions of market conditions. We have always tried to have a much more nuanced and intelligent and deeply analytic approach to originating credits. You can read the headlines and run with the herd, but when you do you miss tremendous opportunities and you often are running in the wrong direction. So what we have tried to do is ignore the headlines to a great extent. I mean, certainly you have to take larger macroeconomic and market themes into account, but we have really tried to not let that drive our decisions. But instead to look at the supply/demand metrics of each sub-market market and macro market and the relative competitive position of each product in the market and do a much, much deeper level of analysis on projects. So as a result of that, we are finding tremendous opportunities in Manhattan, Miami, Houston, Dallas as well as markets that probably have gotten better headlines, such as California, Seattle and Denver. So we are really doing our homework as we have always done and really developing detailed supply/demand analytics and models on the market and finding great business

in a lot of markets where you are seeing some fairly negative headlines. And I will give you an example of that. We have, about 10 or 11, condo projects in South Florida that run all the way from Fort Lauderdale through Miami and down to Sunny Isles. Our average loan to cost on those projects, assuming every loan is fully funded, is 36% loan to cost. Our average loan to appraised value based on discounted net appraised value on those projects is 29%. And I think all of these projects have presale contracts in place that run from somewhere in the high-50s, I believe, low-50s perhaps, all the way up to 100% pre-sold in one case. So you are seeing projects, high-quality projects develop. We are in these projects at a very low basis. They are sizable presales that ensure the exit of our financing in every transaction, even if some of the presales fall out, and these presales were backed by deposits that range from 20% to 30% initially, up to 50% as the project goes on, that are non-refundable deposits. So if you do your analytics and you really look at the projects and you really look at the sub-market, you are really looking at the supply/demand, there is great business to be done in South Florida, there is great business to be done in Manhattan, there is great business to be done in Houston and Dallas and markets all across the country. We've been very fortunate to continue to find tremendous opportunities at very low leverage. And you will note that the weighted average loan to cost and the weighted average loan to value of our portfolio, which was already extremely low at the end of the last quarter, went down another three-tenths or four-tenths of 1% in the quarter just ended, once again reflecting just the extreme conservatism that we employ in managing our credit function.

Tim Abrazilla:

And then just maybe one last one for Tyler, looking at the increase in funding costs, it seems like much of that is driven by time deposits, maybe just talk a little bit about where time deposits fall in the promotional scheme of things right now and how that should trend going forward?

Tyler Vance:

Yes. So most of our spin-up markets, where we are offering deposit specials are in fact certificates of deposits. Those range anywhere from a 10-month term to a 15-month term and ranging rates from 1% to 1.35% rate and we are monitoring those markets and those competitors on a weekly basis. We have seen a little moderation in pricing in some markets, so we will probably look to lower a little bit of our rate in the 15-month term that we have been offering as high as 1.35%, depending on which market. But

most of those specials at this point have been CD specials, we are doing very little money market, premium pricing. It's really all on the CD side.

Matt Olney – *Stephens, Inc.*

George thanks for all of the good details on the RESG credit quality. Can you speak to if there are any RESG loans today that are classified, and if not, when was the last time there was a classified RESG loan?

George Gleason:

We have not had an RESG classified loan probably in 5 years Matt. And there are no classified RESG loans today. I don't think we have had a 30-day past due RESG loan in probably 5 years. So that portfolio, while it did really well throughout the Great Recession, it has gotten even better as we have taken lessons learned in the prior downturn and used those to get even more defensive and more conservative.

Matt Olney:

Okay, that's helpful. Thanks for that. And then just moving on to expenses, I was looking for some additional commentary just in general. At this point, how much of the expense built for the enterprise risk management system is now in the 2Q run rate, and when would you expect to see the cost saves fully loaded for the pending acquisitions, in which quarter?

George Gleason:

A large percentage of the cost of our enterprise risk management is in the Q2 run rate, and a majority of the part that's not in that is probably built in risk management infrastructure we will be incorporating from CSB and C1, and we didn't count that as cost saves in those transactions when we were considering them. So we are well along the way in having that really fully reflected in our numbers. There will be some incremental increase on a quarter-to-quarter basis this year and next year, but the vast majority of that is in there and it should no longer be a really noticeable number as far as the delta in our quarter-to-quarter results.

Matt Olney:

And the follow-up to that was about the pending acquisitions, the cost saves from those, how quickly can you get those cost saves?

George Gleason:

Yes. Obviously, we are converting CSB the last weekend in August, I think, is that right, Tyler? (**Tyler Vance:** Yes.) And C1, the second weekend in October, is that correct? (**Tyler Vance:** Yes.) Yes. So we will get cost saves immediately upon each acquisitions closing on the 20th and the 21st. We will get some additional cost saves in the interim between closing and conversions. We will get another additional wave of cost saves on conversion. And then those cost saves should be pretty much all implemented by the end of the year. So you ought to have about as clean a run rate as you are probably going to get in Q1 with those saves having been fully implemented.

Catherine Mealor - *Keefe, Bruyette & Woods*

George, the non-purchase loan yields were up about 6 bps in this quarter. Can you talk about was there any kind of outside catch-up in deferred loan fees given the higher level of pay downs you had this quarter? And then outside of that, can you talk about trends, maybe pricing trends in recent production given the move in rates and market volatility we have seen in the recent months?

George Gleason:

Good question. We did have a large number of loans pay off this quarter. Most of those loans were toward the end of their maturity cycle. And as a result, there are many of those loans with little or no remaining deferred – net deferred origination cost. We, of course, have as we always do a few loans that paid off earlier than expected. And there were some net deferred credits that dropped into income from those, but I wouldn't characterize that as being an unusually high or low number. I would say it was a relatively typical number. On your question, Catherine, regarding pricing, as we commented in our last call, we are clearly seeing an increase in pricing power in a number of our markets. This varies from market to market depending on how many lenders have changed their approach to a particular market. I would tell you that the loans that we are quoting and pricing and closing today, we are typically probably getting 25 to 75 basis points better yield on those loans than we got in the fourth quarter of last year. And again that varies from geography to geography, but we are seeing a bit of improved pricing

power across much of our footprint. Now, that's not particularly true in community banking, but certainly true in the larger RESG portfolio. As I have said a number of times, people won't really see that in our earnings until probably the back half of '17 and 2018, because the majority of the loans that we are closing this month, it may be 8 to 15 months before we actually start funding that if it's – if we are loaning typically on average slightly less than 50% of the cost of the project and all of the other capital components have to fund before we start funding. You won't see that improved rate that we are getting on more recently originated loans for a number of quarters until we really get a significant amount of that funding out there at the improved pricing.

Catherine Meador:

Great, thanks, that was helpful. And then one other question just to follow-up on capital. So, we have got this \$225 million sub debt raise you just had. But now we have got increased growth guidance and you talked about the momentum in the non-CRE businesses which should probably move the growth, I would think even to a higher pace going into next year and into 2018. And so how should we think about where - how you envision given all of that the timing of the next capital needs and what part of the capital stack do you think would be most likely next?

George Gleason:

Tim Hicks does an ongoing monitoring of that and has our capital needs and the growth on our balance sheet projected out over a number of years on a quarter-to-quarter basis looking at all ratios. On a pro forma basis, using June 30 numbers and assuming the pro forma addition of C&S and C1 into the mix, we project that we have about \$2.5 billion of capacity for organic growth or acquisitions. Now, of course, we will be generating additional retained earnings. So, that doesn't mean that \$2.5 billion from now we will need additional capital, because we should be generating very good retained earnings that will support even more growth. But we will continue to monitor that on a quarter-to-quarter basis and really more frequently and continue to evaluate future capital needs. The sub debt was a very accretive way for us to raise capital at the 5.50 coupon on that at par. It didn't take much more than an equal volume of loans, a little bit more, but not much more than an equal volume of loans to offset the cost of that and then we can leverage that another 8 plus times all accretive to common shareholders. We would expect that the next capital formation would probably likely be another small incremental sub debt possibly by reopening the current issue just to give more volume and liquidity to that issue or

possibly doing another small sub debt issue. Then at some point in the future, we will probably find it most advantageous to do a preferred stock offering and then ultimately a common stock offering. The total capital ratio, the Tier 1 capital ratio, the common equity Tier 1 ratio, are all the ratios that we are monitoring as being relevant. And if we synchronize our growth in a proper manner and achieve the proper mix, then we will reach a point where we need to raise capital in a very orderly manner that would approach one and then two and then all three of those ratios. We have that mapped out and we continually re-project it. We are certainly in a really good position now with about \$2.5 billion of excess growth capacity on a static pro forma basis today.

Joe Gladue – *Merion Capital Group*

I think most of my questions have been answered, but I did have sort of one housekeeping. The tax rate has been a little bit higher than I have been expecting so far this year. Just wondering particularly with the new acquisitions coming on where you are expecting the tax rate to be going forward?

Greg McKinney:

Hi, Joe, this is Greg. Let me just comment on that real quickly and then see if you got any follow-up. With our growth in recent quarters in some of the states with higher state tax rates, specifically California, New York that has had the result of driving up our marginal tax rate a little bit versus where it was if you went back into 2014 or to 2015. With the acquisitions of Community & Southern and C1, those rates should generally have the impact of blending down that marginal rate slightly. So, it wouldn't surprise me to see that rate begin to work its way down a little bit in Q3, then maybe even a little more in Q4. And by the time we get into Q4, it should be somewhat representative of what we would expect for the next few quarters assuming pretty broad-based growth at that point.

Michael Rose – *Raymond James & Associates*

Hey, George. Can you just quickly comment on any sort of interaction you have had with the regulators around the CRE concentration?

George Gleason:

Yes, thank you, Michael. I appreciate the question. Since we crossed \$10 billion literally the first day of January, we have started our new examination cycle with our regulators. And instead of our exams

being all clustered in about a 6 or 7-week, 8-week period in August, September and early October, our examination cycle now as a larger bank has become much more continuous with exams really occurring every month on different parts of our Company. We started that new exam cycle in April and the first subject matter exam that we had, as you would expect, was a targeted CRE exam. That was a joint exam with the State and the FDIC. And the FDIC had their normal complement of Arkansas Texas examiners and then had, because of our growing CRE presence nationally and the growing size of our balance sheet, some of their big more national-oriented CRE examiners come in. So, we have had very recent interaction with our examiners on the subject of CRE. They clearly I think understand our plans and expectations regarding continuing to grow the CRE portfolio. We clearly understand our responsibilities and obligations to – if you are going to have the level of CRE concentrations we have, to do an extraordinary job on that and to do the extra things that the regulators appropriately expect banks that have CRE concentrations to do and that includes extra monitoring, extra management, extra oversight. And these are things we have done for 10 years, because we have always had a CRE concentration. Obviously, the size of our balance sheet and the size of our CRE concentration in dollars gets bigger every year. The more national scope and the larger size projects that we are doing all dictates that we continue to develop and improve our processes for monitoring, measuring and managing that CRE concentration. I think we are doing all of that really well. We are working really hard to make sure we stay ahead of the curve and ahead of expectations. You don't ever want to fall behind and be trying to catch up to where your regulators think you are. So I think our proactive approach to this has been very well received. Our understanding of the guidelines is that they are just guidelines, they are not limits. But if you are at or above the guidelines, you got to do extra stuff and that's the way we have always approached it.

Michael Rose:

So, just to be clear, there was no directive as part of your capital raise to lower that number at all, and they're comfortable with your levels where they're at today?

George Gleason:

I'll let them speak to their comfort level, but I can tell you that the capital that we raised in December and the capital that we raised in June were totally based on our internal policies, which are self-imposed. We have not had our regulators imply to us that our capital policies and practices were

inadequate. They understand that we're operating – by choice and by internal policy – to the 1/1/2019 Basel III standards with a capital conservation buffer. And they understand our capital formation plans to continue to be in compliance with those January 1, 2019 standards. So, the capital raise that we have done, the raises that we have done, were not in any way a result of regulatory directive or suggestion. They were totally a result of our own management practices and directives from our ALCO committee.

Brian Martin – *FIG Partners, LLC*

George, just a couple of things, just are you able to quantify the payoffs in the quarter, to some extent this quarter relative to last quarter or just previous quarters, just kind of an idea of how large they were or maybe just the originations?

George Gleason

I don't have that number totally developed. And of course, that's a combination of payoffs and pay-downs. Because lot loans and land loans and condo loans have pay-downs because you are releasing product incrementally. And sometimes on the mixed-use projects, you have partial pay-downs because the apartment part of the project refi is out and the other parts are still remaining to be stabilized to refi. So it was a combination of all of those. I can tell you we had a higher level of payoffs and pay-downs in Q2 than we did in Q1 or Q4, but it's – and I would guess that number was probably in the \$300 million range, more or less higher, but that's a guess, I have not taken the time to actually go through and add all that up.

Brian Martin

Okay, understood, that's helpful, and just maybe a couple of other things. On the concentration levels that we have talked about, I guess looking at things, can you give us an idea where the real estate concentration levels are at quarter end with the new sub-debt in there, just some ballpark on that or just what the risk based capital ratio was in the quarter?

George Gleason

We don't have that calculated yet. And we will have that in our Q, but I don't have that number yet on a risk based capital ratio.

Brian Martin

Okay, alright, then maybe just the last two things. Maybe can you just give a little color on the thought on building liquidity in the securities portfolio in the quarter. And then just the last thing was, if you can just give any color on the recovery income the quarter had a nice rebound, but just more kind of big picture how to think about that annually, if there is any thoughts on that, that would be helpful. And that's all I have.

George Gleason

Okay, great. Thanks. Let me take the back end of that question first and the recovery income. Yes, we had an improved quarter of recovery income in Q2 as compared to Q1. Obviously, those numbers were way down from where they were a year ago, as we knew they would be. It's very difficult to handicap and give you any really meaningful guidance on that because those things do tend to bounce around quite a bit from quarter-to-quarter. So I would tell you I wouldn't be surprised in the next couple of quarters if we didn't have quarters that look like Q1 and I wouldn't be surprised if we didn't have quarters that look like Q2 in that regard. So there is really no way to predict that until you see what pays off in that purchase loan portfolio and what sort of recoveries we get on prior charge-offs and so forth, that were acquired charge-offs and so forth. So I am afraid I can't give you any better guidance. Now on liquidity, what I can tell you and you saw this in the portfolio this month, our bond portfolio grew to, Greg, what, about \$800 million and that was an increase of roughly how much versus the prior quarter, a couple of hundred or less? (**Greg McKinney:** \$150 to \$200 million, yes.)

So we have made a conscious decision that given the growth in our balance sheet that we should keep more liquidity on balance sheet. And so it's not been a terribly great market in which to buy bonds, obviously yields are at historic lows on a lot of securities, including the U.S. Treasury 10-year. But we are looking for bonds that we can buy that have a very good yield on them that are very high quality that we can get comfortable with. So I would say the guys are probably still buying one out of every 30 to 50 they look at, that's probably an improvement from one out of every 100 to 200 that they looked at in previous quarters, just because we have made a conscious decision that given the growth in our balance sheet and the growth in the unfunded balance of loans, that we should keep more on balance sheet liquidity. You can also see that reflected and the fact that Tyler mentioned in his remarks that we had over \$700 million in excess cash in our cash account. So you should expect to continue to see that trend

of growth in the bond portfolio. I would guess that if we are having a balance sheet that's growing roughly \$1 billion a quarter that \$100 million to \$200 million of that might be growth in that securities book just to increase our own balance sheet liquidity a bit. And kind of following up on your question, in tandem with Michael Rose's question, none of the regulators have told us we should keep more liquidity on the balance sheet. But we try to be very proactive in managing these things. And as we have looked at that we have said that if someone could have a criticism of us, it might be that we just don't keep a lot on balance sheet liquidity and we have taken proactive steps over the last couple of quarters to start addressing that so that it won't be an area of criticism in the future.

Brian Martin

Okay, that's all helpful. Thanks for the color and great quarter George.

George Gleason

Thank you very much for joining our call today. We appreciate your interest in Bank of the Ozarks. There being no further questions, that concludes our call. We look forward to talking with you in about 90 days. Thank you.