

Bank of the Ozarks, Inc.

Conference Call – January 17, 2017

Transcript – Prepared Remarks

Good morning, I am Tim Hicks, Executive Vice President and Chief of Staff 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.

During today's call, and in other disclosures and presentations, we may make certain statements about our plans, estimates, strategies and outlook that are forward-looking statements. These statements are based on management's current expectations concerning future events that, by their nature, are subject to risks and uncertainties. Actual results and future events could differ, possibly materially, from those anticipated in our statements and from historical performance due to a variety of risks and other factors. Information about such factors, as well as GAAP reconciliations and other information on non-GAAP financial measures we discuss, is included in today's earnings press release and in our 10-K, 10-Qs and various other SEC filings and investor materials. These are all available on our corporate website, www.bankozarks.com, under "Investor Relations." 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.

Finally, the Company is not responsible for, and does not edit nor guarantee the accuracy of our earnings teleconference transcripts provided by third parties. The only authorized live and archived webcasts and transcripts are located on our website.

Before I turn the call over to the rest of the team, I want to mention a few of the highlights of another record quarter and record year, and, more importantly, a quarter and year which position us well for the future.

Our \$18.9 billion in total assets at year-end was a 91% increase from our total assets at year-end 2015. This increased balance sheet scope and scale greatly enhance the future prospects and opportunities for our Company. During 2016 our non-purchased loans and leases grew 47% reflecting our exceptional

capabilities to organically grow a large volume of high-quality, good-yielding earning assets; our purchased loans grew 174% reflecting our capabilities to effectively augment our organic growth through triple-accretive acquisitions; and our deposits grew 95% as a result of a potent combination of organic deposit growth and acquired deposits. This balance sheet growth translated into excellent income growth. Our \$87.8 million in net income for the quarter just ended was our fourteenth consecutive quarter of record net income and a 71% increase from the fourth quarter of 2015. Our record \$0.72 diluted earnings per common share for the quarter just ended was a 26% increase compared to the fourth quarter of 2015. Our net interest income, service charge income and trust income for the quarter just ended were also quarterly records. Our 5.02% net interest margin for the quarter just ended was a 12 basis point improvement from the immediately preceding quarter and our best for any quarter of 2016. Even with the costs of integrating our two acquisitions and our C1 core systems conversion in October, our efficiency ratio for the quarter just ended was an excellent 34.3% and our best of 2016, highlighting our status as one of the most efficient banks in the industry.

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

George Gleason

Thank you, Tim.

Asset quality was among the numerous highlights of our 2016 results. Most of our asset quality ratios were at or near record levels throughout the year.

For example, our net charge-off ratio for total loans and leases for 2016 was a record 0.07%, after having varied only slightly from 5 to 9 basis points annualized in each quarter of 2016. This was our lowest annual net charge-off ratio in our 19 years as a public company. At December 31, 2016, excluding purchased loans, our nonperforming loans and leases as a percent of total loans and leases were just 0.15%, having ranged from 8 to 15 basis points at each quarter-end in 2016 and consistently reflecting improvement from an already low 0.20% at year-end 2015. Our nonperforming assets as a percent of total assets at December 31, 2016 were 0.31%, having ranged from 25 to 31 basis points at each quarter-end in 2016 and consistently reflecting improvement from 0.37% at year-end 2015. Our

loans and leases past due 30 days or more, including past due non-accrual loans and leases, to total loans and leases were a record low 0.16% at December 31, 2016, which was our fourth consecutive quarter of reporting a record low past due ratio as a public company.

These ratios reflect our longstanding commitment to conservative underwriting standards and 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 about 35% of the industry's net charge-off ratio, and we have beaten the industry's net charge-off ratio in every year. Our outperformance has been even better recently, as evidenced by the fact that our net charge-off ratio for the first nine months of 2016 was just 13% of the industry's net charge-off ratio.

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 accounted for 70% of the funded balance and 92% of the unfunded balance of our total non-purchased loans and leases at December 31, 2016. At year-end our average loan-to-cost for the RESG portfolio was a very conservative 48.2% and our average loan to appraised value was even lower at just 41.6%. The extremely low leverage of this portfolio exemplifies our very conservative credit culture and is one of the many reasons we have such confidence in the quality and durability of our loan and lease portfolio.

Even with our very conservative underwriting, our discipline, and our four-fold focus on great properties, strong and capable sponsors, very low leverage and defensive loan structures, we have achieved 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 \$845 million and for the full year of 2016 grew \$3.08 billion. Throughout 2016 we saw an accelerated trend in loan payoffs as all categories of construction and development products have sold or been refinanced into permanent financing more quickly than we would have experienced in previous years. This acceleration reflects the quality of the projects we are financing and their acceptance in the marketplace, which is certainly a positive.

Even with the accelerated payoffs, our non-purchased loans and leases outstanding grew 47% in 2016. Our loan origination volume continued to grow in the fourth quarter as reflected in our \$845 million growth in funded non-purchased loans and leases and our \$1.41 billion growth in our unfunded balance of closed loans. For the full year, our unfunded balance of closed loans increased by \$4.27 billion, growing to a record \$10.07 billion at December 31, 2016. This large unfunded balance of closed loans will be instrumental in achieving our loan growth goals in 2017 and 2018.

It appears likely that the strong prepayment trends from 2016 will continue in 2017. Notwithstanding that, given the growth in our customer base, our robust pipeline of transactions currently in underwriting and closing, and our largest ever unfunded balance of closed loans, we expect another year of record growth in non-purchased loans and leases in 2017, exceeding 2016's record growth of \$3.08 billion. However, we expect significant variation in loan growth from quarter to quarter in 2017, and, based on our projections of funding and prepayment of loans and leases already closed, we expect growth in the first half of 2017 to be less than growth in the second half of 2017. Consistent with the thought we expressed in our October conference call, we expect 2017's growth in non-purchased loans and leases to be between \$3.1 billion and \$4 billion.

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 14 years ago. Its priorities have always been: first on asset quality, second on profitability and third on growth. As a result of the emphasis on quality, RESG has had only two loans result in losses in 14 years. RESG's total credit losses since inception are \$10.4 million, which is just a seven basis point average annualized loss ratio over its entire history. In recent years, RESG has tended to be even more conservative. Given the exceptional track record of this division and the low leverage and the significant diversification of its 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 providing 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. In accordance with generally accepted accounting principles, we defer both loan origination

fees and loan origination costs. At December 31, 2016, we had \$43.7 million in net deferred credits, meaning we had \$43.7 million more in unamortized deferred loan origination fees than unamortized deferred loan origination costs. This net deferred credit increased \$15.9 million in 2016. This, along with the \$173.5 million valuation discount on our purchased loans at December 31, 2016, has favorable implications for future earnings.

In 2016 there was much discussion in industry publications about commercial real estate (“CRE”) and CRE concentrations. For decades our focus has been on real estate lending, and we are one of the largest and most active CRE lenders in the country. When bank regulators first issued their CRE concentration guidelines in 2006, our CRE ratios were well above the guidelines, just as our CRE ratios are today. We were comfortable then with our level of CRE lending, and, because of all of 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.

Many people tend to lump everyone involved in CRE transactions in the same category without distinguishing between equity, mezzanine lender and senior secured lender priorities. In almost every transaction we do, we are the sole senior secured lender, which means that in the event of default every penny of equity and every penny provided by a mezzanine lender would be lost before we lose even one cent of interest or principal. Simply stated, we have the lowest risk position in the capital stack. Likewise, our extremely low loan-to-cost and loan-to-value ratios are probably more conservative than just about every other CRE lender in the country. Accordingly, we believe our CRE portfolio is the lowest risk CRE portfolio in the industry.

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 acquisition, developing the consumer and small business lending capabilities and the indirect marine and RV consumer lending capabilities we acquired in our Community & Southern acquisition, and expanding our proven legacy leasing and investment securities portfolio platforms. While we expect our CRE lending volumes to continue to increase significantly, we expect these other areas to grow even faster. By late 2018 our goal is for CRE to account for approximately 57% of our growth in earning assets and for our non-CRE asset categories, including those we just mentioned, to account for approximately 43% of our growth in earning assets. Again, let me emphasize that we expect RESG's growth to accelerate in 2017 and beyond.

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

Greg McKinney:

Net interest income is our largest source of revenue, and the quarter just ended was our eleventh consecutive quarter of record net interest income. Substantial growth in our volume of average earning assets and improvement in our net interest margin both contributed to this record.

Our superb net interest margin, which is among the best in the industry, combined with our favorable prospects for continued growth in earning assets, suggests that we should continue our trend of record net interest income in coming quarters.

We were pleased with the twelve basis point improvement in our net interest margin to 5.02% in the quarter just ended as compared to the immediately preceding quarter. This was our second consecutive quarter of improved net interest margin. Our net interest margin in the quarter benefited from the continued increases in Libor rates during the quarter, the Federal Reserve's recent 25 basis-point increase in the Fed Funds target rate, and our continued high level of loan prepayments, which benefit our net interest margin in that the unamortized portion of any deferred net loan origination fees or purchased loan discount is recognized as interest income when a loan prepays. Additionally, as we have

discussed in our recent quarters, we have been getting better pricing on new loan originations. The benefits of this increased loan pricing should be even more evident as a greater volume of the loans originated in 2016 fund in 2017 and 2018. Going forward, any further increases in the Fed Funds target rate combined with the better loan pricing we have recently enjoyed should be beneficial to our net interest margin, but, on the other hand, the declining volume and yield over time of our portfolio of higher yielding purchased loans will provide some headwind to improvement in our net interest margin.

Our favorable interest rate risk profile has us well positioned for just about any interest rate scenario. At December 31, our variable rate loans were 82% of our total non-purchased loans and leases, and we had floors in 93% 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, our having floors in 93% 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. After reporting a 35.5% efficiency ratio for the first six months of 2016, our efficiency ratio increased to 38.1% in the third quarter, primarily because of costs associated with our two recent acquisitions. In the quarter just ended, even with the costs of integrating our two acquisitions and our C1 core systems conversion in October, our efficiency ratio improved to 34.3%, our best quarterly ratio of 2016. This reflects our culture of efficiency and supports our belief that we can continue to improve our efficiency ratio over the long term in pursuit of our goal of ultimately achieving a sub-30% efficiency ratio.

There are several key factors needed to accomplish our long-term efficiency goals. First, we expect to ultimately utilize a large amount of the excess capacity of our extensive branch network. At June 30, 2016, including the branches acquired in the two recent acquisitions, but excluding the New York market, our pro forma combined organization had deposit gathering branches in 156 cities with 4.13% of the branches in those cities, but only 1.39% of the deposits. Compared to our previous June 30, 2015 data, the 2016 data reflects that we have increased both our deposits and our relative market share in many of these cities over the past year. We expect we can continue this trend for years to come, tapping

billions of dollars of additional deposits through our existing branch network. This ability to achieve substantial deposit growth with limited additions of overhead has favorable implications for our efficiency ratio. Second, we expect to achieve further efficiencies over time from our recent acquisitions, including efficiencies from the increased benefits of having adopted Community & Southern's consumer and small business lending platform and the ongoing deployment of technology applications from the Innovation Labs Group, which we acquired with C1 and subsequently expanded. By fully leveraging these factors, among others, we hope to achieve an improving efficiency ratio over the next several years and ultimately a sub-30% efficiency ratio. Of course, as a larger and growing organization, we are constantly increasing our expenditures to expand and enhance our infrastructure for information technology, information systems, cybersecurity, business resilience, enterprise risk management, internal audit, compliance, BSA/AML monitoring, training and other important areas. We are also expanding our human and physical infrastructure to better serve low-to-moderate income and majority-minority markets and customer segments. The increasing costs for such enhanced infrastructure will be a headwind in our efforts to improve our efficiency ratio. However, we believe that our excellent organic growth will generate sufficient additional revenue for us to achieve both our important infrastructure enhancements and our long-term efficiency ratio goal.

Our guidance regarding an improving efficiency ratio in future years does not consider the potential impact of any future acquisitions.

With both core system conversions now complete, and both integration processes substantially behind us, you might expect to see a substantial reduction in non-interest expense in the first quarter of 2017 as a result of cost savings. There will be substantial cost savings realized, but, as we discussed in our October conference call, those cost savings will be replaced by other costs including staff additions needed for our growth and the enhancement of corporate infrastructure as described earlier, annual compensation increases for our very deserving staff, and our annual health insurance premium increases.

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

Tyler Vance:

Let me first discuss capital. Of course, we continue to be well capitalized by all applicable regulatory standards, and our internal policies for capital adequacy are well above the current regulatory requirements. Specifically, our internal policies require that we maintain well capitalized status in accordance with the fully phased-in 2019 Basel III standards, including the capital conservation buffer.

We currently have substantial capital in excess of our self-imposed capital standards to support continued growth, and our strong rate of capital formation through retained earnings should provide even more capital for future growth. Of course, we constantly monitor our capital position, projections for growth, capital market conditions and capital formation alternatives, all with the goal of effectively managing our capital position for the maximum benefit of shareholders while always maintaining well capitalized status.

In regard to liquidity, we have long expected that, within reasonable limits, we could accelerate deposit growth as needed to fund our loan and lease growth. Our experience in recent years has validated this expectation. In 2016, our deposits grew \$7.6 billion, or 95%, including deposit growth in our legacy offices of over \$3 billion. This provided sufficient liquidity to fund our excellent loan and lease growth and accumulate surplus cash of approximately \$634 million at December 31, 2016.

We consider net growth in core checking accounts as our most important deposit metric. In 2016 we achieved record annual organic growth in our number of net new core checking accounts with approximately 13,196 net accounts added, and that does not include approximately 117,000 core checking accounts added through our two recent acquisitions. Our excellent checking account growth has been an important contributor to our having achieved record service charge income in recent quarters and years.

Currently we have 39 offices in 27 cities in “spin-up” mode offering various deposit specials along with an enhanced level of marketing activity. Our branch network of approximately 243 deposit offices continues to have substantial untapped capacity, and we believe that capacity is sufficient to fund our

expected loan and lease growth over the next several years. Planned *de novo* branch additions and possible future acquisitions should provide additional deposit growth capacity for the future.

Over the course of 2016, our cost of interest-bearing deposits increased 17 basis points from 0.35% in the fourth quarter of 2015 to 0.52% in the fourth quarter of 2016. Given our expectation that our growth in non-purchased loans and leases in 2017 will range between \$3.1 and \$4 billion, we expect to continue to grow deposits significantly this year. Based on this, combined with our expectation for further increases by the Federal Reserve in the Fed Funds target rate during 2017, we expect continued upward pressure on our cost of interest bearing deposits in 2017. Our goal for 2017 is to hold the rate of increase in our cost of interest bearing deposits below, and hopefully well below, the rate of increase in our yield on interest earning assets.

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. The integration of our two recent acquisitions was a major focus in recent quarters. With the integration of these two acquisitions now substantially complete, we expect to be much more active in 2017 in looking for accretive M & A opportunities.

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

George Gleason:

We have a very optimistic outlook for 2017. With that said, let me make my annual cautionary comment that first quarter service charge income, mortgage lending income and loan growth are typically below average compared to other quarters. Also, let me remind you that, unless it is repealed or amended, the Durbin Amendment will impact our service charge revenue starting July 1 of this year. Based on our transaction volume in the quarter just ended, that impact would be a pre-tax reduction in revenue of about \$1.85 million per quarter.

I want to close today's call by elaborating on the accomplishments of our team. Early in 2016, there were some who questioned the wisdom of and our expectations regarding our two recent acquisitions, and there were some who articulated a "parade of imaginary horrors" which they theorized would adversely affect our Company. Our hard work, consistent execution, and constant achievement of record results in each quarter of 2016 should put any such questions to rest. Exceptional results are almost always accomplished by exceptional teams, and the exceptionality of our team was clearly evident in our fourth quarter results. Let me give you one example: how many teams at a \$12.3 billion bank with a 35% efficiency ratio could simultaneously accomplish the acquisitions of a \$4.2 billion bank with a 71% efficiency ratio and a \$1.7 billion bank with a 66% efficiency ratio and, in the first full quarter of combined operations, have an \$18.9 billion bank achieving a 34.3% efficiency ratio? That's exceptional execution, but we can do even better! Constantly striving for better performance and greater achievement are the ultimate hallmarks of any great team, and like all great teams we have a list of things on which we can improve, both immediately and with future acquisitions. I love my job, and the best part of my job is working with our 2,380 amazing team members every day. With a team like this, exceptional results are always possible. I extend my heartfelt thanks and congratulations to all our teammates on a job very well done in 2016.

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 queue in for questions.

Transcript of Q & A

Timur Braziler - *Wells Fargo Securities*

Hi. Good morning, gentlemen.

George Gleason

Good morning.

Timur Braziler

First, maybe on the loan growth expectations for the first half of 2017, maybe can you help us reconcile those expectations relative to a pretty strong print here in the fourth quarter. Did this most recent quarter have any spillover from 3Q or any pull forward from Q1? I guess just trying to reconcile the strong print this quarter versus tempered expectations for one half of 2017.

George Gleason

We certainly don't want to damp down expectations too much for next year. As Tyler said and as I said, we expect our non-purchased loans and leases for the full year of 2017 will grow somewhere between \$3.1 billion and \$4.0 billion. So that's a pretty good growth rate which would give us another record year of growth in 2017. So I think that it's the first point we need to emphasize. Last year was an exception, in that our first quarter growth last year was the largest growth of the year. The fourth quarter just ended was our second largest growth of the year. More typically, the first quarter is our smallest growth of the year and the growth tends to ramp up.

Based on our models and projections of fundings and prepayments, we have a lot of fundings heavily weighted toward the end of next year and less toward the beginning, and prepayments tend to be weighted a little heavier in the front of the year. So we do think we'll return to a much more normal pattern of seeing slow growth, on a relative basis, in Q1 and faster growth, particularly in the third and fourth quarters of next year.

To answer your other specific question, did we really see a pull forward or push of prepayments? Not really. In our call about 90 days ago, I said we might not make our \$3 billion original projection of growth for the year. We had a scenario, or some projections at that time, that assumed if a couple of

our expected Q4 fundings pushed into January and a couple prepayments that we would likely expect in January pull forward into December, that growth for the year could have been more like \$2.9 billion instead of the \$3.08 billion we came up with.

But despite a few moving parts both directions there, those things worked out really consistent with our expectations. So I would say no, there was no real movement from Q3 to Q4 or Q1 to Q4 that really distorted that. It was a pretty good, pretty clean number for Q4.

Timur Braziler

OK. That's helpful. And just keeping pace with the prepayment activity, what was that number in the fourth quarter and what were the subsequent fees associated with that?

George Gleason

I can't give you that number. I'm not even tracking those now. But we did have a very high level of prepayments in Q4 that was consistent with probably the level of prepayments we saw in Q3 and similarly consistent with what we would expect in the next couple of quarters.

So we've built this ongoing high level of prepayments into our models and projections for 2017 and 2018. Things are typically paying off three to six to nine months faster than we would have seen as prepayment speeds in prior years, and we've revised all of our models to pretty much reflect that.

To answer your question about margin, our yield on our legacy loans has gone up from Q3 and Q4 of 2015, when we were at 4.96%. In Q1 of 2016, our yield on our legacy loans was 5%, 5.00%. In Q2, it was 5.06%. In Q3, it was 5.12%. And in the quarter just ended, it went up a little further to 5.14%.

And Greg articulated, that's a combination of factors that have contributed to that, the two Fed rate increases, the changes in the baseline rates for LIBOR that occurred later last year, the better pricing that we're getting, and the accelerated prepayments that drop more unaccreted fees and discounts in the income on those loans sooner than if they were paying off more slowly.

So that's been a nice trend that we experienced over 2016. I'm not guaranteeing that number will go up every quarter, but we would expect that trend to continue in 2017 of improving yields on the legacy non-purchased loan portfolio.

And again, as Greg said, it's for those reasons, expectations that we'll have a continued high level of prepayments. The better pricing that we got in 2016 will become much more evident over the course of 2017 and be evident in 2018 as more of those loans fund, and we do expect some further Fed rate action this year that will be beneficial to us in that regard.

Timur Braziler

Excellent. I appreciate the color. Nice quarter.

George Gleason

Thank you.

Catherine Mealor – *Keefe, Bruyette & Woods*

Thanks. Good morning.

George Gleason

Good morning, Catherine.

Catherine Mealor

Staying on the loan topic, I want to switch over to the purchased loan book. Can you give us a sense as to what the current contractual yield is on that book? I'm just trying to figure out how much of that is from accretable yield? And then also in that book, what are your expectations for the pace of decline that we should see over the next year or so?

George Gleason

I can't give you -- we have data somewhere, but none of us -- we're all looking at each other in the room -- none of us have that data with us on what the coupon rates are on those loans. Obviously, they're not accounted for based on the coupon, but based on the purchase accounting valuation metrics of those loans, so I can't give you that. What I would tell you is that historically in our

acquisitions, the first quarter or two following acquisitions tend to result in a very rapid level of prepayments. That's because lenders that are not going to be a permanent part of your team tend to leave; they tend to try to pick off some customers. Customers who know that their pricing or credit structure is not going to fit the new bank long-term tend to move. So you tend to have an acceleration in prepayments in those portfolios in the first couple of quarters, and I think we got the full impact of that in the quarter just ended.

So we would expect the rate of prepayments of that purchased loan portfolio to slow over the course of 2017. And I would, frankly, be surprised if we saw any quarters, we might, but I would be surprised if we did, saw any quarters where we had as high a level of prepayments in dollars as we did in the quarter just ended. So we think that will slow. That will have a benefit and it will have a detriment. The detriment will be that the discounts on those loans will be recognized less quickly. The benefit is we'll have more earning assets on the books for a longer period of time, earning more gross income.

Catherine Meador

Got it, okay. And then on the non-purchased book, can you give any commentary around geography? Are there any new geographies where you're seeing increased growth, or is it still the break out that we've seen in your most recent investor decks? Is that still a pretty good representation of where a lot of your new unfunded commitments, in terms of new money being put in, is geographically diverse?

George Gleason

There is a lot of geographic diversity in the book. With that said, New York continues to be our number one market for both funded and unfunded loans, and we had good growth in Q4 in New York. That funded balance in New York is, I don't think we're at \$3 billion yet, but it's approaching \$3 billion, and the unfunded balance is between \$1.5 billion and \$2 billion. So our total funded and unfunded commitments for New York MSA, which, of course, includes a little bit other than New York City, but that New York MSA is approaching \$5 billion and is the largest.

Now we've seen a lot of originations in Seattle, Chicago, Denver, Los Angeles, San Francisco, Miami, Austin, Nashville, Tennessee, Charleston, South Carolina, as well, recently. What I think you will see in 2017 is a tremendous increase in California as a percent, because we do have two offices there.

Those offices are maturing. We really built that team up in 2015. It got a lot of traction in 2016, and I think you will see that become a bigger part of our business in the coming year.

If you looked at our last Q, including purchased loans, our state rankings were New York, Florida, Georgia, Florida and Georgia having jumped into the number two and three spots in total loan commitments, based on the two acquisitions, followed closely by Arkansas and Texas in four and five, and the Carolinas. We look at North Carolina and South Carolina as a group, since we manage them as a group, they were six, and California was seven.

I'm reasonably confident that you will see California bump from the second five into the top five over the course of 2017. And in future years, I would be very surprised if some time in a couple of years out, it wasn't New York, California, Georgia, and Florida in three and four, and Arkansas, Texas and probably Texas in five and Arkansas dropping to six longer term, just because of the size of those markets.

But the portfolio continues to have a lot of diversity and you will see, when you see the 10-Q and the breakdown of geographies, there are probably a few new MSAs added this time that have not been there in the previous quarter, just reflecting the fact that our customer base of really large national real estate developers do business all over the United States and beyond, and we tend to travel with them where they do quality transactions.

Catherine Meador

Okay. Great. It's helpful. Thanks.

George Gleason

Thank you.

Stephen Scouten - *Sandler O'Neill & Partners*

Hi. Good morning, guys, how are you doing?

George Gleason

Doing fine. Good morning, Stephen.

Stephen Scouten

Question for you on the small move in non-accruals. Obviously, not a big dollar number, but just curious if you could give any color on the composition of that, what sector of the lending book that came from?

George Gleason

Yes, that was almost all related to a single relationship in our community bank in Dallas, of all places, and it was a home builder. And this homebuilding company had risen very successfully out of the downturn, had grown very large. They were still doing compiled financial statements. We, and some of the other banks loaning money to them, had been urging them to get an audit.

They got a review and determined, based on the review when their accountants got in there, that they had a fundamental error in the way that they were accounting for cost of goods sold, and hence, their profitability and capital for several years. And it was a consistently applied error in their processes. No indication that we've had of any fraud or intentional misconduct, but it caused them to violate all their loan covenants.

So we're involved in a very orderly and cooperative liquidation of that relationship. It's about a \$5 million relationship at year-end. When the problem was identified, it was \$5.8 million, I think, and became \$4.8 million. I believe at year-end, they liquidated about \$1 million. We should have another couple million dollars, or even more of that, liquidate in the next 30 days. We don't expect any loss on the relationship, either principal or interest, well secured. But because of the fundamental foul up in their accounting and hence, their capital position and profitability, they've just gone into liquidation mode. But it is a cooperative thing and again, we expect no loss in it and that's pretty much 100% of the increase.

Stephen Scouten

Perfect. Perfect. That's helpful. And then as it pertains to your net interest margin, curious of a couple things. One, you had mentioned last quarter trying to build in more prepayment fees, unused fees and such into your new loans, wondering what the progress of that has been. Then as it pertains to the 93% of loans with floors, curious as to how many of those you might cross through with the next 25 basis point hike.

George Gleason

That's a good question. I will tell you we're having really good success getting minimum interest or unused fees or prepayment penalties or other fees that are helping us achieve our target return on equity numbers, even in an environment where these loans pay off much faster than historically we would have expected. So we're continuing to work on that. We've got more work to do there, but we're pretty pleased with that.

As Greg mentioned, 82% of our loan portfolio is variable rate, 93%, Greg, of those loans have floors in them at the end of the year, 19% of those loans were at their floor rate and 81% of those variable rate loans were not at their floor rate. So only, of all those variable rate loans, only \$1.5 billion are currently at their floor and hence, would not immediately adjust as a result of a further move in LIBOR or Fed Funds or prime rate, whatever the applicable index is.

The next 0.25 point move eliminates another \$844 million of that, leaving only \$614 million. So with the two Fed Fund increases we've seen and the move in LIBOR, almost all of the loans now, all but \$1.5 billion are in the money, and 66% of that, or 60% roughly of that remaining group, jumps into the money with another 0.25 move in rate. So we're almost as rate sensitive as our total percent of rate sensitive loans would -- variable rate loans would indicate.

Stephen Scouten

Yes, that's great. That's better than I had realized, so that's really helpful. And then maybe one last one for me. Have you guys done any work yet around, or any work that you can disclose to us maybe, around what your effective tax rate would be if we did see a reduction in corporate rates to, say, 20% or 25%? Then, kind of, I don't know if you have any thoughts around earn back on any hit to tangible book and the immediate term of that effect?

George Gleason

We've done some math on that. If the applicable corporate rate were to move from 35% to 30%, our impairment on our deferred tax assets would be about \$12.2 million. If that rate, instead of 30% was 25%, the impairment on our DTA and deferred taxes would be about \$24.5 million. At 20%, that would be about \$36.8 million, and my favorite, 15% corporate tax rate federally, would be \$49.1 million. The earn back on all of those is about two months -- or I'm sorry two quarters, we got a little

optimistic there -- two quarters of improved earnings at the lower marginal federal rates would earn back the DTA/DTL net impairment.

Stephen Scouten

Perfect. Great. That's really helpful. And congrats again on a really strong quarter.

George Gleason

Thank you.

Michael Rose – *Raymond James & Associates, Inc.*

Hi guys, how are you?

George Gleason

Doing fine, Michael.

Michael Rose

Just wanted to talk about the NIM, maybe from a top of the house perspective. George, in previous quarters and years, you talked about the expectations for the full year declines in the margin and I understand higher prepays, everything that's been discussed so far in the call. Looks like the full year margin was down 27 bps in 2016, down 33 in 2015. Would you expect that decline in terms of the margin year-on-year, to lessen as we move forward just generally speaking? I know you won't give guidance.

George Gleason

Well let me tell you this. Certainly, we've had two quarters in a row where the margin has improved and we're fairly positive in our thinking, based on the fact that we do expect some additional Fed increases. I'm not smart enough to quantify exactly what that means. When we were at this point in our call last year, I think the market was expecting four additional increases last year and we got one. I think the expectation this year is two to three. I don't know if that translates into one, two, three or four. I'm not smart enough to figure that out. My crystal ball is not that good. But I do think we will have some further increases in the Fed Funds target rate this year. I would think it's more likely two or three than one, but even one would be helpful. LIBOR continues to seem to be grinding up a bit in

anticipation of that, as it did over the last quarter of last year. As Greg mentioned we're getting better pricing, and prepayments are helping our yield, so we're fairly cautiously optimistic about our ability to keep our legacy loan yields going up. And it's really hard to predict, because it's so prepayment dependent, exactly what the yield on purchased loans is.

But Tyler's done a great job, particularly in the second half of last year, managing our cost of interest bearing deposits increase. You know, we engineered ourselves into a bit of borrowed position to stay under \$10 billion at year-end 2015, so Tyler and his banking team came out of the chute pretty strong, with deposit growth in Q1 and it amped up our cost of interest bearing deposits 9 basis points in Q1. I think they got that moderated to 7 basis points in Q2. Our cost of interest bearing deposits, if I recall, actually went down 1 basis point in Q3 and then were up 2 basis points in Q4. So we're expecting an upward trend in cost of interest bearing deposits next year, but certainly at a more moderate pace than we saw in the front half of last year. So when you blend all those things together, I would tell you our thoughts are fairly constructive and cautiously optimistic about the NIM next year.

Michael Rose

Okay. That's helpful, George. And then maybe just two more quick ones for me. Just looking at non-interest expense, good to see salary and employee benefits down. I assume that's the cost saves from the two deals rolling in for a full quarter's impact, but the occupancy was up. Just trying to figure out if part of that increase is where the merger charges were, or just trying to get a better sense of why occupancy costs were up quarter-on-quarter.

George Gleason

Yes, good question. And what I would tell you is the total non-interest expense in Q4 came in a little better than the guidance we gave in our October call. Because what we said in the call was that we would see a lot of cost savings in Q4 versus Q3 and we would see a lot of cost savings in Q1 versus Q4, but you wouldn't see those cost savings translate through into the bottom line, because we were going to spend those cost savings on the infrastructure build that we've been talking about to build our infrastructure, to be ready to be a \$50 billion bank in future years. And that infrastructure build was risk management people, and BSA/AML people and internal audit people, and IT and technology people, and building up our Innovation Labs Group, and a litany of other things that Greg mentioned in his prepared remarks. So our total non-interest expense in Q3 was \$78.8 million. We

were \$78.4 million, \$400,000 less in Q4, and that was really, I didn't know that number would actually be down any, because yes, we had millions of dollars of transaction costs and conversion costs, but we're re-spending that money and we'll do the same in Q1.

And Greg mentioned in Q1, you'll also have the impact of our annual health insurance increases, most of our annual raises, as well as staff additions, that will be offset by elimination of the transaction costs that we incurred in Q4 and a bunch more of those cost savings flowing through. So, we think that \$78 - \$79 million number for non-interest expense is a good starting point for Q1 of next year. Yes there are a ton of moving parts there. Yes, there are going to be a lot of cost saves. You won't see the transaction cost in Q1, but you won't know that you don't see that, because as we said in October, that money is going to be spent for other things.

I'll give you an example. We had tremendous savings in headcount with the acquisition. Our total number of FTE employees at 9/30 were 2,314.5. Our total number of FTE employees at 12/31 were 2,315, so we have one more FTE, half FTE on the staff at year-end than we did at the end of the third quarter. That's because, yes, we eliminated scores of positions with the consolidation of operations, but we also built up all of this infrastructure that we've talked about in the last call. So we're building what we need to be ready to be a much larger organization than we are today, and we'll continue that build going forward.

Michael Rose

That's very helpful color, George. Maybe one higher level question. Just on C1 Labs, where do you stand in the staff buildout in terms of rolling out their capabilities to the rest of the franchise, and maybe what are some other things that you're working on that you might help improve the efficiency ratio longer term? Thanks.

George Gleason

Yes, I think when we announced the C1 transaction, they had eight people plus their leader in C1 Labs if I'm recalling correctly, Tyler, nine people?

Tyler Vance

Yes.

George Gleason

And how many are you today?

Tyler Vance

We're 22 or 23, George.

George Gleason

22 or 23, and that's pretty much the full build I think.

Tyler Vance

Yes, 23 is the full build.

George Gleason

23 is the budgeted staffing level there throughout 2017. Now, toward the end of 2017 as we're approaching 2018, we'll review that and may increase our allocation of the people to that unit, but we basically have grown at about 150% from where it was from 9 to 23 people. That's where we think it needs to be to accomplish our objectives for that, and they've done some really nice projects for us and done some really good things for us. The real impact of that unit in the efficiency of our Company, both from a quality of service to our external customers, quality of service to our internal customers and gains in efficiency, the big gains there are still to be realized. We're really getting started with that initiative. We're in the early stages of that. So we're very optimistic about that helping us achieve Greg's goal of a sub-30 efficiency ratio over time.

Michael Rose

That's helpful. Thanks for taking my questions, guys.

Matt Olney – *Stephens, Inc.*

Thanks, good morning.

George Gleason

Good morning, Matt.

Matt Olney

Can you provide an update on the various earning asset growth engines in the fourth quarter and specifically, I'm looking for details around the consumer indirect marine/RV segments, thanks.

George Gleason

I can give you some details, and I think our originations in the indirect, marine and RV units were about \$100 million in round numbers. I'm off \$5 or \$10 million one way or the other there, but we have really been pleased with the job that those guys are doing and the traction they're getting and the quality and yield of what they're originating. So we think that unit is at \$100 million a quarter pace and will continue to be accelerating that pace as we go forward.

The poultry, the majority of our poultry lending guys have gotten out of an 18-month non-compete that they had when we acquired a pretty strong part of our team there. They got out of that in early November. Its freed them up to be much more active in business development. We think that unit really begins to accelerate their growth in 2017, as compared to 2016, and we certainly saw that in the second half of the quarter just ended.

The consumer small business lending program that we've blended together, our program and CSB's program, and are rolling that out, is continuing to gain traction. I don't have the exact numbers, and Tim you may have this, but I think of our \$845 million in growth in non-purchased loans in the quarter just ended, about \$300 million was non-RESG, is that right?

Tim Hicks

Around, yes, \$270 to \$300 million.

George Gleason

Yes, just under \$300 million, somewhere between \$250 million and \$300 million of that was non-RESG growth so we're certainly not to our 57/43 mix that we want to be at in Q4 of 2018, but we're making very steady progress in that. And probably the one area we originated quite a few SBA loans, but the CSB and C1 had SBA loans that they had either originated or acquired in their acquisitions. Our SBA team has spent most of the five months since we closed those acquisitions working on those loans and conforming their servicing practices and documentation practices to our higher standards of

servicing and documentation. So because of that, they've been focused more on quality improvements than they have, in those acquired portfolios, than they have on new originations. We're about through with that process now and feeling like we've got all that pretty much where it needs to be, so they will have more focus on growth going forward. So all things considered, we're very pleased with the progress we're making there.

Matt Olney

Okay, that's great color. Thanks for that. Secondly, also wanted to ask you about M & A. I'm curious how you view the current environment for M & A. And obviously, you just completed your two largest deals in Company history, so how would you characterize your M & A appetite today and what are the characteristics you're looking for in a bank, and has that changed at all in recent years? Thanks.

George Gleason

Well, that's a great question. And as Tyler said in his prepared remarks, our focus all of last year was to get our two deals closed, secondly get them converted, and third get the integration substantially complete. And we're still working off a few rough edges on the integration work, but we are almost where we need to be on that. We're 95% plus done with all of that and really pleased with the way that's going. Obviously, as I talked about in the prepared remarks, the efficiency achievements that we've clocked in the fourth quarter clearly reflect how effective we've been in completing the integration, so we are real pleased with all of that. And with that done, we're now fully engaged in looking at new opportunities.

So the question is, what opportunities do you look at? And as I've said publicly, several times, the two transactions that we completed last year were very strategic for us. The highly complementary, very low overlap branch networks in Florida and Georgia were extremely strategic from a branch footprint, geography point of view. The C1 Labs Group, which is now our Innovation Labs Group, a very strategic addition in our technology area. The indirect marine/RV, consumer and small business lending platforms at CSB, very important. And I could add to that, their affordable housing platform, much smaller and we haven't talked about it, but really a nice smaller engine there for us. And then a lot of their team, people who are in risk management or in other disciplines, we needed that

MIS team on the GL and on the loan book, and that loan operations center staff in Carrollton, Georgia, all very strategic important additions for our Company.

So as we look forward now, we don't have a lot of strategic pieces that we need. In fact, I really can't, I don't have a shopping list. There's not anything on my list that says we need to do a strategic acquisition because we need this, that or the other. We've got what we need to build and beef up to be a \$50 billion bank. So the focus on acquisitions going forward is going to be much more on the financial metrics, and all the transactions we've done to date, all 15 of them, appear to be triple accretive on a book value, tangible book value and EPS basis. So we're going to expect that going forward, we will focus even more on those three accretive metrics in the transactions we're doing going forward, and have much less of a need to pay a higher price because something has important strategic value to us.

Matt Olney

Great, thank you.

George Gleason

Thank you, Matt.

George Gleason

Good morning, Joe.

Joe Gladue – *Merion Capital Group*

Good morning. Actually, my questions have been answered, thank you.

George Gleason

Thank you.

Peyton Green – *Piper Jaffrey*

Yes, good morning George. My question is, as it relates to pricing on the Real Estate Specialties Group portfolio and then maybe pricing in your more typical community bank, commercial real estate and construction portfolio. A year or so ago you started to see competitors withdraw from the market and

pricing improved. I was wondering when you might think those balances would start to fund. Is that a reason for optimism in the second half of 2017 or do you think it comes sooner? And then, how were spreads in the fourth quarter relative to the third on new originations?

George Gleason

Yes, Peyton, good question. And what I would tell you is we continue to work hard to maximize our pricing on all of our CRE transactions and other commercial transactions. And, I would tell you that we really didn't see much movement in pricing from Q3 to Q4 and in regard to new originations, so we had a lot of improvement in pricing late in 2015 and then first quarter. And really starting first quarter we really began to get some additional pricing power last year, saw more of that in Q2, more of that in Q3. Q4 seemed to be consistent with Q3, and I think what we're seeing today is consistent with that, so we've managed to move the pricing to a higher level over the last year. We're managing to hold that. It's not gained any from there really, but it's not eroded either.

The two caveats to that, that I would tell you is number one, in response to your question, we saw a little bit of that benefit in 2016, we'll see more in the first half of 2017. We'll see more in the second half of 2017, and we'll see most of that impact in our 2018 numbers, because those loans will fund up. And the second caveat goes back to a question earlier that was asked about how are we doing on getting unused commitment fees and minimum interest and prepayment penalties and other fees to offset the higher cost of prepayments. That continues to be an ongoing effort where we are getting more traction, probably even in January than we got in November or December. So we are really emphasizing that, trying to move that not just from Real Estate Specialties Group where we really started that effort because that's where we saw the faster prepayment, but also really beginning to emphasize that in the community banking side and hope we'll get some traction there on those protective features in the months to come.

Peyton Green

Okay great, thank you very much.

George Gleason

Thank you.

Brian Martin – *FIG Partners, LLC*

Good morning, George.

George Gleason

Hi, good morning, Brian.

Brian Martin

Most of my stuff has been answered, just two things. The pipeline on M & A, can you talk about that, now that you're kind of more engaged on that, is it pretty full? And secondly, the recent 25 basis point increase in rates, can you talk a little bit about how much you expect that to benefit the first quarter's type of margin, rather than full-year type of number? I don't know if you can give any color on that, would be helpful. But those are the only two things I had.

George Gleason

Well I'm not going to try to quantify that impact of that 25 basis points. Most of our loans, and this data is in the Q and you can look at it, what part of our loans are one-month LIBOR, three-month, six-month LIBOR, prime rate and so forth. But of course, the prime rate is kind of a cliff deal. The Fed moves the Fed Fund target rate, and that day or the next day, all the banks move prime rate, so it jumps instantly. That is a smaller part of our variable rate loans than the LIBOR-based loans. And clearly, if you look at a daily chart on LIBOR, you can see that in anticipation of the rate move, it was steadily moving up because everybody kind of reached a consensus that it was 100% probability the Fed was going to move. So that increase got built in over a month or more leading up to it. And then in the days following it, I think LIBOR was going up about 1 basis point a day, even though you were right after a 25 basis point Fed Fund increase. So that gets smoothed in a little more, which is the benefit of having your loans based on LIBOR in a rising rate environment, the increase gets anticipated. So we will see a little bit more of the benefit of that in Q1. What we're really looking for next is when the market decides 100% probability of the next one is going to happen and they start pricing that in advance, that should be very helpful for us.

On your question about the M & A pipeline, of course, I had Dennis James, our Director of Mergers and Acquisitions, severely constrained last year, because, as Tyler said, our focus was on closing, converting, integrating our new deals. We would have looked at a compelling deal that had a short

fuse last year, but the guys knew our preference was to really get these deals salted away before we got another one in the hopper. So, now that Dennis is out looking again and hasn't been as actively engaged in really being able to talk about things, he has a massive list of things to consider, because I've pretty much had him shut out of the game for a year. So there's a massive list of things to consider, and he's trying to work through those and he is working through them, with the help of our M & A committee, to try to prioritize what would be very financially attractive transactions for us to consider.

And the normal caveat I would give you on that is it takes two parties to make a deal and it takes a long time to make a deal. Sometimes things come together quickly and sometimes they take years, so it's hard to handicap when that enhanced focused and new found liberty that Dennis has to bring opportunities to us will come to fruition with one or more transactions for us. But we're fully engaged and there does seem to be a lot of folks out there who would like to be part of our Company.

Brian Martin

Okay, and just a follow-up. Is there a minimum size, now that the focus is maybe more financial in nature versus strategic, like you alluded to?

George Gleason

No, not absolutely. Clearly, our balance sheet is bigger now and we have so many opportunities to work on. There are probably transactions that would just be an injudicious allocation of resources for us to work on because it's too small. But at the same time, if it were a small transaction and it either had some really unique valuable attributes to it or it perhaps was a near 100% overlap with an existing branch network, where we could have almost total cost saves in it, you might look at smaller transactions that had those sort of unique benefits that would make it worth the time to look at them. But we're not going to do small deals that don't add a lot of value, in some way, to our Company, just because we want to do things that have a noticeable benefit to our shareholders, and that requires that the transaction have some scale to do that.

Brian Martin

Okay, perfect. Thanks for the color, George, and nice quarter.

George Gleason

Thank you very much.

George Gleason

Good morning, Blair.

Blair Brantley – Breane Capital, LLC

Hi, George how are you?

George Gleason

Doing well, thank you.

Blair Brantley

Most of my questions have been asked and answered. One thing, on the investment portfolio, can you give us any update there in terms of your thought process around that?

George Gleason

Well, we said at the beginning of last year that given the growth in our balance sheet and our unfunded commitments, we felt it prudent to hold more liquidity on balance sheet. So I think at the end of the year, or on average in the fourth quarter, our securities portfolio accounted for something less than 8%, 7% and change, of our total earning assets. That's still a pretty small number. If you compare that back to 2008, 2009 and 2010, I think we were, at various times there, pushing at or even over 30% of our earning assets in our securities portfolio. We have intentionally, for several years, kept the securities portfolio as a low percentage of earning assets, because we know when rates rise, you're going to have an adverse mark-to-market on the value of that portfolio, and we saw that in the quarter just ended. And that's just part of having an investment securities portfolio in a bank, so it's not surprising. But anticipating that, we have worked to keep that portfolio as low as we could keep it, and at the same time, feel like we had adequate liquidity on balance sheet to one, meet our needs, and two, meet any expectations of regulators regarding that. So we'll continue to be very judicious in keeping that as a low percentage of earning assets until we think that it is a fabulous buying opportunity, and I still think we could be some years away from a fabulous buying opportunity to buy

securities. We will hopefully recognize it when it is, as we did in 2008, 2009 and 2010 and be able to really capitalize on that at that time.

Blair Brantley

Okay great. Thank you.

George Gleason

Thank you guys for joining our call today. There being no further questions, this concludes our call.

We look forward to talking with you in about 90 days. Have a great day.