

BANK OF THE OZARKS INC
Form 10-Q
November 05, 2008
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark one)

☒ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended September 30, 2008

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from _____ to _____.

Commission File Number 0-22759

BANK OF THE OZARKS, INC.

(Exact name of registrant as specified in its charter)

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ARKANSAS
(State or other jurisdiction of
incorporation or organization)

71-0556208
(I.R.S. Employer
Identification Number)

12615 CHENAL PARKWAY, LITTLE ROCK, ARKANSAS
(Address of principal executive offices)

72211
(Zip Code)

Registrant's telephone number, including area code: (501) 978-2265

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Check one:

Large accelerated filer ☐ Accelerated filer ☒
Non-accelerated filer ☐ (Do not check if a smaller reporting company) Smaller reporting company ☐
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practical date.

Class
Common Stock, \$0.01 par value per share

Outstanding at September 30, 2008
16,854,540

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BANK OF THE OZARKS, INC.

FORM 10-Q

September 30, 2008

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Table of Contents**PART I. FINANCIAL INFORMATION**Item 1. **Financial Statements****BANK OF THE OZARKS, INC.****CONSOLIDATED BALANCE SHEETS**

| | Unaudited | | December 31, |
|--|--|--------------|--------------|
| | September 30, | 2007 | 2007 |
| | 2008 | | |
| | (Dollars in thousands, except per share amounts) | | |
| ASSETS | | | |
| Cash and due from banks | \$ 46,254 | \$ 35,215 | \$ 47,192 |
| Interest earning deposits | 329 | 319 | 329 |
| Cash and cash equivalents | 46,583 | 35,534 | 47,521 |
| Investment securities - available for sale (AFS) | 721,285 | 591,480 | 578,348 |
| Loans and leases | 2,055,400 | 1,815,934 | 1,871,135 |
| Allowance for loan and lease losses | (25,427) | (19,067) | (19,557) |
| Net loans and leases | 2,029,973 | 1,796,867 | 1,851,578 |
| Premises and equipment, net | 147,030 | 127,579 | 130,048 |
| Foreclosed assets held for sale, net | 5,887 | 2,496 | 3,112 |
| Accrued interest receivable | 15,927 | 18,242 | 17,420 |
| Bank owned life insurance | 47,648 | 45,659 | 46,148 |
| Intangible assets, net | 5,692 | 5,943 | 5,877 |
| Other, net | 50,521 | 27,505 | 30,823 |
| Total assets | \$ 3,070,546 | \$ 2,651,305 | \$ 2,710,875 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | | |
| Deposits: | | | |
| Demand non-interest bearing | \$ 194,104 | \$ 166,970 | \$ 162,995 |
| Savings and interest bearing transaction | 690,948 | 532,085 | 516,312 |
| Time | 1,416,474 | 1,325,389 | 1,377,754 |
| Total deposits | 2,301,526 | 2,024,444 | 2,057,061 |
| Repurchase agreements with customers | 46,329 | 42,656 | 46,086 |
| Other borrowings | 426,524 | 310,379 | 336,533 |
| Subordinated debentures | 64,950 | 64,950 | 64,950 |
| Accrued interest payable and other liabilities | 12,007 | 16,689 | 11,984 |
| Total liabilities | 2,851,336 | 2,459,118 | 2,516,614 |
| Minority interest | 3,400 | 3,433 | 3,432 |
| Commitments and contingencies | | | |
| Stockholders' equity: | | | |
| Preferred stock; \$0.01 par value; 1,000,000 shares authorized; no shares issued and outstanding | 168 | 168 | 168 |

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Common stock; \$0.01 par value; 50,000,000 shares authorized; 16,854,540, 16,811,040 and 16,818,240 shares issued and outstanding at September 30, 2008, September 30, 2007 and December 31, 2007, respectively

| | | | |
|---|----------|----------|----------|
| Additional paid-in capital | 39,731 | 38,474 | 38,613 |
| Retained earnings | 186,295 | 161,420 | 167,139 |
| Accumulated other comprehensive income (loss) | (10,384) | (11,308) | (15,091) |

| | | | |
|----------------------------|---------|---------|---------|
| Total stockholders' equity | 215,810 | 188,754 | 190,829 |
|----------------------------|---------|---------|---------|

| | | | |
|--|--------------|--------------|--------------|
| Total liabilities and stockholders' equity | \$ 3,070,546 | \$ 2,651,305 | \$ 2,710,875 |
|--|--------------|--------------|--------------|

See accompanying notes to consolidated financial statements.

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BANK OF THE OZARKS, INC.
CONSOLIDATED STATEMENTS OF INCOME

Unaudited

| | Three Months Ended September 30, 2008 | | September 30, 2007 | |
|---|--|-----------|-----------------------|------------|
| | (Dollars in thousands, except per share amounts) | | | |
| Interest income: | | | | |
| Loans and leases | \$ 35,857 | \$ 37,205 | \$ 106,962 | \$ 108,233 |
| Investment securities: | | | | |
| Taxable | 5,332 | 6,064 | 16,467 | 18,904 |
| Tax-exempt | 3,838 | 1,644 | 12,083 | 4,721 |
| Deposits with banks and federal funds sold | 3 | 4 | 10 | 15 |
| Total interest income | 45,030 | 44,917 | 135,522 | 131,873 |
| Interest expense: | | | | |
| Deposits | 15,382 | 21,061 | 50,314 | 64,110 |
| Repurchase agreements with customers | 174 | 387 | 604 | 1,285 |
| Other borrowings | 4,015 | 2,516 | 11,816 | 5,475 |
| Subordinated debentures | 843 | 1,282 | 2,818 | 3,791 |
| Total interest expense | 20,414 | 25,246 | 65,552 | 74,661 |
| Net interest income | 24,616 | 19,671 | 69,970 | 57,212 |
| Provision for loan and lease losses | (3,400) | (1,100) | (10,725) | (3,450) |
| Net interest income after provision for loan and lease losses | 21,216 | 18,571 | 59,245 | 53,762 |
| Non-interest income: | | | | |
| Service charges on deposit accounts | 3,102 | 3,075 | 8,939 | 9,017 |
| Mortgage lending income | 473 | 594 | 1,781 | 2,142 |
| Trust income | 649 | 565 | 1,882 | 1,561 |
| Bank owned life insurance income | 512 | 487 | 1,500 | 1,430 |
| Gains (losses) on sales of investment securities | (317) | 77 | (297) | 414 |
| Gains (losses) on sales of other assets | (78) | 38 | 35 | 26 |
| Other | 530 | 583 | 1,713 | 2,411 |
| Total non-interest income | 4,871 | 5,419 | 15,553 | 17,001 |
| Non-interest expense: | | | | |
| Salaries and employee benefits | 7,728 | 6,936 | 22,684 | 21,263 |
| Net occupancy and equipment | 2,318 | 2,059 | 6,575 | 5,997 |
| Other operating expenses | 3,775 | 2,737 | 10,885 | 8,486 |
| Total non-interest expense | 13,821 | 11,732 | 40,144 | 35,746 |
| Income before taxes | 12,266 | 12,258 | 34,654 | 35,017 |
| Provision for income taxes | 3,255 | 3,856 | 9,271 | 11,008 |

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| | | | | |
|------------------------------|----------|----------|-----------|-----------|
| Net income | \$ 9,011 | \$ 8,402 | \$ 25,383 | \$ 24,009 |
| Basic earnings per share | \$ 0.53 | \$ 0.50 | \$ 1.51 | \$ 1.43 |
| Diluted earnings per share | \$ 0.53 | \$ 0.50 | \$ 1.50 | \$ 1.43 |
| Dividends declared per share | \$ 0.13 | \$ 0.11 | \$ 0.37 | \$ 0.31 |

See accompanying notes to the consolidated financial statements.

Table of Contents**BANK OF THE OZARKS, INC.****CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**

Unaudited

| | Common Stock | Additional Paid-In Capital | Retained Earnings (Dollars in thousands) | Accumulated Other Comprehensive Income (Loss) | Total |
|--|-----------------|----------------------------------|--|--|------------|
| Balances January 1, 2007 | \$ 167 | \$ 36,779 | \$ 142,609 | \$ (4,922) | \$ 174,633 |
| Comprehensive income: | | | | | |
| Net income | | | 24,009 | | 24,009 |
| Other comprehensive income (loss): | | | | | |
| Unrealized gains and losses on AFS investment securities, net of \$3,960 tax effect | | | | (6,134) | (6,134) |
| Reclassification adjustment for gains and losses included in net income, net of \$162 tax effect | | | | (252) | (252) |
| Total comprehensive income | | | | | 17,623 |
| Cash dividends paid | | | (5,198) | | (5,198) |
| Issuance of 64,500 shares of common stock for exercise of stock options | 1 | 369 | | | 370 |
| Tax benefit on exercise of stock options | | 605 | | | 605 |
| Compensation expense under stock-based compensation plans | | 721 | | | 721 |
| Balances September 30, 2007 | \$ 168 | \$ 38,474 | \$ 161,420 | \$ (11,308) | \$ 188,754 |
| Balances January 1, 2008 | \$ 168 | \$ 38,613 | \$ 167,139 | \$ (15,091) | \$ 190,829 |
| Comprehensive income: | | | | | |
| Net income | | | 25,383 | | 25,383 |
| Other comprehensive income: | | | | | |
| Unrealized gains and losses on AFS investment securities, net of \$2,921 tax effect | | | | 4,526 | 4,526 |
| Reclassification adjustment for gains and losses included in net income, net of \$116 tax effect | | | | 181 | 181 |
| Total comprehensive income | | | | | 30,090 |
| Cash dividends paid | | | (6,227) | | (6,227) |
| Issuance of 36,300 shares of common stock for exercise of stock options | | 231 | | | 231 |
| Tax benefit on exercise of stock options | | 236 | | | 236 |
| Compensation expense under stock-based compensation plans | | 651 | | | 651 |
| Balances September 30, 2008 | \$ 168 | \$ 39,731 | \$ 186,295 | \$ (10,384) | \$ 215,810 |

See accompanying notes to consolidated financial statements.

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BANK OF THE OZARKS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS

Unaudited

| | Nine Months Ended September 30, | |
|---|------------------------------------|-----------|
| | 2008 | 2007 |
| | (Dollars in thousands) | |
| Cash flows from operating activities: | | |
| Net income | \$ 25,383 | \$ 24,009 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation | 2,637 | 2,431 |
| Amortization | 186 | 197 |
| Provision for loan and lease losses | 10,725 | 3,450 |
| Provision for losses on foreclosed assets | 553 | 36 |
| Net accretion of investment securities | (676) | (714) |
| Losses (gains) on sales of investment securities | 297 | (414) |
| Originations of mortgage loans for sale | (103,535) | (137,285) |
| Proceeds from sales of mortgage loans for sale | 105,563 | 138,375 |
| Gains on dispositions of premises and equipment and other assets | (35) | (26) |
| Deferred income tax benefit | (905) | (224) |
| Increase in cash surrender value of bank owned life insurance | (1,500) | (1,430) |
| Tax benefit on exercise of stock options | (236) | (605) |
| Compensation expense under stock-based compensation plans | 651 | 721 |
| Changes in assets and liabilities: | | |
| Accrued interest receivable | 1,493 | (858) |
| Other assets, net | (3,251) | 375 |
| Accrued interest payable and other liabilities | (446) | 2,509 |
| Net cash provided by operating activities | 36,904 | 30,547 |
| Cash flows from investing activities: | | |
| Proceeds from sales of investment securities AFS | 10,198 | 40,921 |
| Proceeds from maturities or calls of investment securities AFS | 1,449,127 | 20,769 |
| Purchases of investment securities AFS | (1,612,219) | (36,808) |
| Net increase in loans and leases | (198,313) | (147,008) |
| Purchases of premises and equipment | (21,513) | (13,738) |
| Proceeds from dispositions of premises and equipment and other assets | 5,969 | 3,775 |
| Cash (paid for) received from interests in unconsolidated investments | (30) | 1,839 |
| Net cash used by investing activities | (366,781) | (130,250) |
| Cash flows from financing activities: | | |
| Net increase (decrease) in deposits | 244,465 | (20,648) |
| Net proceeds from other borrowings | 89,991 | 115,719 |
| Net increase in repurchase agreements with customers | 243 | 1,655 |
| Proceeds from exercise of stock options | 231 | 370 |
| Tax benefit on exercise of stock options | 236 | 605 |
| Cash dividends paid | (6,227) | (5,198) |
| Net cash provided by financing activities | 328,939 | 92,503 |

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| | | |
|---|-----------|-----------|
| Net decrease in cash and cash equivalents | (938) | (7,200) |
| Cash and cash equivalents beginning of period | 47,521 | 42,734 |
| Cash and cash equivalents end of period | \$ 46,583 | \$ 35,534 |

See accompanying notes to consolidated financial statements.

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BANK OF THE OZARKS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Unaudited

1. Organization and Principles of Consolidation

Bank of the Ozarks, Inc. (the Company) is a bank holding company headquartered in Little Rock, Arkansas, which operates under the rules and regulations of the Board of Governors of the Federal Reserve System. The Company owns a wholly-owned state chartered bank subsidiary Bank of the Ozarks (the Bank), four 100%-owned finance subsidiary business trusts Ozark Capital Statutory Trust II (Ozark II), Ozark Capital Statutory Trust III (Ozark III), Ozark Capital Statutory Trust IV (Ozark IV) and Ozark Capital Statutory Trust V (Ozark V) (collectively, the Trusts) and, indirectly through the Bank, a subsidiary engaged in the development of real estate. The consolidated financial statements include the accounts of the Company, the Bank and the real estate subsidiary. Significant intercompany transactions and amounts have been eliminated in consolidation.

2. Basis of Presentation

The accompanying consolidated financial statements have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) in Article 10 of Regulation S-X and in accordance with the instructions to Form 10-Q and accounting principles generally accepted in the United States (GAAP) for interim financial information. Certain information, accounting policies and footnote disclosures normally included in complete financial statements prepared in accordance with GAAP have been condensed or omitted in accordance with such rules and regulations. These consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company's annual report on Form 10-K for the year ended December 31, 2007.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. In the opinion of management all adjustments considered necessary, consisting of normal recurring items, have been included for a fair presentation of the accompanying consolidated financial statements. Operating results for the three and nine months ended September 30, 2008 are not necessarily indicative of the results that may be expected for the full year or future periods.

Certain reclassifications of prior period amounts have been made to conform with the current period presentation. These reclassifications had no impact on previously reported net income.

3. Earnings Per Share (EPS)

Basic EPS is computed by dividing reported earnings available to common shareholders by the weighted-average number of shares outstanding. Diluted EPS is computed by dividing reported earnings available to common shareholders by the weighted-average number of shares outstanding after consideration of the dilutive effect of the Company's outstanding stock options. Options to purchase 468,400 shares of the Company's common stock were not included in the diluted EPS calculation for both the three-month and nine-month periods ended September 30, 2008, and options to purchase 237,350 shares of the Company's common stock were not included in the diluted EPS calculation for both the three-month and nine-month periods ended September 30, 2007 because inclusion would have been antidilutive.

Basic and diluted EPS are computed as follows:

| Three Months Ended | | Nine Months Ended | |
|--|------|-------------------|------|
| September 30, | | September 30, | |
| 2008 | 2007 | 2008 | 2007 |
| (In thousands, except per share amounts) | | | |

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| | | | | | |
|--------------------------|--------------------------|----------|----------|-----------|-----------|
| Common shares | weighted-average (basic) | 16,848 | 16,799 | 16,841 | 16,775 |
| Common share equivalents | weighted-average | 24 | 50 | 25 | 55 |
| Common shares | diluted | 16,872 | 16,849 | 16,866 | 16,830 |
| Net income | | \$ 9,011 | \$ 8,402 | \$ 25,383 | \$ 24,009 |
| Basic EPS | | \$ 0.53 | \$ 0.50 | \$ 1.51 | \$ 1.43 |
| Diluted EPS | | 0.53 | 0.50 | 1.50 | 1.43 |

Table of Contents**4. Federal Home Loan Bank of Dallas (FHLB) Advances**

FHLB advances with original maturities exceeding one year totaled \$341 million at September 30, 2008. Interest rates on these advances ranged from 2.53% to 6.43% at September 30, 2008 with a weighted-average interest rate of 4.27%. At September 30, 2008 aggregate annual maturities and weighted-average interest rates of FHLB advances with an original maturity of over one year were as follows.

| Maturity | Amount (Dollars in thousands) | Weighted-Average Interest Rate |
|------------|----------------------------------|-----------------------------------|
| 2008 | \$ 8 | 4.81% |
| 2009 | 33 | 4.81 |
| 2010 | 60,034 | 6.27 |
| 2011 | 31 | 4.80 |
| 2012 | 21 | 4.64 |
| Thereafter | 280,724 | 3.84 |
| | \$ 340,851 | 4.27 |

Included in the above table are \$340 million of FHLB advances that contain quarterly call features and are callable as follows.

| | Amount | Weighted-Average Interest Rate (Dollars in thousands) | Maturity |
|--------------------|-------------------|---|----------|
| Callable quarterly | \$ 60,000 | 6.27% | 2010 |
| Callable quarterly | 260,000 | 3.90 | 2017 |
| Callable quarterly | 20,000 | 2.53 | 2018 |
| | \$ 340,000 | 4.24 | |

At September 30, 2008 the Company had FHLB advances which are not included in the above tables with original maturities of one year or less of \$80 million with a weighted-average interest rate of 2.64%.

5. Subordinated Debentures

At September 30, 2008 the Company had the following issues of trust preferred securities outstanding and subordinated debentures owed to the Trusts.

| Description | Subordinated Debentures Owed to Trusts | Trust Preferred Securities of the Trusts | Interest Rate at September 30, 2008 (Dollars in thousands) | Final Maturity Date |
|-------------|---|---|--|------------------------|
| Ozark III | \$ 14,434 | \$ 14,000 | 5.74% | September 25, 2033 |
| Ozark II | 14,433 | 14,000 | 6.66 | September 29, 2033 |
| Ozark IV | 15,464 | 15,000 | 5.03 | September 28, 2034 |
| Ozark V | 20,619 | 20,000 | 4.42 | December 15, 2036 |
| | \$ 64,950 | \$ 63,000 | | |

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On September 25, 2003 Ozark III sold to investors in a private placement offering \$14 million of adjustable rate trust preferred securities, and on September 29, 2003, Ozark II sold to investors in a private placement offering \$14 million of adjustable rate trust preferred securities (collectively, 2003 Securities). The 2003 Securities bear interest, adjustable quarterly, at 90-day London Interbank Offered Rate (LIBOR) plus 2.95% for Ozark III and 90-day LIBOR plus 2.90% for Ozark II. The aggregate proceeds of \$28 million from the 2003 Securities were used to purchase an equal principal amount of adjustable rate subordinated debentures of the Company that bear interest, adjustable quarterly, at 90-day LIBOR plus 2.95% for Ozark III and 90-day LIBOR plus 2.90% for Ozark II (2003 Debentures).

On September 28, 2004 Ozark IV sold to investors in a private placement offering \$15 million of adjustable rate trust preferred securities (2004 Securities). The 2004 Securities bear interest, adjustable quarterly, at 90-day LIBOR plus 2.22%. The \$15 million proceeds from the 2004 Securities were used to purchase an equal principal amount of adjustable rate subordinated debentures of the Company that bear interest, adjustable quarterly, at 90-day LIBOR plus 2.22% (2004 Debentures).

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On September 29, 2006 Ozark V sold to investors in a private placement offering \$20 million of adjustable rate trust preferred securities (2006 Securities). The 2006 Securities bear interest, adjustable quarterly, at 90-day LIBOR plus 1.60%. The \$20 million proceeds from the 2006 Securities were used to purchase an equal principal amount of adjustable rate subordinated debentures of the Company that bear interest, adjustable quarterly, at 90-day LIBOR plus 1.60% (2006 Debentures).

In addition to the issuance of these adjustable rate securities, Ozark II and Ozark III collectively sold \$0.9 million of trust common equity, Ozark IV sold \$0.4 million of trust common equity and Ozark V sold \$0.6 million of trust common equity to the Company. The proceeds from the sales of the trust common equity were used, respectively, to purchase \$0.9 million of 2003 Debentures, \$0.4 million of 2004 Debentures and \$0.6 million of 2006 Debentures issued by the Company.

At September 30, 2008 the Company had \$64.9 million of subordinated debentures outstanding and had an asset of \$1.9 million representing its investment in the common equity issued by the Trusts. The sole assets of the Trusts are the adjustable rate debentures and the liabilities of the Trusts are the 2003 Securities, the 2004 Securities and the 2006 Securities. At September 30, 2008 the Trusts did not have any restricted net assets. The Company has, through various contractual arrangements, unconditionally guaranteed payment of all obligations of the Trusts with respect to the 2003 Securities, 2004 Securities and 2006 Securities. There are no restrictions on the ability of the Trusts to transfer funds to the Company in the form of cash dividends, loans or advances.

The 2003 Securities, 2003 Debentures, 2004 Securities, 2004 Debentures, 2006 Securities and 2006 Debentures mature at or near the thirtieth anniversary date of their issuance. However, these securities and debentures may be prepaid at par, subject to regulatory approval, prior to maturity at any time on or after September 25 and 29, 2008 for the two issues of 2003 Securities and 2003 Debentures, on or after September 28, 2009 for the 2004 Securities and 2004 Debentures, and on or after December 15, 2011 for the 2006 Securities and 2006 Debentures, or at an earlier date upon certain changes in tax laws, investment company laws or regulatory capital requirements.

6. Supplemental Data for Cash Flows

Supplemental cash flow information is as follows:

| | Nine Months Ended September 30, 2008 2007 (Dollars in thousands) | |
|---|--|-----------|
| Cash paid during the period for: | | |
| Interest | \$ 66,813 | \$ 73,651 |
| Taxes | 10,841 | 9,273 |
| Supplemental schedule of non-cash investing and financing activities: | | |
| Net change in unrealized gains and losses on investment securities available for sale (AFS) | 7,745 | (10,509) |
| Unsettled AFS investment security trades: | | |
| Purchases | 543 | 5,610 |
| Sales/calls | 18,625 | |
| Loans transferred to foreclosed assets held for sale | 9,568 | 6,408 |
| Loans advanced for sales of foreclosed assets | 2,402 | 1,118 |

7. Guarantees and Commitments

Outstanding standby letters of credit are contingent commitments issued by the Company generally to guarantee the performance of a customer in third party arrangements. The maximum amount of future payments the Company could be required to make under these guarantees at September 30, 2008 was \$8.5 million. The Company holds collateral to support guarantees when deemed necessary. Collateralized commitments at September 30, 2008 totaled \$6.4 million.

At September 30, 2008 the Company had outstanding commitments to extend credit of \$306 million. These commitments extend over varying periods of time with the majority to be disbursed or to expire within a one-year period.

Table of Contents**8. Stock-Based Compensation**

The Company has a nonqualified stock option plan for employees of the Company. This plan provides for the granting of incentive nonqualified options to purchase shares of common stock in the Company. No option may be granted under this plan for less than the fair market value of the common stock, defined by the plan as the average of the highest reported asked price and the lowest reported bid price, on the date of the grant. While the vesting period and the termination date for the employee plan options are determined when options are granted, all such employee options outstanding at September 30, 2008 were issued with a vesting period of three years and expire seven years after issuance.

The Company also has a nonqualified stock option plan for non-employee directors. This plan permits each director who is not otherwise an employee of the Company, or any subsidiary, to receive options to purchase 1,000 shares of the Company's common stock on the day following his or her election as a director of the Company at each annual meeting of stockholders and up to 1,000 shares upon election or appointment for the first time as a director of the Company. These options are exercisable immediately and expire ten years after issuance.

All shares issued in connection with options exercised under both the employee and non-employee director stock option plans are in the form of newly issued shares.

The following table summarizes stock option activity for the nine months ended September 30, 2008.

| | | Options | Weighted-Average Exercise Price/Share | Weighted-Average Remaining Contractual Life (in years) | Aggregate Intrinsic Value (in thousands) ⁽¹⁾ |
|-------------|--------------------|----------|---|---|--|
| Outstanding | January 1, 2008 | 520,650 | \$ 27.22 | | |
| Granted | | 117,950 | 26.96 | | |
| Exercised | | (36,300) | 6.36 | | |
| Forfeited | | (35,500) | 31.56 | | |
| Outstanding | September 30, 2008 | 566,800 | \$ 28.23 | 5.0 | \$ 1,111 |
| Exercisable | September 30, 2008 | 208,000 | \$ 23.56 | 3.9 | \$ 1,111 |

(1) Based on closing price of \$27.00 per share on September 30, 2008.

Intrinsic value for stock options is defined as the amount by which the current market price of the underlying stock exceeds the exercise price. For those stock options where the exercise price exceeds the current market price of the underlying stock, the intrinsic value is zero. The total intrinsic value of options exercised during the nine months ended September 30, 2008 and 2007 was \$0.6 million and \$1.5 million, respectively.

Options to purchase 117,950 and 12,000 shares of the Company's common stock were issued during the nine-month periods ended September 30, 2008 and 2007, respectively. The fair value of each option grant is estimated on the grant date using the Black-Scholes option pricing model. The total grant date fair value of options to purchase shares of the Company's common stock that vested during the nine months ended September 30, 2008 and 2007 was \$0.4 million and \$0.5 million, respectively.

Stock-based compensation expense for stock options included in non-interest expense was \$0.2 million for both the quarters ended September 30, 2008 and 2007, and \$0.7 million for both the nine-month periods ended September 30, 2008 and 2007. Total unrecognized compensation cost related to nonvested stock-based compensation was \$1.5 million at September 30, 2008 and is expected to be recognized over a weighted-average period of 2.3 years.

9. Comprehensive Income

Unrealized gains and losses on investment securities available for sale, net of income taxes, are the only items included in accumulated other comprehensive income (loss). Total comprehensive income consists of net income, unrealized gains and losses on investment securities AFS, net

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of income taxes, and reclassification adjustments for unrealized gains and losses on AFS investment securities sold, net of income taxes. Total comprehensive income was \$6.7 million and \$11.7 million, respectively, for the three months ended September 30, 2008 and 2007 and \$30.1 million and \$17.6 million, respectively, for the nine months ended September 30, 2008 and 2007.

Table of Contents**10. Fair Value Measurements**

Effective January 1, 2008, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 157, Fair Value Measurements , which defines fair value, establishes a framework for measuring fair value under GAAP, and expands disclosures about fair value measurement. According to SFAS No. 157, fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The Company measures certain of its financial assets and liabilities on a fair value basis using various valuation techniques and assumptions, depending on the nature of the financial asset or liability. Additionally, fair value is used either annually or on a non-recurring basis to evaluate certain financial assets and liabilities for impairment or for disclosure purposes. With respect to the disclosure provisions for its nonfinancial assets and liabilities, the Company has elected the one-year deferral provision as allowed by Financial Accounting Standards Board (FASB) Staff Position No. FAS 157-2, Effective Date of FASB Statement No. 157.

In accordance with SFAS No. 157, the Company applied the following fair value hierarchy.

Level 1 Quoted prices for identical instruments in active markets.

Level 2 Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose inputs or value drivers are observable.

Level 3 Instruments whose inputs or value drivers are unobservable.

Effective October 10, 2008, the FASB issued Staff Position No. FAS 157-3 (FSP 157-3), Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active. FSP 157-3 clarifies the application of SFAS No. 157 in a market that is not active and addresses specific application issues of SFAS No. 157 including (i) how the reporting entity's own assumptions (expected cash flows and appropriate risk-adjusted discount rates) should be considered when measuring fair value when relevant observable inputs do not exist, (ii) how available observable inputs in a market that is not active should be considered when measuring fair value, and (iii) how the use of market quotes (broker quotes, or pricing services for the same or similar financial assets) should be considered when assessing the relevance of observable and unobservable inputs or value drivers available to measure fair value. The provisions of FSP 157-3 were effective upon its issuance, including prior periods for which financial statements have not been issued. The Company has applied the provisions of FSP 157-3 to its financial statements as of and for the period ended September 30, 2008. At September 30, 2008, the Company determined that no active market existed for investment securities AFS with an amortized cost of \$29.8 million. The Company has estimated fair values of such investment securities through the use of unobservable inputs or value drivers. As a result, the Company has transferred these investment securities from Level 2 to Level 3 and estimated that the fair values of such securities was \$28.4 million at September 30, 2008.

The following table sets forth the Company's financial assets and liabilities at September 30, 2008 that are accounted for at fair value.

| | Quoted Prices in Active Markets for Identical Assets (Level 1) | Other Observable Inputs (Level 2) | Unobservable Inputs (Level 3) | Total |
|---|---|--|-------------------------------------|------------|
| | | | (Dollars in thousands) | |
| Assets: | | | | |
| Investment securities AFS ⁽¹⁾ | \$ 118,960 | \$ 551,154 | \$ 28,394 | \$ 698,508 |
| Impaired loans and leases | | | 11,277 | 11,277 |
| Investments in tax credit investments | | | 6,348 | 6,348 |
| Derivative assets interest rate lock commitments (IRLC) and forward sales commitments (FSC) | | | 81 | 81 |
| Liabilities: | | | | |
| Derivatives liabilities IRLC and FSC | | | (81) | (81) |

(1) Does not include \$22.8 million of FHLB and Arkansas Bankers Bancorporation, Inc. stock that do not have readily determinable fair values and are carried at cost.

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The following methods and assumptions are used to estimate the fair value of the Company's financial assets and liabilities that were accounted for at fair value.

Investment securities For investment securities traded in an active market, fair values are measured on a recurring basis, obtained from an independent pricing service and based on quoted market prices if available. If quoted market prices are not available, fair values are based on quoted market prices of comparable securities, broker quotes or comprehensive interest rate tables and pricing matrices. For investment securities traded in a market that is not active, fair value is determined using unobservable inputs or value drivers and is generally determined using expected cash flows and appropriate risk-adjusted discount rates. Expected cash flows are based primarily on the contractual cash flows of the instrument, and the risk-adjusted discount rate is typically the contractual coupon rate of the instrument on the measurement date, adjusted for changes in interest rate spreads of the yields on comparable corporate or municipal bonds and the yields on U.S. Treasuries between the date of purchase and the measurement date.

Impaired loans and leases Fair values are measured on a nonrecurring basis and are based on the underlying collateral value of the impaired loan or lease, net of holding and selling costs, or the estimated discounted cash flows for such loan or lease. In accordance with the provisions of SFAS No. 114, the Company reduced the carrying value of its impaired loans and leases (all of which are included in nonaccrual loans and leases) by \$2.2 million to the estimated fair value of \$11.3 million for such loans and leases at September 30, 2008. The \$2.2 million adjustment to reduce the carrying value of impaired loans and leases to estimated fair value consisted of \$1.8 million of partial charge-offs and \$0.4 million of specific loan and lease loss allocations.

Investments in tax credit investments Fair values are measured on a recurring basis and are based upon total credits and deductions remaining to be allocated and total estimated credits and deductions to be allocated.

Derivative assets and liabilities The fair values of IRLC and FSC derivative assets and liabilities are measured on a recurring basis and are based primarily on the fluctuation of interest rates between the date on which the IRLC and FSC were entered and September 30, 2008.

The following table presents additional information about financial assets and liabilities measured at fair value on a recurring basis and for which the Company has utilized Level 3 inputs or value drivers to determine fair value.

| | Investment Securities AFS | Investments in Tax Credit Investments | Derivative Assets IRLC and FSC | Derivative Liabilities IRLC and FSC |
|--|---------------------------------|---|--------------------------------------|---|
| Balances January 1, 2008 | \$ | \$ 6,425 | \$ 80 | \$ (80) |
| Total realized gains/(losses) included in earnings | | (154) | 1 | (1) |
| Purchases, sales, issuances and settlements, net | | 77 | | |
| Transfers in and/or out of Level 3 | 28,394 | | | |
| Balances September 30, 2008 | \$ 28,394 | \$ 6,348 | \$ 81 | \$ (81) |

11. Recent Accounting Pronouncements

In December 2007, the FASB issued SFAS No. 160, Noncontrolling Interests in Consolidated Financial Statements – an amendment of ARB No. 51. SFAS No. 160 was issued to improve the relevance, comparability and transparency of consolidated financial information relative to noncontrolling, or minority, interest. The provisions of SFAS No. 160 establish accounting and reporting standards that clearly identify and distinguish between the interests of the parent and the noncontrolling owners. SFAS No. 160 is effective for fiscal years, and interim periods within the fiscal years, beginning on or after December 15, 2008. Management has not yet determined the impact, if any, that adoption of SFAS No. 160 will have on the Company's financial position, results of operations or liquidity.

In December 2007, the FASB issued SFAS No. 141 (revised 2007) (SFAS No. 141R), Business Combinations. SFAS No. 141R replaces SFAS No. 141 and was issued to improve the comparability of the information that a reporting entity provides in its financial reports about business combinations. The provisions of SFAS No. 141R apply prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. Management has not yet determined the impact, if any, that adoption of SFAS No. 141R will have on the Company's financial position, results of operations or liquidity in the event an acquisition is made by the Company on or after its effective date.

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12. Recent Significant Federal Legislation Affecting Financial Institutions

In response to the current financial crisis affecting the overall banking system and financial markets in the U.S. and around the world, on October 3, 2008 Congress passed, and the President signed into law, the Emergency Economic Stabilization Act of 2008 (EESA). Under the EESA, the U.S. Department of the Treasury (Treasury) has the authority, among other things, to purchase up to \$700 billion of mortgages, mortgage backed securities and certain other financial instruments from financial institutions for the purpose of stabilizing and providing liquidity to the U.S. financial markets.

On October 14, 2008, the Treasury announced the availability through the Troubled Asset Relief Program (TARP), which was created as part of the EESA, of its voluntary Capital Purchase Program (CPP) for qualifying public financial institutions such as U.S.-controlled banks, savings associations, and certain bank and savings and loan holding companies. Under the CPP, Treasury will use \$250 billion of its \$700 billion available under the EESA to purchase \$125 billion of preferred stock in nine major financial institutions. The remaining \$125 billion will be available for the purchase of preferred stock in qualifying U.S.-controlled banks, savings associations, and certain bank and savings and loan holding companies engaged only in financial activities. The general terms of the preferred stock program are as follows for a participating bank: pay 5% per annum dividends on the Treasury s preferred stock for the first five years and 9% per annum dividends thereafter; cannot increase common stock dividends for three years without the consent of the Treasury while Treasury is an investor; cannot redeem the Treasury preferred stock for three years unless the participating bank raises fully qualifying Tier 1 capital; must receive Treasury s consent to buy back their own stock; Treasury receives warrants entitling Treasury to buy participating bank s common stock equal to 15% of Treasury s total investment in the participating bank; participating bank executives must agree to certain compensation restrictions; and restrictions on the amount of executive compensation which is tax deductible.

The CPP is voluntary, although applications by qualified financial institutions for participation must be submitted to the Treasury by November 14, 2008. The Company is evaluating whether to participate in the Treasury s CPP. The Treasury will determine eligibility and allocation for participating qualified financial institutions after consultation with the appropriate federal banking agency.

In addition to the creation of the TARP, the EESA included a provision for an increase in the amount of deposits insured by the Federal Deposit Insurance Corporation (FDIC) from \$100,000 to \$250,000 until December 2009. Also on October 14, 2008, the FDIC announced a new program the Temporary Liquidity Guarantee Program (TLGP) that provides unlimited deposit insurance on funds in non-interest bearing transaction deposit accounts not otherwise covered by the existing deposit insurance limit of \$250,000. Such non-interest bearing transaction deposit accounts are initially insured at no cost to the institution for 30 days with coverage continuing through December 31, 2009 at a 10 bps fee on deposit amounts in excess of \$250,000. Eligible institutions have a one time opt-out option available on or before November 12, 2008. Also under TLGP, newly issued senior unsecured debt issued on or before June 30, 2009 will be fully insured in the event the issuing institution subsequently fails, or its holding company files for bankruptcy. The debt included in the program includes all newly issued unsecured senior debt, including: promissory notes, commercial paper, inter-bank funding, and any unsecured portion of secured debt. The aggregate coverage for an institution may not exceed 125% of the debt outstanding on September 30, 2008 that was scheduled to mature before June 30, 2009. The guarantee of any newly issued debt will extend to June 30, 2012, even if the maturity of the debt is after that date. Such unsecured debt is initially insured at no cost to the institution for 30 days with coverage continuing at a 75 bps annualized fee. Institutions eligible to participate have a one time opt-out option available on or before November 12, 2008.

The actions described above, together with additional actions announced by the Treasury and other regulatory agencies continue to develop. It is not clear at this time what impact the EESA, TARP, TLGP or any of the other liquidity and funding initiatives of the Treasury and other bank regulatory agencies that have been previously announced, and any additional programs that may be initiated in the future, will have on the financial markets and the financial services industry. The extreme levels of volatility and limited credit availability currently being experienced could continue to affect the U.S. banking industry and the broader U.S. and global economies, which may have an impact on all financial institutions, including the Company.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations **GENERAL**

Net income for Bank of the Ozarks, Inc. (the "Company") was \$9.0 million for the third quarter of 2008, a 7.2% increase from net income of \$8.4 million for the comparable quarter in 2007. Diluted earnings per share were \$0.53 for the quarter ended September 30, 2008, a 6.0% increase from \$0.50 for the quarter ended September 30, 2007. For the nine months ended September 30, 2008, net income totaled \$25.4 million, a 5.7% increase from net income of \$24.0 million for the first nine months of 2007. Diluted earnings per share for the first nine months of 2008 were \$1.50 compared to \$1.43 for the comparable period in 2007, a 4.9% increase.

The Company's annualized return on average assets was 1.18% for the third quarter of 2008 compared to 1.28% for the third quarter of 2007. Its annualized return on average stockholders' equity was 16.70% for the third quarter of 2008 compared to 18.15% for the comparable quarter of 2007. The Company's annualized return on average assets was 1.14% for the first nine months of 2008 compared to 1.25% for the first nine months of 2007. Its annualized return on average stockholders' equity was 16.23% for the first nine months of 2008 compared to 17.70% for the comparable period of 2007.

Total assets were \$3.07 billion at September 30, 2008 compared to \$2.71 billion at December 31, 2007. Loans and leases were \$2.06 billion at September 30, 2008 compared to \$1.87 billion at December 31, 2007. Deposits were \$2.30 billion at September 30, 2008 compared to \$2.06 billion at December 31, 2007.

Stockholders' equity was \$216 million at September 30, 2008 compared to \$191 million at December 31, 2007. Book value per share was \$12.80 at September 30, 2008 compared to \$11.35 at December 31, 2007. Changes in stockholders' equity and book value per share reflect earnings, dividends paid, stock option transactions and changes in unrealized gains and losses on investment securities available for sale.

Annualized results for these interim periods may not be indicative of those for the full year or future periods.

ANALYSIS OF RESULTS OF OPERATIONS

The Company is a bank holding company whose primary business is commercial banking conducted through its wholly-owned state chartered bank subsidiary Bank of the Ozarks (the "Bank"). The Company's results of operations depend primarily on net interest income, which is the difference between the interest income from earning assets, such as loans, leases and investments, and the interest expense incurred on interest bearing liabilities, such as deposits, borrowings and subordinated debentures. The Company also generates non-interest income, including service charges on deposit accounts, mortgage lending income, trust income, bank owned life insurance ("BOLI") income, other charges and fees and gains and losses on sales of investment securities and other assets.

The Company's non-interest expense consists of employee compensation and benefits, net occupancy and equipment and other operating expenses. The Company's results of operations are significantly impacted by its provision for loan and lease losses and its provision for income taxes. The following discussion provides a comparative summary of the Company's operations for the three and nine months ended September 30, 2008 and 2007 and should be read in conjunction with the consolidated financial statements and related notes presented elsewhere in this report.

Net Interest Income

Net interest income is analyzed in the discussion and the following tables on a fully taxable equivalent ("FTE") basis. The adjustment to convert certain income to a FTE basis consists of dividing federal tax-exempt income by one minus the Company's statutory federal income tax rate of 35%. The FTE adjustments to net interest income were \$2.1 million and \$0.9 million, respectively, for the quarters ended September 30, 2008 and 2007 and \$6.5 million and \$2.6 million, respectively, for the nine months ended September 30, 2008 and 2007. No adjustments have been made in this analysis for income exempt from state income taxes or for interest expense deductions disallowed under the provisions of the Internal Revenue Code as a result of investment in certain tax-exempt securities.

Net interest income (FTE) increased 29.8% to \$26.7 million for the quarter ended September 30, 2008, compared to \$20.6 million for the quarter ended September 30, 2007. Net interest income (FTE) increased 27.9% to \$76.5 million for the nine months ended September 30, 2008 compared to \$59.8 million for the nine months ended September 30, 2007. The Company's growth in average earning assets and improvement in its net interest margin (FTE) contributed to the increase in net interest income (FTE) for the third quarter and first nine months of 2008 compared to the same periods in 2007.

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Average earning assets increased 17.6% in the third quarter and 16.3% in the first nine months of 2008 compared with the same periods in 2007. Average loans and leases increased 14.7% in the third quarter and 13.9% in the first nine months of 2008 compared to the same periods in 2007. The Company's aggregate average balance of investment securities increased 26.6% in the third quarter and 23.3% in the first nine months of 2008 compared to the same periods in 2007. The investment securities portfolio comprised 26.5% of the Company's average earning assets during the third quarter and 26.9% of the Company's average earning assets during the first nine months of 2008 compared to 24.6% for the third quarter and 25.4% for the first nine months of 2007.

Net interest margin (FTE) was 3.82% for the quarter ended September 30, 2008 compared to 3.45% for the third quarter of 2007, an increase of 37 basis points (bps). Net interest margin (FTE) for the nine months ended September 30, 2008 was 3.76% compared with 3.42% for the first nine months of 2007, an increase of 34 bps.

Yields on earning assets decreased 95 bps for the quarter and 71 bps for the nine months ended September 30, 2008 compared to the same periods in 2007. The decrease in yields on earning assets was primarily attributable to a decrease in yields on loans and leases of 130 bps for the quarter and 111 bps for the nine months ended September 30, 2008 compared to the same periods in 2007, offset in part by increases in the aggregate yields on its investment securities of 21 bps for the quarter and 50 bps for the nine months ended September 30, 2008 compared to the same periods in 2007.

The decrease in loan and lease yields is attributable to overall decreases in general interest rate levels as a result of the Federal Open Market Committee (FOMC) lowering its federal funds target rate a total of 325 bps through a series of rate reductions beginning in September 2007 and continuing through April 2008. This resulted in many of the Company's variable rate loans repricing to lower rates beginning in the third quarter of 2007 and continuing through the third quarter of 2008. Additionally the Company's loan and lease originations and renewals generally priced at lower interest rates beginning in the third quarter of 2007 and continuing through the third quarter of 2008 as a result of these FOMC interest rate decreases.

As previously noted, the aggregate yields on the Company's investment securities portfolio increased for both the third quarter and the first nine months of 2008 compared to the same periods of 2007. Beginning in February 2008 and continuing through September, the Company purchased a large volume of tax-exempt investment securities with favorable yields. The interest rates on the majority of these securities reset weekly. The Company estimates that its addition of these tax-exempt investment securities increased its net interest margin (FTE) by approximately 11 bps during the first quarter and by approximately 3 bps during the second quarter, and decreased its net interest margin (FTE) by approximately 3 bps during the third quarter of 2008. While these securities were dilutive to net interest margin (FTE) for the third quarter, they were accretive to net interest income.

The rates on interest bearing liabilities decreased 138 bps for the quarter and 111 bps for the nine months ended September 30, 2008 compared to the same periods in 2007. The decrease in rates on interest bearing liabilities was primarily attributable to the overall decreases in general interest rate levels as a result of previously mentioned FOMC actions. The rate on interest bearing deposits, the Company's largest source of interest bearing liabilities, decreased 142 bps for the quarter and 112 bps for the nine months ended September 30, 2008 compared to the same periods in 2007, while aggregate rates on other interest bearing liabilities decreased 141 bps for the quarter and 146 bps for the nine months ended September 30, 2008 compared to the same periods in 2007.

Analysis of Net Interest Income**(FTE = Fully Taxable Equivalent)**

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|-------------------------|---|-------------|--|-------------|
| | 2008 | 2007 | 2008 | 2007 |
| | (Dollars in thousands) | | | |
| Interest income | \$ 45,030 | \$ 44,917 | \$ 135,522 | \$ 131,873 |
| FTE adjustment | 2,074 | 899 | 6,532 | 2,585 |
| Interest income FTE | 47,104 | 45,816 | 142,054 | 134,458 |
| Interest expense | 20,414 | 25,246 | 65,552 | 74,661 |
| Net interest income FTE | \$ 26,690 | \$ 20,570 | \$ 76,502 | \$ 59,797 |

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| | | | | |
|---------------------------------------|-------|-------|-------|-------|
| Yields on earning assets FTE | 6.74% | 7.69% | 6.99% | 7.70% |
| Rates on interest bearing liabilities | 3.10 | 4.48 | 3.41 | 4.52 |
| Net interest margin FTE | 3.82 | 3.45 | 3.76 | 3.42 |

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Table of Contents**Average Consolidated Balance Sheets and Net Interest Analysis - FTE**

Unaudited

| | Three Months Ended September 30, 2008 | | | | | | Nine Months Ended September 30, 2008 | | | | | |
|--|--|--------------------|----------------|--------------------|--------------------|----------------|---|--------------------|----------------|--------------------|--------------------|----------------|
| | Average Balance | Income/ Expense | Yield/ Rate | Average Balance | Income/ Expense | Yield/ Rate | Average Balance | Income/ Expense | Yield/ Rate | Average Balance | Income/ Expense | Yield/ Rate |
| (Dollars in thousands) | | | | | | | | | | | | |
| ASSETS | | | | | | | | | | | | |
| Earning assets: | | | | | | | | | | | | |
| Interest earning deposits and federal funds sold | \$ 575 | \$ 3 | 2.14% | \$ 337 | \$ 4 | 5.05% | \$ 428 | \$ 10 | 3.15% | \$ 300 | \$ 15 | 6.58% |
| Investment securities: | | | | | | | | | | | | |
| Taxable | 392,819 | 5,332 | 5.40 | 440,595 | 6,064 | 5.46 | 397,039 | 16,467 | 5.54 | 457,573 | 18,904 | 5.52 |
| Tax-exempt FTE | 342,565 | 5,905 | 6.86 | 140,482 | 2,529 | 7.14 | 334,637 | 18,589 | 7.42 | 135,666 | 7,263 | 7.16 |
| Loans and leases | | | | | | | | | | | | |
| FTE | 2,042,307 | 35,864 | 6.99 | 1,781,100 | 37,219 | 8.29 | 1,984,426 | 106,988 | 7.20 | 1,741,972 | 108,276 | 8.31 |
| Total earning assets | | | | | | | | | | | | |
| FTE | 2,778,266 | 47,104 | 6.74 | 2,362,514 | 45,816 | 7.69 | 2,716,530 | 142,054 | 6.99 | 2,335,511 | 134,458 | 7.70 |
| Non-interest earning assets | 258,386 | | | 242,156 | | | 256,686 | | | 233,442 | | |
| Total assets | \$ 3,036,652 | | | \$ 2,604,670 | | | \$ 2,973,216 | | | \$ 2,568,953 | | |
| LIABILITIES AND STOCKHOLDERS EQUITY | | | | | | | | | | | | |
| Interest bearing liabilities: | | | | | | | | | | | | |
| Deposits: | | | | | | | | | | | | |
| Savings and interest bearing transaction | \$ 645,338 | \$ 2,500 | 1.54% | \$ 525,407 | \$ 3,610 | 2.73% | \$ 588,675 | \$ 6,902 | 1.57% | \$ 523,670 | \$ 10,695 | 2.73% |
| Time deposits of \$100,000 or more | 906,137 | 8,347 | 3.66 | 882,360 | 11,359 | 5.11 | 929,586 | 28,431 | 4.09 | 919,944 | 35,399 | 5.14 |
| Other time deposits | 510,430 | 4,535 | 3.53 | 495,413 | 6,092 | 4.88 | 509,703 | 14,981 | 3.93 | 492,928 | 18,016 | 4.89 |
| Total interest bearing deposits | 2,061,905 | 15,382 | 2.97 | 1,903,180 | 21,061 | 4.39 | 2,027,964 | 50,314 | 3.31 | 1,936,542 | 64,110 | 4.43 |
| Repurchase agreements with customers | 43,442 | 174 | 1.60 | 41,806 | 387 | 3.67 | 42,637 | 604 | 1.89 | 45,227 | 1,285 | 3.80 |
| Other borrowings | 446,899 | 4,015 | 3.57 | 224,007 | 2,516 | 4.46 | 431,973 | 11,816 | 3.65 | 159,386 | 5,475 | 4.59 |
| Subordinated debentures | 64,950 | 843 | 5.16 | 64,950 | 1,282 | 7.83 | 64,950 | 2,818 | 5.80 | 64,950 | 3,791 | 7.81 |
| Total interest bearing liabilities | 2,617,196 | 20,414 | 3.10 | 2,233,943 | 25,246 | 4.48 | 2,567,524 | 65,552 | 3.41 | 2,206,105 | 74,661 | 4.52 |
| Non-interest bearing liabilities: | | | | | | | | | | | | |
| Non-interest bearing deposits | 191,225 | | | 173,437 | | | 182,216 | | | 170,033 | | |
| | 13,608 | | | 13,596 | | | 14,605 | | | 11,461 | | |

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Other non-interest
bearing liabilities

| | | | | |
|----------------------|-----------|-----------|-----------|-----------|
| Total liabilities | 2,822,029 | 2,420,976 | 2,764,345 | 2,387,599 |
| Stockholders' equity | 214,623 | 183,694 | 208,871 | 181,354 |

| | | | | |
|---|--------------|--------------|--------------|--------------|
| Total liabilities and stockholders' equity | \$ 3,036,652 | \$ 2,604,670 | \$ 2,973,216 | \$ 2,568,953 |
|---|--------------|--------------|--------------|--------------|

| | | | | |
|----------------------------|-----------|-----------|-----------|-----------|
| Net interest income FTE | \$ 26,690 | \$ 20,570 | \$ 76,502 | \$ 59,797 |
|----------------------------|-----------|-----------|-----------|-----------|

| | | | | |
|----------------------------|-------|-------|-------|-------|
| Net interest margin FTE | 3.82% | 3.45% | 3.76% | 3.42% |
|----------------------------|-------|-------|-------|-------|

Table of Contents**Non-Interest Income**

The Company's non-interest income consists primarily of (1) service charges on deposit accounts, (2) mortgage lending income, (3) trust income, (4) BOLI income, (5) appraisal fees, credit life commissions and other credit related fees, (6) safe deposit box rental, operating lease income, brokerage fees and other miscellaneous fees and (7) gains and losses on sales of investment securities and other assets. Non-interest income for the third quarter of 2008 decreased 10.1% to \$4.9 million compared to \$5.4 million for the third quarter of 2007. Non-interest income for the nine months ended September 30, 2008 decreased 8.5% to \$15.6 million compared to \$17.0 million for the nine months ended September 30, 2007.

Service charges on deposit accounts, the Company's largest source of non-interest income, increased 0.9% for the third quarter of 2008 to \$3.10 million compared to \$3.08 million for the same period in 2007. Service charges on deposit accounts decreased 0.9% for the nine months ended September 30, 2008 to \$8.94 million compared to \$9.02 million for the same period in 2007.

Mortgage lending income decreased 20.4% for the third quarter of 2008 to \$0.47 million compared to \$0.59 million for the same period in 2007. Mortgage lending income decreased 16.9% for the nine months ended September 30, 2008 to \$1.78 million compared to \$2.14 million for the same period in 2007. The volume of originations of mortgage loans available for sale decreased 28.8% and 19.2%, respectively, for the third quarter and first nine months of 2008 compared to the same periods in 2007. During the third quarter and first nine months of 2008, approximately 39% and 49%, respectively, of the Company's originations of mortgage loans available for sale were related to mortgage refinancing and approximately 61% and 51%, respectively, were related to new home purchases.

Trust income increased 14.9% for the third quarter of 2008 to \$0.65 million compared to \$0.57 million for the same period in 2007. Trust income increased 20.6% for the nine months ended September 30, 2008 to \$1.88 million compared to \$1.56 million for the same period in 2007. The increase in trust income for both the quarter and nine months ended September 30, 2008 was primarily due to growth in the Company's corporate trust and investment management business as the Company continued to add new customers.

Net losses from sales of investment securities and other assets were \$0.40 million for the third quarter of 2008 compared to a net gain of \$0.12 million for the same period in 2007. Net losses from sales of investment securities and other assets were \$0.26 million for the nine months ended September 30, 2008 compared to net gains of \$0.44 million for the same period in 2007.

Non-interest income from all other sources was \$1.04 million in the third quarter of 2008 compared to \$1.07 million for the same period of 2007. Non-interest income from all other sources was \$3.21 million for the nine months ended September 30, 2008 compared to \$3.84 million for the same period in 2007. During the first quarter of 2007, the Company benefited from \$0.50 million of other non-interest income from the settlement of a contested branch application.

The following table shows non-interest income for the three months and nine months ended September 30, 2008 and 2007.

Non-Interest Income

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--|---|-----------------|--|------------------|
| | 2008 | 2007 | 2008 | 2007 |
| | (Dollars in thousands) | | | |
| Service charges on deposit accounts | \$ 3,102 | \$ 3,075 | \$ 8,939 | \$ 9,017 |
| Mortgage lending income | 473 | 594 | 1,781 | 2,142 |
| Trust income | 649 | 565 | 1,882 | 1,561 |
| BOLI income | 512 | 487 | 1,500 | 1,430 |
| Appraisal fees, credit life commissions and other credit related fees | 96 | 141 | 344 | 389 |
| Safe deposit box rental, operating lease income, brokerage fees and other miscellaneous fees | 308 | 298 | 909 | 882 |
| Gains (losses) on sales of investment securities | (317) | 77 | (297) | 414 |
| Gains (losses) on sales of other assets | (78) | 38 | 35 | 26 |
| Other | 126 | 144 | 460 | 1,140 |
| Total non-interest income | \$ 4,871 | \$ 5,419 | \$ 15,553 | \$ 17,001 |

Table of Contents**Non-Interest Expense**

Non-interest expense increased 17.8% for the third quarter of 2008 to \$13.8 million compared to \$11.7 million for the same period in 2007. Non-interest expense increased 12.3% for the nine months ended September 30, 2008 to \$40.1 million compared with \$35.7 million for the same period in 2007. At September 30, 2008 the Company had 71 banking offices and two loan production offices compared to 69 banking offices and two loan production offices at September 30, 2007. The Company had 703 full time equivalent employees at September 30, 2008 compared to 686 at September 30, 2007.

The Company's efficiency ratio (non-interest expense divided by the sum of net interest income FTE and non-interest income) was 43.8% for the quarter ended September 30, 2008 compared to 45.1% for the quarter ended September 30, 2007. The Company's efficiency ratio for the nine months ended September 30, 2008 was 43.6% compared to 46.5% for the same period in 2007.

The following table shows non-interest expense for the three and nine months ended September 30, 2008 and 2007.

Non-Interest Expense

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|-------------------------------------|------------------|------------------------------------|------------------|
| | 2008 | 2007 | 2008 | 2007 |
| | (Dollars in thousands) | | | |
| Salaries and employee benefits | \$ 7,728 | \$ 6,936 | \$ 22,684 | \$ 21,263 |
| Net occupancy and equipment | 2,318 | 2,059 | 6,575 | 5,997 |
| Other operating expenses: | | | | |
| Postage and supplies | 397 | 403 | 1,242 | 1,219 |
| Advertising and public relations | 308 | 224 | 867 | 756 |
| Telephone and data lines | 318 | 268 | 1,232 | 1,034 |
| Professional and outside services | 338 | 202 | 1,034 | 804 |
| ATM expense | 169 | 201 | 478 | 530 |
| Software expense | 319 | 318 | 918 | 908 |
| FDIC insurance | 283 | 239 | 842 | 449 |
| FDIC and state assessments | 168 | 153 | 482 | 472 |
| Other real estate and foreclosure expense | 468 | 85 | 1,002 | 228 |
| Amortization of intangibles | 55 | 66 | 186 | 197 |
| Other | 952 | 578 | 2,602 | 1,889 |
| Total non-interest expense | \$ 13,821 | \$ 11,732 | \$ 40,144 | \$ 35,746 |

Income Taxes

The provision for income taxes was \$3.3 million for the third quarter and \$9.3 million for the first nine months of 2008 compared to \$3.9 million for the third quarter and \$11.0 million for the first nine months of 2007. The effective income tax rate was 26.5% for the third quarter and 26.8% for the first nine months of 2008 compared to 31.5% for the third quarter and 31.4% for the first nine months of 2007. The increase in the Company's tax-exempt income, principally as a result of purchasing tax-exempt securities beginning in late February 2008 and continuing through September 2008, was the primary factor in the decrease in the effective tax rates as compared to the same periods in 2007. Income exempt from federal and, in some cases, state income taxes includes earnings on certain investment securities, loans and leases with state and political subdivisions, increases in the cash surrender value of BOLI and returns on an investment in a low income housing limited liability company. Certain U.S. government agency securities are exempt from state income taxes but are subject to federal income tax.

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Table of Contents**ANALYSIS OF FINANCIAL CONDITION****Loan and Lease Portfolio**

At September 30, 2008 the Company's loan and lease portfolio was \$2.06 billion, compared to \$1.87 billion at December 31, 2007 and \$1.82 billion at September 30, 2007. Real estate loans, the Company's largest category of loans, include all loans made to finance the development of real property construction projects, provided such loans are secured by real estate, and all other loans secured by real estate as evidenced by mortgages or other liens. Total real estate loans were \$1.70 billion at September 30, 2008, compared to \$1.53 billion at December 31, 2007 and \$1.48 billion at September 30, 2007. The amount and type of loans and leases outstanding at September 30, 2008 and 2007 and at December 31, 2007 and their respective percentage of the total loan and lease portfolio are reflected in the following table.

Loan and Lease Portfolio

| | September 30, | | December 31, | | | |
|--------------------------------|-------------------------------|--------|---------------------|--------|--------------|--------|
| | 2008 | | 2007 | | 2007 | |
| | (Dollars in thousands) | | | | | |
| Real estate: | | | | | | |
| Residential 1-4 family | \$ 276,349 | 13.5% | \$ 277,240 | 15.3% | \$ 279,375 | 14.9% |
| Non-farm/non-residential | 555,616 | 27.0 | 438,841 | 24.2 | 445,303 | 23.8 |
| Construction/land development | 673,202 | 32.8 | 599,418 | 33.0 | 684,775 | 36.6 |
| Agricultural | 90,341 | 4.4 | 95,547 | 5.2 | 91,810 | 4.9 |
| Multifamily residential | 101,489 | 4.9 | 68,813 | 3.8 | 31,414 | 1.7 |
| Total real estate | 1,696,997 | 82.6 | 1,479,859 | 81.5 | 1,532,677 | 81.9 |
| Commercial and industrial | 203,445 | 9.9 | 171,601 | 9.4 | 173,128 | 9.3 |
| Consumer | 79,521 | 3.9 | 88,129 | 4.9 | 87,867 | 4.7 |
| Direct financing leases | 51,128 | 2.5 | 51,606 | 2.8 | 53,446 | 2.8 |
| Agricultural (non-real estate) | 21,382 | 1.0 | 22,815 | 1.3 | 22,439 | 1.2 |
| Other | 2,927 | 0.1 | 1,924 | 0.1 | 1,578 | 0.1 |
| Total loans and leases | \$ 2,055,400 | 100.0% | \$ 1,815,934 | 100.0% | \$ 1,871,135 | 100.0% |

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The amount and type of non-farm/non-residential loans at September 30, 2008 and 2007 and at December 31, 2007, and their respective percentage of the total non-farm/non-residential loan portfolio are reflected in the following table.

Non-Farm/Non-Residential Loans

| | September 30, 2008 | | September 30, 2007 | | December 31, 2007 | |
|---|-----------------------|--------|------------------------|--------|----------------------|--------|
| | | | (Dollars in thousands) | | | |
| Retail, including shopping centers and strip centers | \$ 149,814 | 27.0% | \$ 164,519 | 37.5% | \$ 160,615 | 36.1% |
| Churches and schools | 80,035 | 14.4 | 71,627 | 16.3 | 78,989 | 17.7 |
| Office, including medical offices | 63,076 | 11.3 | 61,362 | 14.0 | 63,920 | 14.4 |
| Office warehouse, warehouse and mini-storage | 42,439 | 7.6 | 44,801 | 10.2 | 44,015 | 9.9 |
| Gasoline stations and convenience stores | 17,052 | 3.1 | 19,742 | 4.5 | 19,297 | 4.3 |
| Hotels and motels | 23,771 | 4.3 | 12,532 | 2.9 | 12,679 | 2.8 |
| Restaurants and bars | 48,184 | 8.7 | 13,609 | 3.1 | 13,902 | 3.1 |
| Manufacturing and industrial facilities | 25,908 | 4.7 | 9,884 | 2.2 | 9,942 | 2.2 |
| Nursing homes and assisted living centers | 15,319 | 2.8 | 6,782 | 1.5 | 5,282 | 1.2 |
| Hospitals, surgery centers and other medical | 49,067 | 8.8 | 3,367 | 0.8 | 2,977 | 0.7 |
| Golf courses, entertainment and recreational facilities | 11,739 | 2.1 | 4,012 | 0.9 | 2,992 | 0.7 |
| Other non-farm/non residential | 29,212 | 5.2 | 26,604 | 6.1 | 30,693 | 6.9 |
| Total | \$ 555,616 | 100.0% | \$ 438,841 | 100.0% | \$ 445,303 | 100.0% |

The amount and type of construction/land development loans at September 30, 2008 and 2007 and at December 31, 2007, and their respective percentage of the total construction/land development loan portfolio are reflected in the following table.

Construction/Land Development Loans

| | September 30, 2008 | | September 30, 2007 | | December 31, 2007 | |
|--|-----------------------|--------|------------------------|--------|----------------------|--------|
| | | | (Dollars in thousands) | | | |
| Unimproved land | \$ 90,444 | 13.4% | \$ 107,765 | 18.0% | \$ 113,526 | 16.6% |
| Land development and lots: | | | | | | |
| 1-4 family residential and multifamily | 215,906 | 32.1 | 171,835 | 28.7 | 185,703 | 27.1 |
| Non-residential | 105,688 | 15.7 | 57,874 | 9.6 | 58,100 | 8.5 |
| Construction: | | | | | | |
| 1-4 family residential: | | | | | | |
| Owner occupied | 18,790 | 2.8 | 21,553 | 3.6 | 24,416 | 3.6 |
| Non-owner occupied: | | | | | | |
| Pre-sold | 15,729 | 2.3 | 9,573 | 1.6 | 7,175 | 1.0 |
| Speculative | 78,728 | 11.7 | 100,199 | 16.7 | 97,710 | 14.3 |
| Multifamily | 21,968 | 3.3 | 18,986 | 3.2 | 63,224 | 9.2 |
| Industrial, commercial and other | 125,949 | 18.7 | 111,633 | 18.6 | 134,921 | 19.7 |
| Total | \$ 673,202 | 100.0% | \$ 599,418 | 100.0% | \$ 684,775 | 100.0% |

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The amount and type of the Company's real estate loans at September 30, 2008 based on the metropolitan statistical area (MSA) and other geographic areas in which the principal collateral is located are reflected in the following table.

Geographic Distribution of Real Estate Loans

| | Residential 1-4 Family | Non-Farm/Non Residential | Construction/ Land Development | Agricultural | Multifamily Residential | Total |
|---|------------------------------|-----------------------------|--------------------------------------|--------------|----------------------------|--------------|
| | (Dollars in thousands) | | | | | |
| Little Rock North Little Rock, AR MSA | \$ 68,110 | \$ 189,334 | \$ 128,630 | \$ 12,054 | \$ 4,998 | \$ 403,126 |
| Fayetteville Springdale Rogers, AR MSA | 16,761 | 25,780 | 72,915 | 6,205 | 771 | 122,432 |
| Fort Smith, AR MSA | 25,300 | 52,106 | 17,624 | 3,322 | 4,096 | 102,448 |
| Hot Springs, AR MSA | 5,304 | 10,184 | 9,073 | | 1,793 | 26,354 |
| Western Arkansas ⁽¹⁾ | 31,907 | 47,231 | 13,445 | 16,384 | 1,730 | 110,697 |
| Northern Arkansas ⁽²⁾ | 98,121 | 45,329 | 16,632 | 48,519 | 639 | 209,240 |
| All other Arkansas ⁽³⁾ | 7,707 | 12,835 | 3,828 | 2,475 | 1,047 | 27,892 |
| Total Arkansas | 253,210 | 382,799 | 262,147 | 88,959 | 15,074 | 1,002,189 |
| Dallas Fort Worth Arlington, TX MSA | 3,078 | 49,802 | 209,991 | | 37,407 | 300,278 |
| Houston Baytown Sugar Land, TX MSA | | 3,407 | 41,098 | | | 44,505 |
| Texarkana, TX Texarkana, AR MSA | 9,083 | 10,670 | 3,957 | 390 | 855 | 24,955 |
| All other Texas ⁽³⁾ | 686 | 15,476 | 8,139 | | | 24,301 |
| Total Texas | 12,847 | 79,355 | 263,185 | 390 | 38,262 | 394,039 |
| Charlotte Gastonia Concord, NC/SC MSA | 611 | 31,129 | 39,290 | | 3,460 | 74,490 |
| All other North Carolina ⁽³⁾ | 72 | 9,450 | 27,416 | | | 36,938 |
| All other South Carolina ⁽³⁾ | 6,404 | 7,732 | 8,610 | | | 22,746 |
| Total North Carolina/ South Carolina | 7,087 | 48,311 | 75,316 | | 3,460 | 134,174 |
| Alabama | | 1,092 | 9,064 | | 36,164 | 46,320 |
| California | | 2,750 | 31,205 | | | 33,955 |
| Virginia | | 1,075 | 15,535 | | | 16,610 |
| Oklahoma ⁽³⁾ | 101 | 3,540 | 10,768 | | | 14,409 |
| All other states ^{(3) (4)} | 3,104 | 36,694 | 5,982 | 992 | 8,529 | 55,301 |
| Total real estate loans | \$ 276,349 | \$ 555,616 | \$ 673,202 | \$ 90,341 | \$ 101,489 | \$ 1,696,997 |

(1) This geographic area includes the following counties in Western Arkansas: Conway, Johnson, Logan, Pope and Yell counties.

(2) This geographic area includes the following counties in Northern Arkansas: Baxter, Boone, Carroll, Fulton, Marion, Newton, Searcy and Van Buren counties.

(3) These geographic areas include all MSA and non-MSA areas that are not separately reported.

(4) Data for individual states is separately presented when aggregate real estate loans in that state exceed \$10 million.

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The amount and percentage of the Company's loan and lease portfolio originated at its offices in Arkansas, Texas and North Carolina are reflected in the following table.

Loan and Lease Portfolio by State of Originating Office

| Originated at Offices In | September 30, | | December 31, | |
|--------------------------|------------------------|--------|--------------|--------|
| | 2008 | 2007 | 2007 | 2007 |
| | (Dollars in thousands) | | | |
| Arkansas | \$ 1,406,902 | 68.4% | \$ 1,460,287 | 78.1% |
| Texas | 554,627 | 27.0 | 264,318 | 16.9 |
| North Carolina | 93,871 | 4.6 | 91,329 | 5.0 |
| Total | \$ 2,055,400 | 100.0% | \$ 1,815,934 | 100.0% |

During 2007 and the first nine months of 2008, the Company's loan and lease portfolio growth was primarily attributable to its Texas offices.

The following table reflects loans and leases as of September 30, 2008 grouped by expected amortizations, expected paydowns or the earliest repricing opportunity for floating rate loans. This cash flow or repricing schedule approximates the Company's ability to reprice the outstanding principal of loans and leases either by adjusting rates on existing loans and leases or reinvesting principal cash flow in new loans and leases.

Loan and Lease Cash Flows or Repricing

| | 1 Year or Less | Over 1 Through 2 Years | Over 2 Through 3 Years | Over 3 Years | Total |
|---|------------------------|------------------------------|------------------------------|-----------------|--------------|
| | (Dollars in thousands) | | | | |
| Fixed rate | \$ 383,998 | \$ 197,261 | \$ 161,525 | \$ 185,896 | \$ 928,680 |
| Floating rate (not at a floor or ceiling rate) | 484,907 | 841 | 331 | 300 | 486,379 |
| Floating rate (at floor rate) | 639,957 | 328 | | | 640,285 |
| Floating rate (at ceiling rate) | 56 | | | | 56 |
| Total | \$ 1,508,918 | \$ 198,430 | \$ 161,856 | \$ 186,196 | \$ 2,055,400 |
| Percentage of total | 73.4% | 9.7% | 7.9% | 9.0% | 100.0% |
| (The remainder of this page intentionally left blank) | | | | | |

Table of Contents**Nonperforming Assets**

Nonperforming assets consist of (1) nonaccrual loans and leases, (2) accruing loans and leases 90 days or more past due, (3) certain restructured loans and leases providing for a reduction or deferral of interest or principal because of a deterioration in the financial position of the borrower or lessee and (4) real estate or other assets that have been acquired in partial or full satisfaction of loan or lease obligations or upon foreclosure.

The Company generally places a loan or lease on nonaccrual status when payments are contractually past due 90 days, or earlier when doubt exists as to the ultimate collection of payments. The Company may continue to accrue interest on certain loans or leases contractually past due 90 days if such loans or leases are both well secured and in the process of collection. At the time a loan or lease is placed on nonaccrual status, interest previously accrued but uncollected is generally reversed and charged against interest income. Nonaccrual loans and leases are generally returned to accrual status when payments are less than 90 days past due and the Company reasonably expects to collect all payments. If a loan or lease is determined to be uncollectible, the portion of the principal determined to be uncollectible will be charged against the allowance for loan and lease losses. Income on nonaccrual loans or leases is recognized on a cash basis when and if actually collected.

The following table presents information concerning nonperforming assets, including nonaccrual and certain restructured loans and leases and foreclosed assets held for sale and repossessions at September 30, 2008 and 2007 and at December 31, 2007.

Nonperforming Assets

| | September 30, 2008 | September 30, 2007 (Dollars in thousands) | December 31, 2007 |
|--|-----------------------|---|----------------------|
| Nonaccrual loans and leases | \$ 14,416 | \$ 3,383 | \$ 6,610 |
| Accruing loans and leases 90 days or more past due | | | 26 |
| Restructured loans and leases ⁽¹⁾ | | | |
| Total nonperforming loans and leases | 14,416 | 3,383 | 6,636 |
| Foreclosed assets held for sale and repossessions ⁽²⁾ | 5,887 | 2,496 | 3,112 |
| Total nonperforming assets | \$ 20,303 | \$ 5,879 | \$ 9,748 |
| Nonperforming loans and leases to total loans and leases | 0.70% | 0.19% | 0.35% |
| Nonperforming assets to total assets | 0.66 | 0.22 | 0.36 |

- (1) All restructured loans and leases as of the dates shown were on nonaccrual status and are included as nonaccrual loans and leases in this table.
- (2) Foreclosed assets held for sale and repossessions are generally written down to estimated market value net of estimated selling and holding costs at the time of transfer from the loan and lease portfolio. The value of such assets is reviewed from time to time throughout the holding period with the value adjusted to the then estimated market value net of estimated selling and holding costs, if lower, until disposition.

The increases in the above ratios at September 30, 2008 were not due to a specific customer or a specific market, but were a result of a number of loans and leases spread across the Company's market area. While the Company's markets in Arkansas, Texas and the Carolinas appear to have been less significantly impacted by weaker economic conditions nationally than some other markets, the Company has not been immune to the effects of the slower economic conditions and the slow down in housing activity, particularly in northwest Arkansas. As a result, its ratios of nonperforming loans and leases and nonperforming assets were higher at September 30, 2008 compared to September 30, 2007 and December 31, 2007.

The Company's credit practices dictate that the larger the loan or lease, the more stringent are the credit standards applied. Softening economic conditions therefore typically affect the Company's smaller loans or leases more adversely than its larger loans or leases, as these smaller loans or leases are not typically underwritten to the more rigorous standards applied progressively to larger loans or leases.

In accordance with the provisions of SFAS No. 114, the Company reduced the carrying value of its impaired loans and leases (all of which were included in nonaccrual loans and leases) by \$2.2 million to the estimated fair value of \$11.3 million for such loans and leases at September 30,

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2008. The \$2.2 million adjustment to reduce the carrying value of impaired loans and leases to estimated fair value consisted of \$1.8 million of partial charge-offs and \$0.4 million of specific loan and lease loss allocations.

Table of Contents**Allowance and Provision for Loan and Lease Losses**

Allowance for Loan and Lease Losses: The following table shows an analysis of the allowance for loan and lease losses for the nine-month periods ended September 30, 2008 and 2007 and the year ended December 31, 2007.

| | Nine Months Ended September 30, 2008 | | Year Ended December 31, 2007 |
|--|--|----------------------|------------------------------------|
| | (Dollars in thousands) | | |
| Balance, beginning of period | \$ 19,557 | \$ 17,699 | \$ 17,699 |
| Loans and leases charged off: | | | |
| Real estate | 2,215 | 674 | 1,230 |
| Commercial and industrial | 1,135 | 806 | 1,798 |
| Consumer | 1,192 | 612 | 1,046 |
| Direct financing leases | 315 | 183 | 367 |
| Agricultural (non-real estate) | 372 | 90 | 203 |
| Total loans and leases charged off | 5,229 | 2,365 | 4,644 |
| Recoveries of loans and leases previously charged off: | | | |
| Real estate | 86 | 44 | 47 |
| Commercial and industrial | 26 | 59 | 62 |
| Consumer | 238 | 172 | 209 |
| Direct financing leases | 20 | 7 | 27 |
| Agricultural (non-real estate) | 4 | 1 | 7 |
| Total recoveries | 374 | 283 | 352 |
| Net loans and leases charged off | 4,855 | 2,082 | 4,292 |
| Provision charged to operating expense | 10,725 | 3,450 | 6,150 |
| Balance, end of period | \$ 25,427 | \$ 19,067 | \$ 19,557 |
| Net charge-offs to average loans and leases outstanding during the periods indicated | 0.33% ⁽¹⁾ | 0.16% ⁽¹⁾ | 0.24% |
| Allowance for loan and lease losses to total loans and leases | 1.24% | 1.05% | 1.05% |
| Allowance for loan and lease losses to nonperforming loans and leases | 176% | 564% | 295% |

(1) Annualized.

Provisions to and the adequacy of the allowance for loan and lease losses are determined in accordance with Statement of Financial Accounting Standards (SFAS) No. 114, Accounting by Creditors for Impairment of a Loan, and SFAS No. 5, Accounting for Contingencies, and are based on the Company's judgment and evaluation of the loan and lease portfolio utilizing objective and subjective criteria. The objective criteria utilized by the Company to assess the adequacy of its allowance for loan and lease losses and required additions to such allowance consists primarily of an internal grading system and specific allowances determined in accordance with SFAS No. 114. The Company also utilizes a peer group analysis and an historical analysis in an effort to validate the overall adequacy of its allowance for loan and lease losses. In addition to these objective criteria, the Company subjectively assesses the adequacy of the allowance for loan and lease losses and the need for additions thereto, with consideration given to the nature and volume of the portfolio, overall portfolio quality, review of specific problem loans and leases, national, regional and local business and economic conditions that may affect the borrowers' or lessees' ability to pay, the value of collateral securing the loans and leases, and other relevant factors.

The Company's allowance for loan and lease losses increased to \$25.4 million at September 30, 2008, or 1.24% of total loans and leases, compared with \$19.6 million, or 1.05% of total loans and leases, at December 31, 2007 and \$19.1 million, or 1.05% of total loans and leases, at September 30, 2007. The Company's allowance for loan and lease losses was equal to 176% of its total nonperforming loans and leases at September 30, 2008 compared to 295% at December 31, 2007 and 564% at September 30, 2007. The increase in the Company's allowance for

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loan and lease losses in 2008 is due to a number of factors including growth in the loan and lease portfolio, changes in loss estimates for individual loans and leases and certain categories of loans and leases and uncertainty regarding economic conditions in general and market conditions in northwest Arkansas in particular. While management believes the current allowance is appropriate, changing economic and other conditions may require future adjustments to the allowance for loan and lease losses.

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Provision for Loan and Lease Losses: The loan and lease loss provision is based on management's judgment and evaluation of the loan and lease portfolio utilizing the criteria discussed above. The provision for loan and lease losses was \$3.4 million for the third quarter and \$10.7 million for the nine months ended September 30, 2008 compared to \$1.1 million for the third quarter and \$3.5 million for the nine months ended September 30, 2007.

Investment Securities

The Company's investment securities portfolio provides a significant source of revenue to the Company. At September 30, 2008 and 2007 and at December 31, 2007, the Company classified all of its investment securities portfolio as available for sale (AFS). Accordingly, its investment securities are stated at estimated fair value in the consolidated financial statements with the unrealized gains and losses, net of related income tax, reported as a separate component of stockholders' equity and included in accumulated other comprehensive income (loss). The Company's investments in Federal Home Loan Bank of Dallas (FHLB) and Arkansas Bankers' Bancorporation, Inc. (ABB) stock do not have readily determinable fair values and are carried at cost. The table below presents the amortized cost and estimated fair value of investment securities AFS at September 30, 2008 and 2007 and at December 31, 2007.

Investment Securities

| | September 30, 2008 | | September 30, 2007 | | December 31, 2007 | |
|---|------------------------|------------------------------|-----------------------|------------------------------|----------------------|------------------------------|
| | Amortized Cost | Fair Value ⁽¹⁾ | Amortized Cost | Fair Value ⁽¹⁾ | Amortized Cost | Fair Value ⁽¹⁾ |
| | (Dollars in thousands) | | | | | |
| Mortgage-backed securities | \$ 371,421 | \$ 353,033 | \$ 371,353 | \$ 353,841 | \$ 370,061 | \$ 344,346 |
| Obligations of state and political subdivisions | 333,206 | 336,094 | 147,540 | 149,148 | 163,339 | 166,467 |
| Securities of U.S. Government agencies | 9,967 | 8,537 | 75,921 | 73,218 | 51,982 | 49,738 |
| FHLB and ABB Stock | 22,777 | 22,777 | 14,229 | 14,229 | 16,753 | 16,753 |
| Other securities | 1,000 | 844 | 1,044 | 1,044 | 1,044 | 1,044 |
| Total | \$ 738,371 | \$ 721,285 | \$ 610,087 | \$ 591,480 | \$ 603,179 | \$ 578,348 |

- (1) For investment securities traded in an active market, the fair values are obtained from an independent third-party pricing source and are based on quoted market prices if available. If quoted market prices are not available, fair values are based on market prices for comparable securities, broker quotes or comprehensive interest rate tables and pricing matrices. For investment securities traded in a market that is not active, fair value is determined using unobservable inputs or value drivers and is generally determined using expected cash flows and appropriate risk-adjusted discount rates. Expected cash flows are based primarily on the contractual cash flows of the instrument, and the risk-adjusted discount rate is typically the contractual coupon rate of the instrument on the measurement date, adjusted for changes in interest rate spreads of the yields on comparable corporate or municipal bonds and the yields on U.S. Treasuries between the date of purchase and the measurement date.

The Company's investment securities portfolio is reported net of unrealized losses of \$17.1 million at September 30, 2008, \$18.6 million at September 30, 2007 and \$24.8 million at December 31, 2007. Except as discussed in the following paragraph, management believes that all of its unrealized losses on investment securities AFS at September 30, 2008 are the result of fluctuations in interest rates and do not reflect deterioration in the credit quality of its investments. Accordingly management considers these unrealized losses to be temporary in nature. The Company has both the ability and the intent to hold these investment securities until maturity or until such time as fair value recovers above cost.

At September 30, 2008, the Company's investment securities portfolio includes a bond issued by SLM Corporation (Sallie Mae) with an amortized cost of \$10.0 million and estimated fair value of \$8.5 million resulting in an unrealized loss of \$1.5 million. The Company believes the unrealized loss was attributable primarily to (i) a recent decrease in profitability and near-term earnings forecasts by industry analysts, (ii) recent changes in federal legislation that have, or are expected to, negatively impact the profitability of federally guaranteed student lending and (iii) severely restricted credit markets that have increased Sallie Mae's cost of funds and reduced available liquidity. The contractual terms of this bond do not permit Sallie Mae to settle it at a price less than the Company's amortized cost. While the Standard & Poor's credit rating for Sallie Mae has recently declined from an A rating to a BBB rating, the Company currently believes it is probable that it will be able to collect all amounts due according to the contractual terms of this security. The Sallie Mae bond matures in September 2015. The Company has the ability

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and intent to hold this investment security until its fair value recovers the unrealized loss, which may be upon maturity, and the Company does not consider the Sallie Mae bond to be other-than-temporarily impaired at September 30, 2008.

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The Company had net losses of \$0.3 million from the sale of \$1.7 million investment securities in the third quarter of 2008 compared with net gains of \$0.1 million from the sale of \$6.3 million of investment securities in the third quarter of 2007. During the first nine months of 2008, the Company generated net losses of \$0.3 million from the sale of approximately \$10.2 million of investment securities. Net gains for the nine months ended September 30, 2007 were \$0.4 million from the sale of approximately \$40.5 million of investment securities. During the quarters ended September 30, 2008 and 2007, investment securities totaling \$309.5 million and \$7.0 million, respectively, matured or were called by the issuer. Investment securities totaling \$1,449.1 million and \$20.8 million matured or were called by the issuer during the nine months ended September 30, 2008 and 2007, respectively. The Company also purchased \$281.5 million and \$22.5 million, respectively, of investment securities during the third quarters of 2008 and 2007 and \$1,612.2 million and \$36.8 million, respectively, during the nine months ended September 30, 2008 and 2007.

During late February and continuing through September of 2008, the Company purchased a large volume of tax-exempt investment securities with favorable yields. The opportunity to acquire these tax-exempt securities was due to unusual market conditions which could change at any time. The interest rates on the majority of these securities reset weekly, and the Company expects that a significant portion of these securities will be called or otherwise paid off in the fourth quarter of 2008.

At September 30, 2008, approximately 49% of the Company's investment securities portfolio was comprised of mortgage-backed securities, primarily collateralized mortgage obligations (CMOs). These CMOs are all U.S. government agency-backed bonds and carry a AAA rating. Substantially all such CMOs have a fixed rate coupon, and the estimated modified duration of the Company's portfolio of CMOs was 6.92 years at September 30, 2008. Modified duration is considered a measure of bond price sensitivity to changes in yield.

The Company invests in securities it believes offer good relative value at the time of purchase, and it will, from time to time reposition its investment securities portfolio. In making its decisions to sell or purchase securities, the Company considers credit ratings, call features, maturity dates, relative yields, current market factors and other relevant factors.

Deposits

The Company's lending and investment activities are funded primarily by deposits. The amount and type of deposits outstanding at September 30, 2008 and 2007 and at December 31, 2007 and their respective percentage of the total deposits are reflected in the following table.

Deposits

| | September 30, 2008 | | September 30, 2007 (Dollars in thousands) | | December 31, 2007 | |
|------------------------------------|-----------------------|--------|---|--------|----------------------|--------|
| Non-interest bearing | \$ 194,104 | 8.4% | \$ 166,970 | 8.3% | \$ 162,994 | 7.9% |
| Interest bearing: | | | | | | |
| Transaction (NOW) | 397,722 | 17.3 | 405,214 | 20.0 | 399,700 | 19.4 |
| Savings | 29,406 | 1.3 | 25,872 | 1.3 | 25,178 | 1.2 |
| Money market | 263,820 | 11.5 | 100,999 | 5.0 | 91,434 | 4.5 |
| Time deposits less than \$100,000 | 531,331 | 23.1 | 486,573 | 24.0 | 471,080 | 22.9 |
| Time deposits of \$100,000 or more | 885,143 | 38.4 | 838,816 | 41.4 | 906,675 | 44.1 |
| Total deposits | \$ 2,301,526 | 100.0% | \$ 2,024,444 | 100.0% | \$ 2,057,061 | 100.0% |

The amount and percentage of the Company's deposits attributable to its offices located in Arkansas and Texas are reflected in the following table.

Deposits by State

| Attributable to Offices In | September 30, 2008 | September 30, 2007 | December 31, 2007 |
|----------------------------|-----------------------|-----------------------|----------------------|
|----------------------------|-----------------------|-----------------------|----------------------|

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| (Dollars in thousands) | | | | | | |
|------------------------|--------------|--------|--------------|--------|--------------|--------|
| Arkansas | \$ 2,022,034 | 87.9% | \$ 1,899,530 | 93.8% | \$ 1,922,746 | 93.5% |
| Texas | 279,492 | 12.1 | 124,914 | 6.2 | 134,315 | 6.5 |
| Total | \$ 2,301,526 | 100.0% | \$ 2,024,444 | 100.0% | \$ 2,057,061 | 100.0% |

As of September 30, 2008, the Company had outstanding brokered deposits assigned to Arkansas offices of \$428 million compared to \$381 million at December 31, 2007 and \$305 million at September 30, 2007.

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LIQUIDITY AND CAPITAL RESOURCES

Growth and Expansion. At September 30, 2008 the Company, through its state chartered subsidiary bank, conducted operations through 73 offices, including 65 banking offices in 34 communities throughout northern, western and central Arkansas, six Texas banking offices, and two loan production offices in Little Rock, Arkansas and Charlotte, North Carolina.

The Company expects to continue its growth and *de novo* branching strategy. During the fourth quarter of 2008, the Company expects to open its new corporate headquarters in Little Rock, Arkansas, and it expects to close a nearby in-store branch. The Company expects to open approximately two additional banking offices and a new operations center in 2009.

Opening new offices is subject to availability of qualified personnel and suitable sites, designing, constructing, equipping and staffing such offices, obtaining regulatory and other approvals and many other conditions and contingencies that the Company cannot predict with certainty.

During the first nine months of 2008, the Company spent \$21.5 million on capital expenditures for premises and equipment. In the fourth quarter of 2008, the Company's capital expenditures are expected to be in the range of \$1.5 million to \$3.5 million including progress payments on construction projects expected to be completed in 2008 through 2009, furniture and equipment costs and acquisition of sites for future development. Actual expenditures may vary significantly from those expected, depending on the number and cost of additional sites acquired for future development, progress or delays encountered on ongoing and new construction projects and other factors.

Bank Liquidity. Liquidity represents an institution's ability to provide funds to satisfy demands from depositors, borrowers and other creditors by either converting assets into cash or accessing new or existing sources of incremental funds. Generally the Company relies on deposits, loan and lease repayments and repayments of its investment securities as its primary sources of funds. The principal deposit sources utilized by the Company include consumer, commercial and public funds customers in the Company's markets and brokered deposits. The Company has used these funds, together with FHLB advances, federal funds purchased and other sources of short-term borrowings, to make loans and leases, acquire investment securities and other assets and to fund continuing operations.

Deposit levels may be affected by a number of factors, including rates paid by competitors, general interest rate levels, returns available to customers on alternative investments, general economic and market conditions and other factors. Loan and lease repayments are a relatively stable source of funds but are subject to the borrowers' and lessees' ability to repay the loans and leases, which can be adversely affected by a number of factors including changes in general economic conditions, adverse trends or events affecting business industry groups or specific businesses, declines in real estate values or markets, business closings or lay-offs, inclement weather, natural disasters and other factors. Furthermore, loans and leases generally are not readily convertible to cash. Accordingly, the Company may be required to rely from time to time on other sources of liquidity to meet loan, lease and deposit withdrawal demands or otherwise fund operations. Such sources include FHLB advances, secured and unsecured federal funds lines of credit from correspondent banks and Federal Reserve Bank (FRB) borrowings.

At September 30, 2008 the Company had unused borrowing availability that was primarily comprised of the following four sources: (1) \$170 million of available blanket borrowing capacity with the FHLB, (2) \$188 million of investment securities available to pledge for federal funds or other borrowings, (3) \$37 million of available unsecured federal funds borrowing lines and (4) \$177 million from borrowing programs of the FRB.

The Company anticipates it will continue to rely primarily on deposits, loan and lease repayments and repayments of its investment securities to provide liquidity, as well as considering other funding resources as appropriate. Additionally, when necessary, the sources of borrowed funds described above will be used to augment the Company's primary funding sources.

In response to the current financial crisis affecting the overall banking system and financial markets in the U.S. and around the world, on October 3, 2008 Congress passed, and the President signed into law, the Emergency Economic Stabilization Act of 2008 (EESA). Under the EESA, the U.S. Department of the Treasury (Treasury) has the authority, among other things, to purchase up to \$700 billion of mortgages, mortgage backed securities and certain other financial instruments from financial institutions for the purpose of stabilizing and providing liquidity to the U.S. financial markets.

On October 14, 2008, the Treasury announced the availability through the Troubled Asset Relief Program (TARP), which was created as part of the EESA, of its voluntary Capital Purchase Program (CPP) for qualifying public financial institutions such as U.S.-controlled banks, savings associations, and certain bank and savings and loan holding companies.

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Under the CPP, Treasury will use \$250 billion of its \$700 billion available under the EESA to purchase \$125 billion of preferred stock in nine major financial institutions. The remaining \$125 billion will be available for the purchase of preferred stock in qualifying U.S.-controlled banks, savings associations, and certain bank and savings and loan holding companies engaged only in financial activities. The general terms of the preferred stock program are as follows for a participating bank: pay 5% per annum dividends on the Treasury's preferred stock for the first five years and 9% per annum dividends thereafter; cannot increase common stock dividends for three years without the consent of the Treasury while Treasury is an investor; cannot redeem the Treasury preferred stock for three years unless the participating bank raises fully qualifying Tier 1 capital; must receive Treasury's consent to buy back their own stock; Treasury receives warrants entitling Treasury to buy participating bank's common stock equal to 15% of Treasury's total investment in the participating bank; participating bank executives must agree to certain compensation restrictions; and restrictions on the amount of executive compensation which is tax deductible.

The CPP is voluntary, although applications by qualified financial institutions for participation must be submitted to the Treasury by November 14, 2008. The Company is evaluating whether to participate in the Treasury's CPP. The Treasury will determine eligibility and allocation for participating qualified financial institutions after consultation with the appropriate federal banking agency.

In addition to the creation of the TARP, the EESA included a provision for an increase in the amount of deposits insured by the Federal Deposit Insurance Corporation (FDIC) from \$100,000 to \$250,000 until December 2009. Also on October 14, 2008, the FDIC announced a new program the Temporary Liquidity Guarantee Program (TLGP) that provides unlimited deposit insurance on funds in non-interest bearing transaction deposit accounts not otherwise covered by the existing deposit insurance limit of \$250,000. Such non-interest bearing transaction deposit accounts are initially insured at no cost to the institution for 30 days with coverage continuing through December 31, 2009 at a 10 bps fee on deposit amounts in excess of \$250,000. Eligible institutions have a one time opt-out option available on or before November 12, 2008. Also under TLGP, newly issued senior unsecured debt issued on or before June 30, 2009 will be fully insured in the event the issuing institution subsequently fails, or its holding company files for bankruptcy. The debt included in the program includes all newly issued unsecured senior debt, including: promissory notes, commercial paper, inter-bank funding, and any unsecured portion of secured debt. The aggregate coverage for an institution may not exceed 125% of the debt outstanding on September 30, 2008 that was scheduled to mature before June 30, 2009. The guarantee of any newly issued debt will extend to June 30, 2012, even if the maturity of the debt is after that date. Such unsecured debt is initially insured at no cost to the institution for 30 days with coverage continuing at a 75 bps annualized fee. Institutions eligible to participate have a one time opt-out option available on or before November 12, 2008.

The actions described above, together with additional actions announced by the Treasury and other regulatory agencies continue to develop. It is not clear at this time what impact the EESA, TARP, TLGP or any of the other liquidity and funding initiatives of the Treasury and other bank regulatory agencies that have been previously announced, and any additional programs that may be initiated in the future, will have on the financial markets and the financial services industry. The extreme levels of volatility and limited credit availability currently being experienced could continue to affect the U.S. banking industry and the broader U.S. and global economies, which may have an impact on all financial institutions, including the Company.

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Capital Compliance. Bank regulatory authorities in the United States impose certain capital standards on all bank holding companies and banks. These capital standards require compliance with certain minimum risk-based capital ratios and a minimum leverage ratio. The risk-based capital ratios consist of (1) Tier 1 capital (i.e. common stockholders' equity excluding goodwill, certain intangibles and net unrealized gains and losses on AFS investment securities, and including, subject to limitations, trust preferred securities (TPS) and other qualifying items) to risk-weighted assets and (2) total capital (Tier 1 capital plus Tier 2 capital, including the qualifying portion of the allowance for loan and lease losses and the portion of TPS not counted as Tier 1 capital) to risk-weighted assets. The leverage ratio is measured as Tier 1 capital to adjusted quarterly average assets.

The Company's and the Bank's risk-based capital and leverage ratios exceeded these minimum requirements at September 30, 2008 and December 31, 2007, and are presented in the following tables.

Consolidated Capital Ratios

| | September 30, 2008 | December 31, 2007 |
|---|------------------------|----------------------|
| | (Dollars in thousands) | |
| Tier 1 capital: | | |
| Stockholders' equity | \$ 215,810 | \$ 190,829 |
| Allowed amount of TPS (subordinated debentures) | 63,000 | 63,000 |
| Net unrealized (gains) losses on AFS investment securities | 10,384 | 15,091 |
| Less goodwill and certain intangible assets | (5,692) | (5,877) |
| Total tier 1 capital | 283,502 | 263,043 |
| Tier 2 capital: | | |
| Qualifying allowance for loan and lease losses | 25,427 | 19,557 |
| Total risk-based capital | \$ 308,929 | \$ 282,600 |
| Risk-weighted assets | \$ 2,500,649 | \$ 2,230,309 |
| Adjusted quarterly average assets for leverage capital | \$ 3,030,960 | \$ 2,683,323 |
| Ratios at end of period: | | |
| Leverage | 9.35% | 9.80% |
| Tier 1 risk-based capital | 11.34 | 11.79 |
| Total risk-based capital | 12.35 | 12.67 |
| Minimum ratio guidelines: | | |
| Leverage ⁽¹⁾ | 3.00% | 3.00% |
| Tier 1 risk-based capital | 4.00 | 4.00 |
| Total risk-based capital | 8.00 | 8.00 |

- (1) Regulatory authorities require institutions to operate at varying levels (ranging from 100-200 bps) above a minimum leverage ratio of 3% depending upon capitalization classification.

Capital Ratios of the Bank

| | September 30, 2008 | December 31, 2007 |
|-----------------------------|------------------------|----------------------|
| | (Dollars in thousands) | |
| Stockholders' equity Tier 1 | \$ 265,260 | \$ 236,122 |

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| | | |
|---------------------------------|-------|-------|
| Leverage ratio | 8.79% | 8.82% |
| Tier 1 risk-based capital ratio | 10.66 | 10.63 |
| Total risk-based capital ratio | 11.68 | 11.51 |

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Dividend Policy. During the quarter ended September 30, 2008, the Company paid a dividend of \$0.13 per share compared to \$0.11 per share in the quarter ended September 30, 2007. On October 1, 2008, the Company's board of directors approved a dividend of \$0.13 per share to be paid during the fourth quarter of 2008. The determination of future dividends on the Company's common stock will depend on conditions existing at that time. The Company's goal is to continue declaring quarterly dividends at approximately the current level, with consideration given to future changes depending on the Company's earnings, capital, liquidity needs and, if the Company participates in the Treasury CPP discussed above, subject to such restrictions as may be required by the Treasury.

CRITICAL ACCOUNTING POLICIES

The Company's determination of the adequacy of the allowance for loan and lease losses is considered to be a critical accounting policy. Provisions to and the adequacy of the allowance for loan and lease losses are based on management's judgment and evaluation of the loan and lease portfolio utilizing objective and subjective criteria. Changes in these criteria or the availability of new information could cause the allowance to be increased or decreased in future periods. In addition, bank regulatory agencies as part of their examination process may require adjustments to the allowance for loan and lease losses based on their judgments and estimates. See the "Analysis of Financial Condition" section of Management's Discussion and Analysis contained in the Company's 2007 annual report on Form 10-K for a detailed discussion of the Company's allowance for loan and lease losses.

The Company's determination of the fair value of its investment securities portfolio is also considered a critical accounting policy. The Company has classified all of its investment securities as AFS. Accordingly, its investment securities are stated at estimated fair value in the consolidated financial statements with unrealized gains and losses, net of related income taxes, reported as a separate component of stockholders' equity and included in accumulated other comprehensive income (loss).

For investment securities traded in an active market, the fair values are obtained from an independent third-party pricing source and are based on quoted market prices if available. If quoted market prices are not available, fair values are based on market prices for comparable securities, broker quotes or comprehensive interest rate tables and pricing matrices. For investment securities traded in a market that is not active, fair value is determined using unobservable inputs or value drivers and is generally determined using expected cash flows and appropriate risk-adjusted discount rates. Expected cash flows are based primarily on the contractual cash flows of the instrument. The risk-adjusted discount rate is typically the contractual coupon rate of the instrument on the measurement date, adjusted for changes in interest rate spreads of the yields on comparable corporate or municipal bonds and the yields on U.S. Treasuries between the date of purchase and the measurement date.

The fair values of the Company's investment securities traded in both active and inactive markets can be volatile and may be influenced by a number of factors including market interest rates, prepayment speeds, discount rates, credit quality of the issuer, general market conditions including market liquidity conditions and other factors. Factors and conditions are constantly changing and fair values could be subject to material variations that may significantly impact the Company's financial condition, results of operations and liquidity.

FORWARD-LOOKING INFORMATION

This Management's Discussion and Analysis of Financial Condition and Results of Operations, other filings made by the Company with the Securities and Exchange Commission and other oral and written statements or reports by the Company and its management include certain forward-looking statements including, without limitation, statements about economic, housing market, competitive and interest rate conditions, plans, goals, expectations and outlook for revenue growth, net income, earnings per share, net interest margin, net interest income, non-interest income including service charge, mortgage lending and trust income, gains and losses on sales of investment securities and other assets, non-interest expense, efficiency ratio, asset quality including the effects of current economic and housing market conditions, nonperforming loans and leases, nonperforming assets, net charge-offs, past due loans and leases, interest rate sensitivity including the effects of possible interest rate changes, future growth and expansion including the plans for opening new offices, opportunities and goals for market share growth, loan, lease and deposit growth, changes in the investment securities portfolio, availability of unused borrowing sources, and other similar forecasts and statements of expectation. Words such as anticipate, believe, estimate, plan, expect, intend and similar expressions, as they apply to the Company or its management, identify forward-looking statements. 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.

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Actual future performance, outcomes and results may differ materially from those expressed in forward-looking statements made by the Company and its management due to certain risks, uncertainties and assumptions. Certain factors that may affect operating results of the Company include, but are not limited to, the following: potential delays or other problems in implementing the Company's growth and expansion strategy, including delays in identifying satisfactory sites, obtaining permits, designing, constructing and opening new offices, obtaining regulatory and other approvals and employing qualified personnel; the ability to attract new deposits, loans and leases; the ability to generate future revenue growth or to control future growth in non-interest expenses; interest rate fluctuations, including changes in the yield curve between short-term and long-term interest rates; competitive factors and pricing pressures, including their effect on net interest margin; general economic (including inflationary pressures and governmental monetary policies) and housing market conditions, including their effect on investment securities values, the creditworthiness of borrowers and lessees and collateral values; changes in legal and regulatory requirements; adoption of new accounting standards or changes in existing accounting requirements; recently enacted and potential legislation, including, but not limited to, legislation intended to stabilize economic and credit markets, to protect homeowners and to regulate securities markets and market participants; and adverse results in future litigation, as well as other factors described in this and other Company reports and statements. Should one or more of the foregoing risks materialize, or should underlying assumptions prove incorrect, actual results or outcomes may vary materially from those described in the forward-looking statements.

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Table of Contents**SELECTED AND SUPPLEMENTAL FINANCIAL DATA**

The following tables set forth selected consolidated financial data of the Company for the three and nine months ended September 30, 2008 and 2007 and supplemental quarterly financial data of the Company for each of the most recent eight quarters beginning with the fourth quarter of 2006 through the third quarter of 2008. These tables are qualified in their entirety by the consolidated financial statements and related notes presented elsewhere in this report.

Selected Consolidated Financial Data

Unaudited

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--|--|--------------|------------------------------------|--------------|
| | 2008 | 2007 | 2008 | 2007 |
| | (Dollars in thousands, except per share amounts) | | | |
| <u>Income statement data:</u> | | | | |
| Interest income | \$ 45,030 | \$ 44,917 | \$ 135,522 | \$ 131,873 |
| Interest expense | 20,414 | 25,246 | 65,552 | 74,661 |
| Net interest income | 24,616 | 19,671 | 69,970 | 57,212 |
| Provision for loan and lease losses | 3,400 | 1,100 | 10,725 | 3,450 |
| Non-interest income | 4,871 | 5,419 | 15,553 | 17,001 |
| Non-interest expense | 13,821 | 11,732 | 40,144 | 35,746 |
| Net income | 9,011 | 8,402 | 25,383 | 24,009 |
| <u>Share and per share data:</u> | | | | |
| Earnings diluted | \$ 0.53 | \$ 0.50 | \$ 1.50 | \$ 1.43 |
| Book value | 12.80 | 11.23 | 12.80 | 11.23 |
| Dividends | 0.13 | 0.11 | 0.37 | 0.31 |
| Weighted-average diluted shares outstanding (thousands) | 16,872 | 16,849 | 16,866 | 16,830 |
| End of period shares outstanding (thousands) | 16,855 | 16,811 | 16,855 | 16,811 |
| <u>Balance sheet data at period end:</u> | | | | |
| Total assets | \$ 3,070,546 | \$ 2,651,305 | \$ 3,070,546 | \$ 2,651,305 |
| Total loans and leases | 2,055,400 | 1,815,934 | 2,055,400 | 1,815,934 |
| Allowance for loan and lease losses | 25,427 | 19,067 | 25,427 | 19,067 |
| Total investment securities | 721,285 | 591,480 | 721,285 | 591,480 |
| Total deposits | 2,301,526 | 2,024,444 | 2,301,526 | 2,024,444 |
| Repurchase agreements with customers | 46,329 | 42,656 | 46,329 | 42,656 |
| Other borrowings | 426,524 | 310,379 | 426,524 | 310,379 |
| Subordinated debentures | 64,950 | 64,950 | 64,950 | 64,950 |
| Total stockholders' equity | 215,810 | 188,754 | 215,810 | 188,754 |
| Loan and lease to deposit ratio | 89.31% | 89.70% | 89.31% | 89.70% |
| <u>Average balance sheet data:</u> | | | | |
| Total average assets | \$ 3,036,652 | \$ 2,604,670 | \$ 2,973,216 | \$ 2,568,953 |
| Total average stockholders' equity | 214,623 | 183,694 | 208,871 | 181,354 |
| Average equity to average assets | 7.07% | 7.05% | 7.03% | 7.06% |
| <u>Performance ratios:</u> | | | | |
| Return on average assets* | 1.18% | 1.28% | 1.14% | 1.25% |
| Return on average stockholders' equity* | 16.70 | 18.15 | 16.23 | 17.70 |
| Net interest margin FTE* | 3.82 | 3.45 | 3.76 | 3.42 |
| Efficiency | 43.79 | 45.14 | 43.61 | 46.55 |
| Dividend payout | 24.29 | 21.97 | 24.53 | 21.65 |
| <u>Asset quality ratios:</u> | | | | |
| Net charge-offs to average total loans and leases* | 0.27% | 0.17% | 0.33% | 0.16% |
| Nonperforming loans and leases to total loans and leases | 0.70 | 0.19 | 0.70 | 0.19 |
| Nonperforming assets to total assets | 0.66 | 0.22 | 0.66 | 0.22 |
| Allowance for loan and lease losses as a percentage of: | | | | |

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| | | | | |
|---|-------|-------|-------|-------|
| Total loans and leases | 1.24% | 1.05% | 1.24% | 1.05% |
| Nonperforming loans and leases | 176% | 564% | 176% | 564% |
| <u>Capital ratios at period end:</u> | | | | |
| Leverage | 9.35% | 9.89% | 9.35% | 9.89% |
| Tier 1 risk-based capital | 11.34 | 11.98 | 11.34 | 11.98 |
| Total risk-based capital | 12.35 | 12.87 | 12.35 | 12.87 |

* Ratios annualized based on actual days.

Table of Contents**Supplemental Quarterly Financial Data**

Unaudited

| | 12/31/06 | 3/31/07 | 6/30/07 | 9/30/07 | 12/31/07 | 3/31/08 | 6/30/08 | 9/30/08 |
|--|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|
| Earnings Summary: | | | | | | | | |
| Net interest income | \$ 17,523 | \$ 18,249 | \$ 19,291 | \$ 19,671 | \$ 20,406 | \$ 21,751 | \$ 23,603 | \$ 24,616 |
| Federal tax (FTE) adjustment | 912 | 848 | 838 | 899 | 974 | 1,691 | 2,767 | 2,074 |
| Net interest income (FTE) | 18,435 | 19,097 | 20,129 | 20,570 | 21,380 | 23,442 | 26,370 | 26,690 |
| Provision for loan and lease losses | (900) | (1,100) | (1,250) | (1,100) | (2,700) | (3,325) | (4,000) | (3,400) |
| Non-interest income | 6,434 | 5,959 | 5,623 | 5,419 | 5,975 | 5,125 | 5,557 | 4,871 |
| Non-interest expense | (12,506) | (12,138) | (11,876) | (11,732) | (12,507) | (12,881) | (13,442) | (13,821) |
| Pretax income (FTE) | 11,463 | 11,818 | 12,626 | 13,157 | 12,148 | 12,361 | 14,485 | 14,340 |
| FTE adjustment | (912) | (848) | (838) | (899) | (974) | (1,691) | (2,767) | (2,074) |
| Provision for income taxes | (3,196) | (3,449) | (3,702) | (3,856) | (3,437) | (2,905) | (3,111) | (3,255) |
| Net income | \$ 7,355 | \$ 7,521 | \$ 8,086 | \$ 8,402 | \$ 7,737 | \$ 7,765 | \$ 8,607 | \$ 9,011 |
| Earnings per share - diluted | \$ 0.44 | \$ 0.45 | \$ 0.48 | \$ 0.50 | \$ 0.46 | \$ 0.46 | \$ 0.51 | \$ 0.53 |
| Non-interest Income: | | | | | | | | |
| Service charges on deposit accounts | \$ 2,768 | \$ 2,834 | \$ 3,107 | \$ 3,075 | \$ 3,176 | \$ 2,871 | \$ 2,967 | \$ 3,102 |
| Mortgage lending income | 744 | 731 | 817 | 594 | 526 | 672 | 636 | 473 |
| Trust income | 550 | 465 | 531 | 565 | 661 | 604 | 629 | 649 |
| Bank owned life insurance income | 471 | 465 | 478 | 487 | 489 | 489 | 499 | 512 |
| Gains (losses) on sales of investment securities | 1,341 | 337 | | 77 | 106 | 20 | | (317) |
| Gains (losses) on sales of other assets | (145) | 35 | (47) | 38 | 461 | (93) | 206 | (78) |
| Other | 705 | 1,092 | 737 | 583 | 556 | 562 | 620 | 530 |
| Total non-interest income | \$ 6,434 | \$ 5,959 | \$ 5,623 | \$ 5,419 | \$ 5,975 | \$ 5,125 | \$ 5,557 | \$ 4,871 |
| Non-interest Expense: | | | | | | | | |
| Salaries and employee benefits | \$ 7,360 | \$ 7,310 | \$ 7,016 | \$ 6,936 | \$ 7,399 | \$ 7,332 | \$ 7,624 | \$ 7,728 |
| Net occupancy expense | 1,900 | 1,971 | 1,967 | 2,059 | 2,101 | 2,074 | 2,183 | 2,318 |
| Other operating expenses | 3,181 | 2,792 | 2,827 | 2,671 | 2,942 | 3,410 | 3,569 | 3,720 |
| Amortization of intangibles | 65 | 65 | 66 | 66 | 65 | 65 | 66 | 55 |
| Total non-interest expense | \$ 12,506 | \$ 12,138 | \$ 11,876 | \$ 11,732 | \$ 12,507 | \$ 12,881 | \$ 13,442 | \$ 13,821 |
| Allowance for Loan and Lease Losses: | | | | | | | | |
| Balance at beginning of period | \$ 17,340 | \$ 17,699 | \$ 18,128 | \$ 18,747 | \$ 19,067 | \$ 19,557 | \$ 21,063 | \$ 23,432 |
| Net charge-offs | (541) | (671) | (631) | (780) | (2,210) | (1,819) | (1,631) | (1,405) |
| Provision for loan and lease losses | 900 | 1,100 | 1,250 | 1,100 | 2,700 | 3,325 | 4,000 | 3,400 |
| Balance at end of period | \$ 17,699 | \$ 18,128 | \$ 18,747 | \$ 19,067 | \$ 19,557 | \$ 21,063 | \$ 23,432 | \$ 25,427 |
| Selected Ratios: | | | | | | | | |
| Net interest margin - FTE* | 3.22% | 3.35% | 3.46% | 3.45% | 3.47% | 3.69% | 3.77% | 3.82% |
| Overhead ratio* | 1.99 | 1.94 | 1.86 | 1.79 | 1.84 | 1.84 | 1.76 | 1.81 |
| Efficiency ratio | 50.29 | 48.44 | 46.12 | 45.14 | 45.72 | 45.09 | 42.10 | 43.79 |

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| | | | | | | | | |
|---|------|------|------|------|------|------|------|------|
| Net charge-offs to average loans and leases* | 0.13 | 0.16 | 0.14 | 0.17 | 0.47 | 0.38 | 0.33 | 0.27 |
| Nonperforming loans and leases/total loans and leases | 0.34 | 0.25 | 0.23 | 0.19 | 0.35 | 0.68 | 0.74 | 0.70 |
| Nonperforming assets/total assets | 0.24 | 0.27 | 0.26 | 0.22 | 0.36 | 0.58 | 0.59 | 0.66 |
| Loans and leases past due 30 days or more, including past due non-accrual loans and leases, to total loans and leases | 0.60 | 0.84 | 0.53 | 0.45 | 1.14 | 1.30 | 0.92 | 0.94 |

* Annualized based on actual days.

Table of Contents**Item 3. Quantitative and Qualitative Disclosures about Market Risk**

Interest rate risk results from timing differences in the repricing of assets and liabilities or from changes in relationships between interest rate indexes. The Company's interest rate risk management is the responsibility of the ALCO and Investments Committee (ALCO), which reports to the board of directors. The ALCO oversees the asset/liability (interest rate risk) position, liquidity and funds management and investment portfolio functions of the Company.

The Company regularly reviews its exposure to changes in interest rates. Among the factors considered are changes in the mix of interest earning assets and interest bearing liabilities, interest rate spreads and repricing periods. Typically, the ALCO reviews on at least a quarterly basis the Company's relative ratio of rate sensitive assets (RSA) to rate sensitive liabilities (RSL) and the related cumulative gap for different time periods. However, the primary tool used by ALCO to analyze the Company's interest rate risk and interest rate sensitivity is an earnings simulation model.

This earnings simulation modeling process projects a baseline net interest income (assuming no changes in interest rate levels) and estimates changes to that baseline net interest income resulting from changes in interest rate levels. The Company relies primarily on the results of this model in evaluating its interest rate risk. This model incorporates a number of additional factors including: (1) the expected exercise of call features on various assets and liabilities, (2) the expected rates at which various RSA and RSL will reprice, (3) the expected growth in various interest earning assets and interest bearing liabilities and the expected interest rates on new assets and liabilities, (4) the expected relative movements in different interest rate indexes which are used as the basis for pricing or repricing various assets and liabilities, (5) existing and expected contractual cap and floor rates on various assets and liabilities, (6) expected changes in administered rates on interest bearing transaction, savings, money market and time deposit accounts and the expected impact of competition on the pricing or repricing of such accounts and (7) other relevant factors. Inclusion of these factors in the model is intended to more accurately project the Company's expected changes in net interest income resulting from interest rate changes. The Company models its change in net interest income assuming interest rates go up 100 bps, up 200 bps, down 100 bps and down 200 bps. For purposes of this model, the Company has assumed that the change in interest rates phases in over a 12-month period. While the Company believes this model provides a reasonably accurate projection of its interest rate risk, the model includes a number of assumptions and predictions which may or may not be correct and may impact the model results. These assumptions and predictions include inputs to compute baseline net interest income, growth rates, expected changes in administered rates on interest bearing deposit accounts, competition and a variety of other factors that are difficult to accurately predict. Accordingly, there can be no assurance the earnings simulation model will accurately reflect future results.

The following table presents the earnings simulation model's projected impact of a change in interest rates on the projected baseline net interest income for the 12-month period commencing October 1, 2008. This change in interest rates assumes parallel shifts in the yield curve and does not take into account changes in the slope of the yield curve.

| Shift in Interest Rates (in bps) | % Change in Projected Baseline Net Interest Income |
|----------------------------------|--|
| +200 | 0.6% |
| +100 | 0.2 |
| -100 | (0.5) |
| -200 | (1.1) |

In the event of a shift in interest rates, management may take certain actions intended to mitigate the negative impact to net interest income or to maximize the positive impact to net interest income. These actions may include, but are not limited to, restructuring of interest earning assets and interest bearing liabilities, seeking alternative funding sources or investment opportunities and modifying the pricing or terms of loans, leases and deposits.

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Item 4. **Controls and Procedures**

(a) Evaluation of disclosure controls and procedures.

An evaluation as of the end of the period covered by this quarterly report was carried out under the supervision and with the participation of the Company's management, including the Company's Chairman and Chief Executive Officer and its Chief Financial Officer and Chief Accounting Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures, which are defined under SEC rules as controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files under the Exchange Act is recorded, processed, summarized and reported within required time periods. Based upon that evaluation, the Company's Chairman and Chief Executive Officer and its Chief Financial Officer and Chief Accounting Officer concluded that the Company's disclosure controls and procedures were effective.

(b) Changes in Internal Control over Financial Reporting.

The Company's management, including the Company's Chairman and Chief Executive Officer and its Chief Financial Officer and Chief Accounting Officer, has evaluated any changes in the Company's internal control over financial reporting that occurred during the quarterly period covered by this report and has concluded that there was no change during the quarterly period covered by this report that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

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PART II. OTHER INFORMATION

Item 1. **Legal Proceedings**

The Company is party to various litigation matters arising in the ordinary course of business. While the ultimate resolution of these matters cannot be determined at this time, management of the Company does not believe that such matters, individually or in the aggregate, will have a material adverse effect on the future results of operations, financial condition or liquidity of the Company.

Item 1A. **Risk Factors**

There have been no material changes to the risk factors disclosed in Item 1A. Risk Factors in the Company's 2007 annual report on Form 10-K filed with the Securities and Exchange Commission on March 12, 2008.

Item 2. **Unregistered Sales of Equity Securities and Use of Proceeds**

The Company had no unregistered sales of equity securities and did not purchase any shares of its common stock during the period covered by this report.

Item 3. **Defaults Upon Senior Securities**

Not Applicable.

Item 4. **Submission of Matters to a Vote of Security Holders**

Not Applicable

Item 5. **Other Information**

Not Applicable.

Item 6. **Exhibits**

Reference is made to the Exhibit Index set forth immediately following the signature page of this report.

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SIGNATURE

Pursuant to the requirements of the Securities and Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Bank of the Ozarks, Inc.

DATE: November 5, 2008

/s/ Paul Moore

Paul Moore

Chief Financial Officer and Chief Accounting Officer

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Bank of the Ozarks, Inc.

Exhibit Index

**Exhibit
Number**

- 3 (i) (a) Amended and Restated Articles of Incorporation of the Registrant, dated May 22, 1997 (previously filed as Exhibit 3.1 to the Company's Registration Statement on Form S-1 filed with the Commission on May 22, 1997, as amended, Commission File No. 333-27641, and incorporated herein by this reference).
- 3 (i) (b) Articles of Amendment to the Amended and Restated Articles of Incorporation of the Registrant dated December 9, 2003 (previously filed as Exhibit 3.2 to the Company's Annual Report on Form 10-K filed with the Commission on March 12, 2004 for the year ended December 31, 2003, and incorporated herein by this reference).
- 3 (ii) Amended and Restated Bylaws of the Registrant, dated December 11, 2007 (previously filed as Exhibit 3(ii) to the Company's Current Report on Form 8-K filed with the Commission on December 11, 2007, and incorporated herein by this reference).
- 31.1 Certification of Chairman and Chief Executive Officer.
- 31.2 Certification of Chief Financial Officer and Chief Accounting Officer.
- 32.1 Certification of Chairman and Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of Chief Financial Officer and Chief Accounting Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.