STATE BOARD OF FINANCE

November 17, 2008
10:00 a.m.
Conference Room, Suite 275, Victory Building

AGENDA

a. Old business, including approval of minutes of July 29, 2008.

b. $110 million State Board of Finance CD maturing on December 31, 2008, and the investment of $110 million.

c. Arkansas Capital Group Corporation's Request for Restructuring of State Line of Credit (updated memorandum attached).

d. New Business.

e. Next meeting.

To: State Board of Finance
From: Sam Walls, CEO
Date: July 24, 2008 **(UPDATED 11/12/08)**
RE: Refinance of State Notes

Arkansas Capital Corporation respectfully requests the following:

1. Refinance the following three state notes (Currently priced at the 2-year treasury):

	Current Rate	New Rate
• #157 - $8,928,000	3.723%	1.25% (Primary Credit), adjust qtrly
• #158 - $6,550,000	2.820%	1.25% (Primary Credit), adjust qtrly
• #159 - $11,400,000	4.765%	1.25% (Primary Credit), adjust qtrly

2. Change the borrowing formula and rate associated with new state notes:

    - Current – 10 year note tied to 6 month CD rate, adjusted every six months.

    - Proposed – 10 year note tied to primary credit rate, adjusted quarterly.

3. Approve access to additional $6,422,000 under state line of credit to be drawn as needed to facilitate increasing loan demand.

Historically, the State invested in ACC notes at the federal discount rate fixed for ten years. In 2003, the formula was changed to the 2-year treasury note, adjusted every two years. In 2005, the formula was again changed to the "Average six month CD rate as determined by the State Bank Commissioner", adjusted every six months. As a SBA lender, ACC prices its loans in relation to prime with lending rates adjusted quarterly. Due to the unprecedented drop in interest rates, a mismatch in the timing of the repricing of our loans and the state's invested dollars has occurred. The situation has resulted in ACC incurring an operational loss.

A recent examination by the Arkansas State Bank Department resulted in a favorable outcome. The exam concluded that ACC's earnings performance is hampered by an increasing cost of funds. In addition, it was noted that the mismatching of re-pricing assets (loans) and liabilities (state notes) coupled with SBA lending cost (which lowers risk to the state) has negatively impacted ACC's earnings and constrained our ability to manage the interest rate risk during the most recent falling rate environment. Our goal is to be equally matched with state borrowings and our clients' loans both repricing on a quarterly basis, thus minimizing interest rate risk exposure.

Thank you in advance for your consideration.