CapStone Bank

October 16, 2008

Dear Shareholder:

We are pleased to report continued growth and positive operating results for CapStone for the quarter and nine months ended September 30, 2008. Total assets at the end of the quarter were $141.6 million, compared to $98.1 million at September 30, 2007, an increase of 44.4%. During the same period loans grew from $74.6 million to $110.3 million, an increase of 48%, and deposits grew from $66.7 million to $97.4 million, an increase of 46.1%. Net income for the nine months ended September 30, 2008 was $203,033, an increase of $623,253 over the $420,220 loss incurred during the same period last year. The growth in net income for this nine month period was a function of net interest income growing by $809,118 (33.8%), non interest income growing by $71,219 (262.1%) and non interest expense increasing by $95,852 (4.2%).

Net income for the third quarter of 2008 was $80,127 compared to $59,183 for the third quarter of 2007, an increase of 35.4%. In further comparing the two quarters, net interest income grew by $131,515 (13.6%), non interest income grew by $38,466 (518.4%) and non interest expense increased by $5,804 (0.7%).

Our asset quality at September 30, 2008 was solid, with no loans thirty days or more past due, no non performing loans and no non accrual loans. However, during the third quarter we had one loan charge-off which represented 0.35% of average loans for the year through September 30, 2008. At September 30, 2008, our loan loss allowance was $1.4 million, or 1.30% of total loans, compared to $932,000 or 1.25% of total loans at September, 30 2007. We also continue to be a very well capitalized institution with a tier one leverage ratio of 16.41% at September 30, 2008. This is one of the highest capital ratios for a commercial bank in North Carolina and far exceeds the 5% “well capitalized” tier one level as defined by the FDIC.

There is no doubt these are uncertain economic times for both the national and local economies. While our local economy will not be immune to the current credit cycle, we believe we are well positioned to weather the cycle given our strong capital position, liquidity and core earnings. We also have one of the most experienced executive management teams and boards of directors of any community bank operating in North Carolina. We know what it takes to manage through tough economic times. Our focus will remain on asset quality and capital preservation, while at the same time building quality relationships with both new and existing clients. In spite of the numerous challenges our economy faces in the quarters ahead, we are optimistic about the future of CapStone.

Our stock continues to perform well with 12,000 shares trading during the third quarter of 2008 and a last trade price of $13.75 per share.

Thank you for your continued support of CapStone Bank. If you have any questions about the performance of the bank or the services we provide, please contact either of us.

Sincerely,

Michael S. Patterson
Executive Chairman

Steven R. Ogburn
President and CEO

CapStone Bank

Balance Sheet - Unaudited

	Actual Sep 08	Actual Sep 07	$ Change	% Change
Assets				
Cash and due from banks	974,915	1,059,275	-84,359	-8
Fed funds sold & repos	2,753,120	2,654,668	98,452	3.7
Investment Securities - Taxable	27,300,662	19,512,191	7,788,472	39.9
Loans, net of unearned income	110,315,567	74,559,556	35,756,012	48
Less: Allowance for loan losses	-1,435,000	-932,000	-503,000	-54
Premises and equipment, net	564,145	575,183	-11,038	-1.9
Accrued interest receivable	587,556	540,235	47,321	8.8
Other assets	563,704	96,068	467,636	486.8
Total Assets	**141,624,670**	**98,065,175**	**43,559,495**	**44.4**
Liabilities				
Non-Interest Bearing Deposits	5,985,007	7,150,693	-1,165,687	-16.3
Interest bearing demand deposits	11,203,374	4,451,254	6,752,120	151.7
Savings and Money Market Deposits	21,352,209	24,316,391	-2,964,182	-12.2
Time Deposits - Retail	25,831,685	22,648,440	3,183,245	14.1
Time Deposits - Wholesale	33,035,980	8,126,000	24,909,980	306.5
Total Deposits	97,408,254	66,692,778	30,715,476	46.1
Accrued expenses and other liabilities	536,519	632,985	-96,466	-15.2
FHLB Advances	16,000,000	5,000,000	11,000,000	220
Other Borrowings	4,001,880	3,084,390	917,490	29.7
Total Liabilities	117,946,653	75,410,153	42,536,500	56.4
Equity				
Common stock	10,812,000	10,811,000	1,000	0
Capital surplus	13,218,585	12,882,740	335,845	2.6
Retained earnings	-910,941	-636,819	-274,122	-43
Accumulated other comprehensive income (loss)	355,340	18,321	337,019	1839.5
Net Income	203,033	-420,220	623,253	148.3
Total Equity	23,678,017	22,655,021	1,022,995	4.5
Total Liabilities & Equity	**141,624,670**	**98,065,175**	**43,559,495**	**44.4**

CAPSTONE BANK

Income Statement - Unaudited

	YTD Actual Sep 08	YTD Actual Sep 07	$ Change	% Change
Interest Income				
Interest on Loans	4,642,029	3,243,723	1,398,305	43.1
Fees on Loans	70,209	42,392	27,817	65.6
Interest on federal funds sold	28,705	244,271	-215,566	-88.2
Interest on deposits with banks	7,678	0	7,678	0
Investment Securities - Taxable	932,473	496,163	436,310	87.9
Total Interest Income	5,681,093	4,026,549	1,654,545	41.1
Interest Expense				
Interest bearing demand deposits	93,624	27,104	66,519	245.4
Savings and Money Market Deposits	416,054	754,331	-338,278	-44.8
Time Deposits - Retail	857,840	525,980	331,859	63.1
Time Deposits - Wholesale	574,050	186,394	387,655	208
FHLB Advances	430,656	62,579	368,077	588.2
Interest on other borrowings	105,522	75,928	29,594	39
Total Interest Expense	2,477,744	1,632,318	845,427	51.8
Net Interest Income	**3,203,349**	**2,394,231**	**809,118**	**33.8**
Provision for loan losses	737,232	576,000	161,232	28
Net Int. Inc. After Prov. for Loan Losses	**2,466,117**	**1,818,231**	**647,886**	**35.6**
Non Interest Income				
Service charges and fees	53,515	4,904	48,611	991.3
Securities gains (losses), net	13,537	0	13,537	0
Mortgage loan and related fees	11,040	5,108	5,932	116.1
Other noninterest income	20,295	17,157	3,138	18.3
Total Non Interest Income	98,388	27,169	71,219	262.1
Non Interest Expense				
Salaries and employee benefits	1,396,569	1,537,111	-140,542	-9.1
Occupancy	222,909	178,965	43,944	24.6
Other noninterest expense	741,993	549,544	192,449	35
Total Non Interest Expense	2,361,472	2,265,620	95,852	4.2
Income Before Taxes	**203,033**	**-420,220**	**623,253**	**148.3**
Net Income	**203,033**	**-420,220**	**623,253**	**148.3**