CapStone Bank

April 14, 2011

Dear Shareholder:

For the quarter ended March 31, 2011, we are pleased to once again report positive operating results for CapStone Bank. We ended the first quarter of 2011 with $203.6 million in total assets, an increase of $9.6 million or 4.9% above the same period in 2010. Total loans were $133.2 million on March 31, 2011, an increase of $2.5 million or 1.9% over the same period in 2010. For the same comparative period, total deposits grew from $130.2 million to $136.9 million, an increase of $6.7 million or 5.1%.

Net income for the quarter ended March 31, 2011 was $428,105 versus $360,057 for the same period in 2010, an increase of $68,048 or 18.9%. Our pre tax, pre provision income for the quarter ended March 31, 2011 was $806,105 compared to $719,015 for the same quarter in 2010, an increase of $87,090 or 12.1%. Our return on average equity was 6.48% for the quarter ended March 31, 2011, compared to 5.70% for the same period in 2010. Return on average assets for the first quarter of 2011 was 0.87% versus 0.76% for the same period in 2010. The increase in net income was fueled primarily by growth in net interest income which increased by $263,356 or 15.5% over the same period in 2010.

The overall quality of our loan portfolio improved significantly when compared to the same quarterly period in 2010. At quarter end March 31, 2011, total nonperforming assets to total assets were 0.75% or $1.5 million, compared to 1.07% or $2.1 million for the same period last year. It is also an improvement over year end 2010 when they were 0.99% or $2.0 million. Net charge offs during the quarter were $11,687 or 0.01% of total loans. During the first quarter of 2011, we added $148,000 to our provision for loan losses, bringing our total to $3.2 million or 2.37% of total loans. We also continue to be a very well capitalized bank with a ratio of average equity to average assets of 13.2% which is one of the highest ratios of any bank in North Carolina.

While we are pleased with our growth in net income and improvement in our asset quality, we would like to see stronger growth in our loan portfolio. However, until the local economy shows further improvement, loan growth will continue to be sluggish. As always, we will continue to look for opportunities to grow the Bank in a manner which will increase shareholder value.

We sincerely appreciate the support of our shareholders and encourage you to attend our Annual Meeting of Shareholders which will be held at North Ridge Country Club on April 20, 2011 at 10:00 a.m.

Sincerely,

Michael S. Patterson
Executive Chairman

Steven R. Ogburn
President and CEO

CapStone Bank

Balance Sheet

(Unaudited)

	Actual Mar 2011	Actual Mar 2010	$ Change	% Change
Assets				
Cash and due from banks	$ 3,399,758	$ 1,926,738	$ 1,473,020	76.5
Fed funds sold & repos	8,187,452	2,618,919	5,568,534	212.6
Interest bearing deposits with banks	24,676,216	27,136,105	-2,459,889	-9.1
Investment Securities - Taxable	19,730,368	21,968,427	-2,238,059	-10.2
Investment Securities - Tax-exempt	9,826,925	5,621,294	4,205,631	74.8
Loans, net of unearned income	133,200,899	130,665,347	2,535,553	1.9
Less: Allowance for loan losses	-3,159,764	-2,610,639	-549,125	-21
Premises and equipment, net	259,428	414,158	-154,731	-37.4
Accrued interest receivable	680,593	651,583	29,011	4.5
Other assets	6,758,376	5,577,514	1,180,862	21.2
Total Assets	**$ 203,560,252**	**$ 193,969,446**	**$ 9,590,806**	**4.9**
Liabilities				
Non-Interest Bearing Deposits	$ 14,610,709	$ 11,021,977	$ 3,588,732	32.6
Interest bearing demand deposits	24,820,735	20,365,302	4,455,433	21.9
Savings and Money Market Deposits	38,454,282	34,618,549	3,835,733	11.1
Time Deposits - Retail	29,275,519	32,729,769	-3,454,251	-10.6
Time Deposits - Wholesale	29,714,154	31,469,688	-1,755,534	-5.6
Total Deposits	136,875,399	130,205,284	6,670,114	5.1
Accrued expenses and other liabilities	1,112,974	1,621,854	-508,880	-31.4
FHLB Advances	35,000,000	22,500,000	12,500,000	55.6
Other Borrowings	3,634,534	13,953,312	-10,318,778	-74
Total Liabilities	**176,622,906**	**168,280,450**	**8,342,457**	**5**
Equity				
Common stock	10,812,000	10,812,000	-	-
Capital surplus	13,717,099	13,597,949	119,150	0.9
Retained earnings	1,534,382	301,305	1,233,077	409.2
Accumulated other comprehensive income (los	445,760	617,686	-171,926	-27.8
Net Income	428,105	360,058	68,047	18.9
Total Equity	**26,937,346**	**25,688,997**	**1,248,349**	**4.9**
Total Liabilities & Equity	**$ 203,560,252**	**$ 193,969,446**	**$ 9,590,806**	**4.9**

CapStone Bank

Income Statement

(Unaudited)

	QTD Actual Mar 2011	QTD Actual Mar 2010	$ Change	% Change
Interest Income				
Interest on Loans	$ 1,929,897	$ 1,837,215	$ 92,682	5
Fees on Loans	55,807	33,309	22,498	67.5
Interest on federal funds sold	1,297	1,016	281	27.6
Interest on deposits with banks	114,346	112,236	2,110	1.9
Investment Securities - Taxable	206,058	255,705	-49,646	-19.4
Investment Securities - Tax-exempt	84,089	57,106	26,983	47.3
Total Interest Income	2,391,494	2,296,586	94,908	4.1
Interest Expense				
Interest bearing demand deposits	33,668	56,291	-22,623	-40.2
Savings and Money Market Deposits	73,641	110,290	-36,649	-33.2
Time Deposits - Retail	108,898	174,128	-65,230	-37.5
Time Deposits - Wholesale	58,359	105,941	-47,582	-44.9
Total Interest Expense on Deposits	274,566	446,649	-172,084	-38.5
FHLB Advances	150,135	138,562	11,572	8.4
Interest on other borrowings	1,030	8,967	-7,936	-88.5
Total Interest Expense	425,731	594,179	-168,448	-28.3
Net Interest Income	**1,965,763**	**1,702,407**	**263,356**	**15.5**
Provision for loan losses	148,000	189,000	-41,000	-21.7
Net In. Inc. After Prov. for Loan Losses	**1,817,763**	**1,513,407**	**304,356**	**20.1**
Non Interest Income				
Service charges and fees	17,813	22,938	-5,125	-22.3
Securities gains (losses), net	2,603	-	2,603	-
Mortgage loan and related fees	4,842	-	4,842	-
Other noninterest income	35,648	32,595	3,052	9.4
Total Non Interest Income	60,906	55,533	5,372	9.7
Non Interest Expense				
Salaries and employee benefits	778,596	599,258	179,339	29.9
Occupancy	102,851	98,230	4,621	4.7
Other noninterest expense	339,117	341,438	-2,321	-0.7
Total Non Interest Expense	1,220,564	1,038,926	181,638	17.5
Income Before Taxes	**658,105**	**530,015**	**128,090**	**24.2**
Income taxes	230,000	169,957	60,043	35.3
Net Income	**$ 428,105**	**$ 360,057**	**$ 68,047**	**18.9**