

CAPITAL CITY BANK GROUP INC  
Form 10-Q  
August 08, 2011

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended June 30, 2011

OR

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: 0-13358

CAPITAL CITY BANK GROUP, INC.  
(Exact name of registrant as specified in its charter)

Florida  
(State or other jurisdiction of incorporation or organization)

59-2273542  
(I.R.S. Employer Identification No.)

217 North Monroe Street, Tallahassee, Florida  
(Address of principal executive office)

32301  
(Zip Code)

(850) 402-7000  
(Registrant's telephone number, including area code)

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 has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "large accelerated filer", "accelerated filer", and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer       Accelerated filer       Non-accelerated filer       Smaller reporting company   
(Do not check if 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

At July 31, 2011, 17,151,996 shares of the Registrant's Common Stock, \$.01 par value, were outstanding.

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CAPITAL CITY BANK GROUP, INC.  
 QUARTERLY REPORT ON FORM 10-Q  
 FOR THE PERIOD ENDED JUNE 30, 2011  
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INTRODUCTORY NOTE  
Caution Concerning Forward-Looking Statements

This Quarterly Report on Form 10-Q contains "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements include, among others, statements about our beliefs, plans, objectives, goals, expectations, estimates and intentions that are subject to significant risks and uncertainties and are subject to change based on various factors, many of which are beyond our control. The words "may," "could," "should," "would," "believe," "anticipate," "estimate," "expect," "intend," "plan," "target," "goal," and similar expressions are intended to identify forward-looking statements.

All forward-looking statements, by their nature, are subject to risks and uncertainties. Our actual future results may differ materially from those set forth in our forward-looking statements.

Our ability to achieve our financial objectives could be adversely affected by the factors discussed in detail in Part I, Item 2. "Management's Discussion and Analysis of Financial Condition and Results of Operations" and Part II, Item 1A. "Risk Factors" in this Quarterly Report on Form 10-Q, the following sections of our Annual Report on Form 10-K for the year ended December 31, 2010 (the "2010 Form 10-K"): (a) "Introductory Note" in Part I, Item 1. "Business"; (b) "Risk Factors" in Part I, Item 1A., as updated in our subsequent quarterly reports filed on Form 10-Q, and (c) "Introduction" in "Management's Discussion and Analysis of Financial Condition and Results of Operations," in Part II, Item 7 as well as:

- § legislative or regulatory changes, including the Dodd-Frank Wall Street Reform and Consumer Protection Act;
- § the strength of the United States economy in general and the strength of the local economies in which we conduct operations;
- § the accuracy of our financial statement estimates and assumptions, including the estimate for our loan loss provision and the valuation allowance on deferred tax assets;
  - § the frequency and magnitude of foreclosure of our loans;
  - § continued depression of the market value of the Company that could result in an impairment of goodwill;
  - § restrictions on our operations, including the inability to pay dividends without our regulators' consent;
- § the effects of the health and soundness of other financial institutions, including the FDIC's need to increase Deposit Insurance Fund assessments;
  - § our ability to declare and pay dividends;
  - § changes in the securities and real estate markets;
  - § changes in monetary and fiscal policies of the U.S. Government;
- § increased competition and its effect on pricing, including the effect of the repeal of Regulation Q on our net interest income;
  - § inflation, interest rate, market and monetary fluctuations;
- § the effects of our lack of a diversified loan portfolio, including the risks of geographic and industry concentrations;
  - § our need and our ability to incur additional debt or equity financing;
  - § the effects of harsh weather conditions, including hurricanes, and man-made disasters;
  - § our ability to comply with the extensive laws and regulations to which we are subject;
- § the willingness of clients to accept third-party products and services rather than our products and services and vice versa;
  - § technological changes;
  - § negative publicity and the impact on our reputation;
- § the effects of security breaches and computer viruses that may affect our computer systems;
  - § changes in consumer spending and saving habits;
  - § growth and profitability of our noninterest income;
  - § changes in accounting principles, policies, practices or guidelines;

- § the limited trading activity of our common stock;
- § the concentration of ownership of our common stock;
- § anti-takeover provisions under federal and state law as well as our Articles of Incorporation and our Bylaws;
- § our ability to integrate the business and operations of companies and banks that we have acquired, and those we may acquire in the future;
- § other risks described from time to time in our filings with the Securities and Exchange Commission; and
- § our ability to manage the risks involved in the foregoing.

However, other factors besides those referenced also could adversely affect our results, and you should not consider any such list of factors to be a complete set of all potential risks or uncertainties. Any forward-looking statements made by us or on our behalf speak only as of the date they are made. We do not undertake to update any forward-looking statement, except as required by applicable law.

## PART I. FINANCIAL INFORMATION

## Item 1. CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

CAPITAL CITY BANK GROUP, INC.  
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION  
AS OF JUNE 30, 2011 AND DECEMBER 31, 2010

| (Dollars In Thousands, Except Share Data)   | Unaudited<br>June 30,<br>2011 | December<br>31, 2010 |
|---|-------------------------------|----------------------|
| <b>ASSETS</b>   |                               |                      |
| Cash and Due From Banks   | \$ 71,554                     | \$ 35,410            |
| Federal Funds Sold and Interest Bearing Deposits  | 223,183                       | 200,783              |
| Total Cash and Cash Equivalents   | 294,737                       | 236,193              |
| Investment Securities, Available-for-Sale   | 304,313                       | 309,731              |
| Loans, Net of Unearned Interest   | 1,687,602                     | 1,758,671            |
| Allowance for Loan Losses   | (31,080)                      | (35,436)             |
| Loans, Net  | 1,656,522                     | 1,723,235            |
| Premises and Equipment, Net   | 112,576                       | 115,356              |
| Goodwill  | 84,811                        | 84,811               |
| Other Intangible Assets   | 888                           | 1,348                |
| Other Real Estate Owned   | 61,016                        | 57,937               |
| Other Assets  | 84,395                        | 93,442               |
| Total Assets  | \$ 2,599,258                  | \$ 2,622,053         |
| <b>LIABILITIES</b>  |                               |                      |
| Deposits:   |                               |                      |
| Noninterest Bearing Deposits  | \$ 568,813                    | \$ 546,257           |
| Interest Bearing Deposits   | 1,532,198                     | 1,557,719            |
| Total Deposits  | 2,101,011                     | 2,103,976            |
| Short-Term Borrowings   | 65,237                        | 92,928               |
| Subordinated Notes Payable  | 62,887                        | 62,887               |
| Other Long-Term Borrowings  | 49,196                        | 50,101               |
| Other Liabilities   | 60,383                        | 53,142               |
| Total Liabilities   | 2,338,714                     | 2,363,034            |
| <b>SHAREOWNERS' EQUITY</b>  |                               |                      |
| Preferred Stock, \$.01 par value, 3,000,000 shares authorized; no shares outstanding  | -                             | -                    |
| Common Stock, \$.01 par value, 90,000,000 shares authorized; 17,127,320 and 17,100,081 shares issued and outstanding at June 30, 2011 and December 31, 2010, respectively | 171                           | 171                  |
| Additional Paid-In Capital  | 37,724                        | 36,920               |
| Retained Earnings   | 237,709                       | 237,679              |
| Accumulated Other Comprehensive Loss, Net of Tax  | (15,060)                      | (15,751)             |

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|   |              |              |
|---|--------------|--------------|
| Total Shareowners' Equity                 | 260,544      | 259,019      |
| Total Liabilities and Shareowners' Equity | \$ 2,599,258 | \$ 2,622,053 |

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.



CAPITAL CITY BANK GROUP, INC.  
CONSOLIDATED STATEMENTS OF INCOME  
FOR THE THREE AND SIX MONTHS ENDED JUNE 30  
(Unaudited)

| (Dollars in Thousands, Except Per Share Data)       | Three Months Ended |               | Six Months Ended |                |
|---|--------------------|---------------|------------------|----------------|
|   | 2011               | 2010          | 2011             | 2010           |
| <b>INTEREST INCOME</b>                              |                    |               |                  |                |
| Interest and Fees on Loans                          | \$ 24,305          | \$ 26,644     | \$ 48,252        | \$ 53,636      |
| Investment Securities:                              |                    |               |                  |                |
| U.S. Treasuries                                     | 405                | 330           | 806              | 433            |
| U.S. Government Agencies                            | 336                | 299           | 693              | 619            |
| States and Political Subdivisions                   | 193                | 406           | 412              | 896            |
| Other Securities                                    | 83                 | 79            | 177              | 156            |
| Federal Funds Sold                                  | 145                | 176           | 316              | 348            |
| Total Interest Income                               | 25,467             | 27,934        | 50,656           | 56,088         |
| <b>INTEREST EXPENSE</b>                             |                    |               |                  |                |
| Deposits  | 1,083              | 2,363         | 2,341            | 5,301          |
| Short-Term Borrowings                               | 110                | 12            | 221              | 29             |
| Subordinated Notes Payable                          | 343                | 639           | 683              | 1,290          |
| Other Long-Term Borrowings                          | 492                | 551           | 986              | 1,077          |
| Total Interest Expense                              | 2,028              | 3,565         | 4,231            | 7,697          |
| <b>NET INTEREST INCOME</b>                          | <b>23,439</b>      | <b>24,369</b> | <b>46,425</b>    | <b>48,391</b>  |
| Provision for Loan Losses                           | 3,545              | 3,633         | 7,678            | 14,373         |
| Net Interest Income After Provision For Loan Losses | 19,894             | 20,736        | 38,747           | 34,018         |
| <b>NONINTEREST INCOME</b>                           |                    |               |                  |                |
| Service Charges on Deposit Accounts                 | 6,309              | 7,039         | 12,292           | 13,667         |
| Data Processing                                     | 764                | 919           | 1,738            | 1,819          |
| Asset Management Fees                               | 1,080              | 1,080         | 2,160            | 2,100          |
| Retail Brokerage Fees                               | 939                | 846           | 1,668            | 1,411          |
| Securities Transactions                             | -                  | -             | -                | 5              |
| Mortgage Banking Fees                               | 568                | 641           | 1,185            | 1,149          |
| Bank Card Fees                                      | 2,558              | 2,362         | 5,054            | 4,537          |
| Other   | 2,230              | 1,787         | 6,685            | 3,953          |
| Total Noninterest Income                            | 14,448             | 14,674        | 30,782           | 28,641         |
| <b>NONINTEREST EXPENSE</b>                          |                    |               |                  |                |
| Salaries and Associate Benefits                     | 16,000             | 15,584        | 32,577           | 32,363         |
| Occupancy, Net                                      | 2,447              | 2,585         | 4,843            | 4,993          |
| Furniture and Equipment                             | 2,117              | 2,192         | 4,343            | 4,373          |
| Intangible Amortization                             | 107                | 710           | 460              | 1,420          |
| Other Real Estate                                   | 3,033              | 4,082         | 6,710            | 6,907          |
| Other   | 7,463              | 9,476         | 15,565           | 17,957         |
| Total Noninterest Expense                           | 31,167             | 34,629        | 64,498           | 68,013         |
| <b>INCOME (LOSS) BEFORE INCOME TAXES</b>            | <b>3,175</b>       | <b>781</b>    | <b>5,031</b>     | <b>(5,354)</b> |
| Income Tax Expense (Benefit)                        | 1,030              | 50            | 1,576            | (2,622)        |

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|                                     |    |            |    |            |    |            |    |            |
|-------------------------------------|----|------------|----|------------|----|------------|----|------------|
| NET INCOME (LOSS)                   | \$ | 2,145      | \$ | 731        | \$ | 3,455      | \$ | (2,732)    |
| Basic Net Income (Loss) Per Share   | \$ | 0.12       | \$ | 0.04       | \$ | 0.20       | \$ | (0.16)     |
| Diluted Net Income (Loss) Per Share | \$ | 0.12       | \$ | 0.04       | \$ | 0.20       | \$ | (0.16)     |
| Average Basic Shares Outstanding    |    | 17,127,302 |    | 17,063,176 |    | 17,124,468 |    | 17,060,135 |
| Average Diluted Shares Outstanding  |    | 17,139,234 |    | 17,074,202 |    | 17,134,520 |    | 17,071,031 |

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

CAPITAL CITY BANK GROUP, INC.  
CONSOLIDATED STATEMENT OF CHANGES IN SHAREOWNERS' EQUITY  
(Unaudited)

| (Dollars In Thousands,<br>Except Share Data)  | Shares<br>Outstanding | Common<br>Stock | Additional<br>Paid-In<br>Capital | Retained<br>Earnings | Accumulated<br>Other<br>Comprehensive<br>Income, Net<br>of Taxes | Total      |
|---|-----------------------|-----------------|----------------------------------|----------------------|--|------------|
| Balance, December 31,<br>2010                 | 17,100,081            | \$ 171          | \$ 36,920                        | \$ 237,679           | \$ (15,751)  | \$ 259,019 |
| Comprehensive Income:                         |                       |                 |                                  |                      |  |            |
| Net Income                                    | -                     | -               | -                                | 3,455                | -  | 3,455      |
| Net Change in Unrealized<br>Gain On           |                       |                 |                                  |                      |  |            |
| Available-for-Sale<br>Securities (net of tax) | -                     | -               | -                                | -                    | 691  | 691        |
| Total Comprehensive<br>Income                 | -                     | -               | -                                | -                    | -  | 4,146      |
| Cash Dividends (\$0.20 per<br>share)          | -                     | -               | -                                | (3,425)              | -  | (3,425)    |
| Stock Performance Plan                        |                       |                 |                                  |                      |  |            |
| Compensation                                  | -                     | -               | 391                              | -                    | -  | 391        |
| Issuance of Common Stock                      | 27,239                | -               | 413                              | -                    | -  | 413        |
| Balance, June 30, 2011                        | 17,127,320            | \$ 171          | \$ 37,724                        | \$ 237,709           | \$ (15,060)  | \$ 260,544 |

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

CAPITAL CITY BANK GROUP, INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
FOR THE SIX MONTHS ENDED JUNE 30  
(Unaudited)

| (Dollars in Thousands)   | 2011          | 2010            |
|--|---------------|-----------------|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>                                      |               |                 |
| Net Income (Loss)  | \$ 3,455      | \$ (2,732)      |
| Adjustments to Reconcile Net Income to<br>Cash Provided by Operating Activities: |               |                 |
| Provision for Loan Losses  | 7,678         | 14,373          |
| Depreciation   | 3,464         | 3,495           |
| Net Securities Amortization  | 1,951         | 1,537           |
| Amortization of Intangible Assets  | 460           | 1,420           |
| Gain (Loss) on Securities Transactions   | -             | (5)             |
| Loss on Impaired Security  | -             | 61              |
| Origination of Loans Held-for-Sale   | (51,887)      | (59,639)        |
| Proceeds From Sales of Loans Held-for-Sale                                       | 54,181        | 56,119          |
| Net Gain From Sales of Loans Held-for-Sale                                       | (1,186)       | (1,149)         |
| Non-Cash Compensation  | 391           | 115             |
| Decrease in Deferred Income Taxes  | 417           | 538             |
| Net Decrease in Other Assets   | 28,048        | 7,495           |
| Net Increase in Other Liabilities  | 7,353         | 10,186          |
| Net Cash Provided By Operating Activities  | 54,325        | 31,814          |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>                                      |               |                 |
| Securities Available-for-Sale:   |               |                 |
| Purchases  | (41,915)      | (91,038)        |
| Sales  | -             | 505             |
| Payments, Maturities, and Calls  | 46,502        | 47,871          |
| Net Decrease in Loans  | 35,001        | 54,993          |
| Purchase of Premises & Equipment   | (685)         | (4,858)         |
| Net Cash Provided By Investing Activities  | 38,903        | 7,473           |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>                                      |               |                 |
| Decrease in Deposits   | (2,965)       | (57,923)        |
| Net Decrease in Short-Term Borrowings  | (27,690)      | (14,465)        |
| Increase in Other Long-Term Borrowings   | 789           | 8,015           |
| Repayment of Other Long-Term Borrowings  | (1,695)       | (1,790)         |
| Dividends Paid   | (3,425)       | (4,949)         |
| Issuance of Common Stock   | 302           | 420             |
| Net Cash Used by Financing Activities  | (34,684)      | (70,692)        |
| <b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>                                   | <b>58,544</b> | <b>(31,405)</b> |
| Cash and Cash Equivalents at Beginning of Period                                 | 236,193       | 334,293         |
| Cash and Cash Equivalents at End of Period                                       | \$ 294,737    | \$ 302,888      |

Supplemental Disclosure:

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|   |    |        |    |        |
|---|----|--------|----|--------|
| Interest Paid on Deposits                           | \$ | 2,641  | \$ | 5,804  |
| Interest Paid on Debt                               |    | 1,975  |    | 2,407  |
| Taxes Paid  |    | 2,737  |    | 338    |
| Loans Transferred to Other Real Estate Owned        |    | 22,926 |    | 23,904 |
| Issuance of Common Stock as Non-Cash Compensation   |    | 413    |    | 420    |
| Transfer of Current Portion of Long-Term Borrowings | \$ | -      | \$ | 16     |

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

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CAPITAL CITY BANK GROUP, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

Capital City Bank Group, Inc. (“CCBG” or the “Company”) provides a full range of banking and banking-related services to individual and corporate clients through its subsidiary, Capital City Bank, with banking offices located in Florida, Georgia, and Alabama. The Company is subject to competition from other financial institutions, is subject to regulation by certain government agencies and undergoes periodic examinations by those regulatory authorities.

The unaudited consolidated financial statements included herein have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission, including Regulation S-X. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations. Prior period financial statements have been reformatted and amounts reclassified, as necessary, to conform to the current presentation. The Company and its subsidiary follow accounting principles generally accepted in the United States (“GAAP”) and reporting practices applicable to the banking industry. The principles that materially affect its financial position, results of operations and cash flows are set forth in the Notes to Consolidated Financial Statements, which are included in the 2010 Form 10-K.

In the opinion of management, the consolidated financial statements contain all adjustments, which are those of a recurring nature, and disclosures necessary to present fairly the financial position of the Company as of June 30, 2011 and December 31, 2010, the results of operations for the three and six months ended June 30, 2011 and 2010, and cash flows for the six months ended June 30, 2011 and 2010.

NOTE 2 - INVESTMENT SECURITIES

Investment Portfolio Composition. The amortized cost and related market value of investment securities available-for-sale were as follows:

| (Dollars in Thousands)                    | June 30, 2011  |                  |                   |              |
|---|----------------|------------------|-------------------|--------------|
|   | Amortized Cost | Unrealized Gains | Unrealized Losses | Market Value |
| U.S. Treasury                             | \$ 168,585     | \$ 1,625         | \$ 3              | \$ 170,207   |
| U.S. Government Agencies and Corporations | 10,367         | -                | 4                 | 10,363       |
| States and Political Subdivisions         | 56,577         | 255              | 14                | 56,818       |
| Mortgage-Backed Securities                | 54,149         | 985              | 59                | 55,075       |
| Other Securities(1)                       | 12,450         | -                | 600               | 11,850       |
| Total Investment Securities               | \$ 302,128     | \$ 2,865         | \$ 680            | \$ 304,313   |

| (Dollars in Thousands) | December 31, 2010 |                  |                   |              |
|------------------------|-------------------|------------------|-------------------|--------------|
|                        | Amortized Cost    | Unrealized Gains | Unrealized Losses | Market Value |
| U.S. Treasury          | \$ 160,913        | \$ 1,371         | \$ 134            | \$ 162,150   |
|                        | -                 | -                | -                 | -            |

U.S. Government Agencies and  
Corporations

|                                   |            |          |          |            |
|-----------------------------------|------------|----------|----------|------------|
| States and Political Subdivisions | 78,990     | 319      | 9        | 79,300     |
| Mortgage-Backed Securities        | 56,099     | 678      | 560      | 56,217     |
| Other Securities(1)               | 12,664     | -        | 600      | 12,064     |
| Total Investment Securities       | \$ 308,666 | \$ 2,368 | \$ 1,303 | \$ 309,731 |

(1) Includes Federal Home Loan Bank and Federal Reserve Bank stock recorded at cost of \$7.0 million and \$4.8 million, respectively, at June 30, 2011 and \$7.2 million and \$4.8 million, respectively, at December 31, 2010.

Securities with an amortized cost of \$130.8 million and \$131.6 million at June 30, 2011 and December 31, 2010, respectively, were pledged to secure public deposits and for other purposes.

The Company's subsidiary, Capital City Bank, as a member of the Federal Home Loan Bank ("FHLB") of Atlanta, is required to own capital stock in the FHLB of Atlanta based generally upon the balances of residential and commercial real estate loans, and FHLB advances. FHLB stock of \$7.0 million, which is included in other securities, is pledged to secure FHLB advances. No ready market exists for this stock, and it has no quoted market value. However, redemption of this stock has historically been at par value.

**Maturity Distribution.** As of June 30, 2011, the Company's investment securities had the following maturity distribution based on contractual maturities:

| (Dollars in Thousands)           | Amortized Cost |         | Market Value |         |
|----------------------------------|----------------|---------|--------------|---------|
| Due in one year or less          | \$             | 107,175 | \$           | 107,682 |
| Due after one through five years |                | 169,954 |              | 172,110 |
| Due after five through 10 years  |                | 10,797  |              | 10,926  |
| Due after 10 years               |                | 1,752   |              | 1,745   |
| No Maturity                      |                | 12,450  |              | 11,850  |
| Total Investment Securities      | \$             | 302,128 | \$           | 304,313 |

Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

**Other Than Temporarily Impaired Securities.** The following table summarizes the investment securities with unrealized losses at June 30, 2011 aggregated by major security type and length of time in a continuous unrealized loss position:

| (Dollars in Thousands)                       | Less Than<br>12 Months |                      | June 30, 2011<br>Greater Than<br>12 Months |                      | Total           |                      |
|--|------------------------|----------------------|--|----------------------|-----------------|----------------------|
|  | Market<br>Value        | Unrealized<br>Losses | Market<br>Value                            | Unrealized<br>Losses | Market<br>Value | Unrealized<br>Losses |
| U.S. Treasury                                | \$ 3,481               | \$ 3                 | \$ -                                       | \$ -                 | \$ 3,481        | \$ 3                 |
| U.S. Government Agencies<br>and Corporations | 10,367                 | 4                    | -  | -                    | 10,367          | 4                    |
| States and Political<br>Subdivisions         | 3,716                  | 14                   | -  | -                    | 3,716           | 14                   |
| Mortgage-Backed Securities                   | 7,011                  | 59                   | -  | -                    | 7,011           | 59                   |
| Other Securities                             | -                      | -                    | -  | 600                  | -               | 600                  |
| Total Investment Securities                  | \$ 24,575              | \$ 80                | \$ -                                       | \$ 600               | \$ 24,575       | \$ 680               |

Management evaluates securities for other than temporary impairment at least quarterly, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to the nature of the securities, the underlying collateral, the financial condition of the issuer, the extent and duration of the loss, our intent related to the individual securities, and the likelihood that we will have to sell the securities prior to the expected recovery. In analyzing an issuer's financial condition, management considers whether the securities are issued by the federal government or its agencies, whether downgrades by rating agencies have occurred, regulatory issues, and analysts' reports.



At June 30, 2011, the Company had securities of \$302.1 million with net pre-tax unrealized gains of \$2.2 million on these securities, of which \$25.0 million have unrealized losses totaling \$0.1 million and have been in a loss position for less than 12 months. These securities are primarily in a loss position because they were acquired when the general level of interest rates was lower than that on June 30, 2011. The Company believes that the losses in these securities are temporary in nature and that the full principal will be collected as anticipated. Because the declines in the market value of these investments are attributable to changes in interest rates and not credit quality and because the Company has the ability and intent to hold these investments until there is a recovery in fair value, which may be at maturity, the Company does not consider these investments to be other-than-temporarily impaired at June 30, 2011. One preferred bank stock issue for \$0.6 million has been in a loss position for greater than 12 months. The Company continues to closely monitor the fair value of this security as the subject bank continues to experience negative operating trends.

## NOTE 3 - LOANS

The composition of the Company's loan portfolio was as follows:

| (Dollars in Thousands)                 | June 30,<br>2011 | December<br>31, 2010 |
|--|------------------|----------------------|
| Commercial, Financial and Agricultural | \$ 149,830       | \$ 157,394           |
| Real Estate-Construction               | 30,867           | 43,239               |
| Real Estate-Commercial                 | 660,058          | 671,702              |
| Real Estate-Residential(1)             | 395,199          | 424,229              |
| Real Estate-Home Equity                | 248,228          | 251,565              |
| Real Estate-Loans Held-for-Sale        | 5,914            | 6,312                |
| Consumer                               | 197,506          | 204,230              |
| Loans, Net of Unearned Interest        | \$ 1,687,602     | \$ 1,758,671         |

(1) Includes loans in process with outstanding balances of \$6.3 million and \$10.0 million for June 30, 2011 and December 31, 2010, respectively.

Net deferred fees included in loans at June 30, 2011 and December 31, 2010 were \$1.7 million and \$1.8 million, respectively.

Past Due Loans. A loan is defined as a past due loan when one full payment is past due or a contractual maturity is over 30 days past due ("DPD").

The following table presents the aging of the recorded investment in past due loans as of June 30, 2011 and December 31, 2010 by class of loans:

| June 30, 2011<br>(Dollars in Thousands)     | 30-59<br>DPD | 60-89<br>DPD | 90 +<br>DPD | Total<br>Past Due | Total<br>Current | Total<br>Loans |
|---|--------------|--------------|-------------|-------------------|------------------|----------------|
| Commercial, Financial and<br>Agricultural   | \$ 754       | 208          | -           | 962               | 147,736          | \$ 149,830     |
| Real Estate - Construction                  | 140          | -            | -           | 140               | 29,571           | 30,867         |
| Real Estate - Commercial<br>Mortgage        | 3,681        | 1,217        | -           | 4,898             | 627,931          | 660,058        |
| Real Estate - Residential                   | 4,695        | 2,398        | 271         | 7,364             | 360,256          | 395,126        |
| Real Estate - Home Equity                   | 1,519        | 431          | -           | 1,950             | 243,004          | 248,228        |
| Consumer                                    | 2,787        | 273          | -           | 3,060             | 196,772          | 203,493        |
| Total Past Due Loans                        | \$ 13,576    | 4,527        | 271         | 18,374            | 1,605,270        | \$ 1,687,602   |
| December 31, 2010<br>(Dollars in Thousands) | 30-59<br>DPD | 60-89<br>DPD | 90 +<br>DPD | Total<br>Past Due | Total<br>Current | Total<br>Loans |
| Commercial, Financial and<br>Agricultural   | \$ 645       | 193          | -           | 838               | 155,497          | \$ 157,394     |
| Real Estate - Construction                  | 314          | 129          | -           | 443               | 40,890           | 43,239         |
| Real Estate - Commercial<br>Mortgage        | 5,577        | 840          | -           | 6,417             | 638,411          | 671,702        |
| Real Estate - Residential                   | 7,171        | 3,958        | 120         | 11,249            | 389,103          | 430,541        |
| Real Estate - Home Equity                   | 1,444        | 698          | 39          | 2,182             | 244,579          | 251,565        |
| Consumer                                    | 2,867        | 356          | -           | 3,223             | 200,139          | 204,230        |

|                      |    |        |       |     |        |           |    |           |
|----------------------|----|--------|-------|-----|--------|-----------|----|-----------|
| Total Past Due Loans | \$ | 18,018 | 6,174 | 159 | 24,352 | 1,668,619 | \$ | 1,758,671 |
|----------------------|----|--------|-------|-----|--------|-----------|----|-----------|

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Nonaccrual Loans. Loans are generally placed on non-accrual status if principal or interest payments become 90 days past due and/or management deems the collectability of the principal and/or interest to be doubtful. Loans are returned to accrual status when the principal and interest amounts contractually due are brought current or when future payments are reasonably assured.

The following table presents the recorded investment in nonaccrual loans and loans past due over 90 days and still on accrual by class of loans as of June 30, 2011 and December 31, 2010:

| (Dollars in Thousands)                 | June 30, 2011 |          | December 31, 2010 |         |
|--|---------------|----------|-------------------|---------|
|  | Nonaccrual    | 90 + DPD | Nonaccrual        | 90+ DPD |
| Commercial, Financial and Agricultural | \$ 1,133      | \$-      | \$ 1,059          | \$-     |
| Real Estate - Construction             | 1,156         | -        | 1,907             | -       |
| Real Estate - Commercial Mortgage      | 27,229        | -        | 26,874            | -       |
| Real Estate - Residential              | 27,505        | 271      | 30,189            | 120     |
| Real Estate - Home Equity              | 3,275         | -        | 4,803             | 39      |
| Consumer                               | 778           | -        | 868               | -       |
| Total Nonaccrual Loans                 | \$61,076      | \$271    | \$65,700          | \$ 159  |

Credit Quality Indicators. As part of the ongoing monitoring of the Company's loan portfolio quality, management categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment performance, credit documentation, and current economic/market trends, among other factors. Risk ratings are assigned to each loan and revised as needed through established monitoring procedures for individual loan relationships over a predetermined amount and review of smaller balance homogenous loan pools. The Company uses the following definitions for the categorizing and managing its problem loans.

Special Mention – Loans in this category are presently protected from loss, but weaknesses are apparent which, if not corrected, could cause future problems. Adverse economic or market conditions may negatively impact the borrower's ability to repay. Loans in this category may not meet required underwriting criteria and have no mitigating factors. More than the ordinary amount of attention is warranted for these loans.

Substandard – Loans in this category exhibit well-defined weaknesses that would typically bring normal repayment into jeopardy. These loans are no longer adequately protected due to well-defined weaknesses that affect the repayment capacity of the borrower. The possibility of loss is much more evident and above average supervision is required for these loans.

Nonaccrual – Loans in this category are on nonaccrual status due to the borrower's inability to meet the repayment terms and where future capacity to repay is remote.

The following table presents the risk category of loans by segment as of June 30, 2011 and December 31, 2010:

| June 30, 2011<br>(Dollars in Thousands) | Commercial,<br>Financial,<br>Agriculture | Real Estate | Consumer | Total     |
|---|--|-------------|----------|-----------|
| Special Mention                         | \$ 9,165                                 | \$94,141    | \$116    | \$103,422 |
| Substandard                             | 8,627                                    | 152,207     | 623      | 161,457   |
| Nonaccrual                              | 1,133                                    | 59,165      | 778      | 61,076    |

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|   |  |             |          |            |
|---|--|-------------|----------|------------|
| Total Loans                                 | \$ 18,925                                | \$ 305,513  | \$ 1,517 | \$ 325,955 |
| December 31, 2010<br>(Dollars in Thousands) | Commercial,<br>Financial,<br>Agriculture | Real Estate | Consumer | Total      |
| Special Mention                             | \$ 20,539                                | \$ 100,008  | \$ 102   | \$ 120,649 |
| Substandard                                 | 10,599                                   | 165,143     | 719      | 176,461    |
| Nonaccrual                                  | 1,060                                    | 63,773      | 867      | 65,700     |
| Total Loans                                 | \$ 32,198                                | \$ 328,924  | \$ 1,688 | \$ 362,810 |

## NOTE 4 - ALLOWANCE FOR LOAN LOSSES

An analysis of the changes in the allowance for loan losses for the three month periods ended June 30 was as follows:

| (Dollars in Thousands)                     | 2011      | 2010      |
|--|-----------|-----------|
| Balance, Beginning of Year                 | \$ 35,436 | \$ 43,999 |
| Provision for Loan Losses                  | 7,678     | 14,373    |
| Recoveries on Loans Previously Charged-Off | 1,226     | 2,129     |
| Loans Charged-Off                          | (13,260)  | (22,059)  |
| Balance, End of Period                     | \$ 31,080 | \$ 38,442 |

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio class based on impairment method as of June 30, 2011 and December 31, 2010:

| June 30, 2011<br>(Dollars in<br>Thousands)           | Commercial,<br>Financial,<br>Agricultural | Real<br>Estate<br>Construction | Real Estate<br>Commercial<br>Mortgage | Real Estate<br>Residential | Real Estate<br>Home<br>Equity | Consumer | Unallocated | Total     |
|--|---|--------------------------------|---------------------------------------|----------------------------|-------------------------------|----------|-------------|-----------|
| Allowance<br>Allocated to:                           |   |                                |                                       |                            |                               |          |             |           |
| Loans<br>Individually<br>Evaluated for<br>Impairment | 591                                       |                                | 3,582                                 |                            | 506                           |          |             |           |
|  | \$  | 487                            |                                       | 5,800                      |                               | 41       | -           | \$11,007  |
| Loans<br>Collectively<br>Evaluated for<br>Impairment | 1,193                                     |                                | 4,979                                 |                            | 1,742                         |          |             |           |
|  |   | 1,258                          |                                       | 8,147                      |                               | 1,754    | 1,000       | 20,073    |
| Total  | \$ 1,784                                  | 1,745                          | 8,561                                 | 13,947                     | 2,248                         | 1,795    | 1,000       | \$ 31,080 |

|   |            |        |         |         |         |         |   |              |
|---|------------|--------|---------|---------|---------|---------|---|--------------|
| Total Loans:                                |            |        |         |         |         |         |   |              |
| Individually<br>Evaluated for<br>Impairment | 1,730      |        | 42,531  |         | 2,351   |         |   |              |
|   | \$         | 1,311  |         | 29,829  |         | 79      | - | \$ 77,831    |
| Collectively<br>Evaluated for<br>Impairment | 148,100    |        | 617,526 |         | 245,878 |         |   |              |
|   |            | 29,556 |         | 365,297 |         | 203,414 | - | 1,609,771    |
| Total                                       | \$ 149,830 | 30,867 | 660,057 | 395,126 | 248,229 | 203,493 | - | \$ 1,687,602 |

| December 31,<br>2010<br>(Dollars in<br>Thousands) | Commercial,<br>Financial,<br>Agricultural | Real Estate<br>Construction | Real Estate<br>Commercial<br>Mortgage | Real Estate<br>Residential | Real Estate<br>Home<br>Equity | Consumer | Unallocated | Total  |
|---|---|-----------------------------|---------------------------------------|----------------------------|-------------------------------|----------|-------------|--------|
| Allowance<br>Allocated to:                        |   |                             |                                       |                            |                               |          |             |        |
| Loans<br>Individually<br>Evaluated                | \$ 252                                    | 413                         | \$ 4,640                              | 7,965                      | \$ 1,389                      | \$ 71    | -\$         | 14,730 |

|  |          |       |       |        |       |       |       |           |
|--|----------|-------|-------|--------|-------|-------|-------|-----------|
| for<br>Impairment<br>Loans<br>Collectively Evaluated | 292      | 1,647 | 4,005 | 9,081  | 1,133 | 2,541 | 1,007 | 20,706    |
| for<br>Impairment<br>Total                           | \$ 1,544 | 2,060 | 8,645 | 17,046 | 2,522 | 2,612 | 1,007 | \$ 35,436 |

|   |            |        |           |         |          |         |   |              |
|---|------------|--------|-----------|---------|----------|---------|---|--------------|
| Total Loans:<br>Individually<br>Evaluated for<br>Impairment | \$ 1,685   | 2,533  | \$ 42,369 | 37,779  | \$ 3,278 | \$ 144  | - | \$ 87,788    |
| Collectively<br>Evaluated for<br>Impairment                 | \$ 155,709 | 40,706 | 629,333   | 392,762 | 248,287  | 204,086 | - | 1,670,883    |
| Total   | \$ 157,394 | 43,239 | 671,702   | 430,541 | 251,565  | 204,230 | - | \$ 1,758,671 |

Impaired Loans. Loans are deemed to be impaired when, based on current information and events, it is probable that the Company will not be able to collect all amounts due (principal and interest payments), according to the contractual terms of the loan agreement. Loans, for which the terms have been modified, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings and classified as impaired. Interest income recognized on impaired loans was approximately \$1.2 million for the six month periods ended June 30, 2011 and June 30, 2010, respectively.

The following table presents loans individually evaluated for impairment by class of loans as of June 30, 2011 and December 31, 2010:

| (Dollars in Thousands)                 | Unpaid<br>Principal<br>Balance | Recorded<br>Investment<br>With No<br>Allowance | Recorded<br>Investment<br>With<br>Allowance | Related<br>Allowance | Average<br>Recorded<br>Investment |
|--|--------------------------------|--|---|----------------------|-----------------------------------|
| June 30, 2011:                         |                                |  |   |                      |                                   |
| Commercial, Financial and Agricultural | \$1,730                        | \$273  | \$1,458                                     | \$591                | \$1,563                           |
| Real Estate - Construction             | 1,311                          | 10,557   | 1,311                                       | 487                  | 1,950                             |
| Real Estate - Commercial Mortgage      | 42,531                         | 4,746  | 31,974                                      | 3,582                | 46,145                            |
| Real Estate - Residential              | 29,829                         | 522  | 25,083                                      | 5,800                | 30,782                            |
| Real Estate - Home Equity              | 2,351                          | 4  | 1,829                                       | 506                  | 2,844                             |
| Consumer                               | 79                             | -  | 74  | 41                   | 108                               |
| Total                                  | \$77,831                       | \$16,102                                       | \$61,729                                    | \$11,007             | \$83,392                          |
| December 31, 2010:                     |                                |  |   |                      |                                   |
| Commercial, Financial and Agricultural | \$1,684                        | \$389  | \$1,295                                     | \$252                | \$2,768                           |
| Real Estate - Construction             | 2,533                          | -  | 2,533                                       | 413                  | 5,801                             |
| Real Estate - Commercial Mortgage      | 42,370                         | 9,030  | 33,340                                      | 4,640                | 48,820                            |
| Real Estate - Residential              | 37,780                         | 3,295  | 34,485                                      | 7,965                | 41,958                            |
| Real Estate - Home Equity              | 3,278                          | 375  | 2,903                                       | 1,389                | 3,087                             |
| Consumer                               | 143                            | -  | 143   | 71                   | 172                               |
| Total                                  | \$87,788                       | \$13,089                                       | \$74,699                                    | \$14,730             | \$102,606                         |

#### NOTE 5 - INTANGIBLE ASSETS

The Company had net intangible assets of \$85.7 million and \$86.2 million at June 30, 2011 and December 31, 2010, respectively. Intangible assets were as follows:

| (Dollars in Thousands)           | June 30, 2011   |                             | December 31, 2010 |                             |
|----------------------------------|-----------------|-----------------------------|-------------------|-----------------------------|
|                                  | Gross<br>Amount | Accumulated<br>Amortization | Gross<br>Amount   | Accumulated<br>Amortization |
| Core Deposit Intangibles         | \$ 47,176       | \$ 46,798                   | \$ 47,176         | \$ 46,434                   |
| Goodwill                         | 84,811          | -                           | 84,811            | -                           |
| Customer Relationship Intangible | 1,867           | 1,357                       | 1,867             | 1,261                       |
| Total Intangible Assets          | \$ 133,854      | \$ 48,155                   | \$ 133,854        | \$ 47,695                   |



Net Core Deposit Intangibles: As of June 30, 2011 and December 31, 2010, the Company had net core deposit intangibles of \$0.4 million and \$0.7 million, respectively. Amortization expense for the first six months of 2011 and 2010 was approximately \$0.4 million and \$1.4 million, respectively. Estimated annual amortization expense for 2011 is \$0.5 million. All of our core deposit intangibles will be fully amortized in January 2013.

Goodwill: As of June 30, 2011 and December 31, 2010, the Company had goodwill, net of accumulated amortization, of \$84.8 million.

Goodwill is tested for impairment on an annual basis, or more often if impairment indicators exist. A goodwill impairment test consists of two steps. Step One compares the estimated fair value of the reporting unit to its carrying amount. If the carrying amount exceeds the estimated fair value, Step Two is performed by comparing the fair value of the reporting unit's implied goodwill to the carrying value of goodwill. If the carrying value of the reporting unit's goodwill exceeds the estimated fair value, an impairment charge is recorded equal to the excess.

As of June 30, 2011, the book value of the Company's equity exceeded its market capitalization, and as such the Company performed goodwill impairment testing. The Step One test indicated that the carrying amount (including goodwill) of the Company's reporting unit exceeded its estimated fair value. The Step Two test indicated the estimated fair value of our reporting unit's implied goodwill exceeded its carrying amount. Based on the results of the Step Two analysis, the Company concluded that goodwill was not impaired as of June 30, 2011. The Company will continue to test goodwill as defined by ASC Topic 350.

Other: As of June 30, 2011 and December 31, 2010, the Company had a customer relationship intangible asset, net of accumulated amortization, of \$0.5 million and \$0.6 million, respectively. This intangible asset was recorded as a result of the March 2004 acquisition of trust customer relationships. Amortization expense for the first six months of 2011 and 2010 was approximately \$96,000. Estimated annual amortization expense is approximately \$191,000 based on use of a 10-year useful life.

#### NOTE 6 - DEPOSITS

The composition of the Company's interest bearing deposits at June 30, 2011 and December 31, 2009 was as follows:

| (Dollars in Thousands)                 | June 30,<br>2011    | December<br>31, 2010 |
|--|---------------------|----------------------|
| NOW Accounts                           | \$ 764,480          | \$ 770,149           |
| Money Market Accounts                  | 283,230             | 275,416              |
| Savings Deposits                       | 153,403             | 139,888              |
| Other Time Deposits                    | 331,085             | 372,266              |
| <b>Total Interest Bearing Deposits</b> | <b>\$ 1,532,198</b> | <b>\$ 1,557,719</b>  |

#### NOTE 7 - STOCK-BASED COMPENSATION

The Company recognizes the cost of stock-based associate stock compensation in accordance with ASC-718-20-05-1 and ASC 718-50-05-01, (formerly SFAS No. 123R), "Share-Based Payment" (Revised) under the fair value method.

As of June 30, 2011, the Company had three stock-based compensation plans, consisting of the 2011 Associate Stock Incentive Plan ("ASIP"), the 2011 Associate Stock Purchase Plan ("ASPP"), and the 2011 Director Stock Purchase Plan ("DSPP"). These plans are new plans replacing substantially similar plans approved by the shareowners in 2004. Total compensation expense associated with these plans for the six months ended June 30, 2011 and 2010 was \$448,000 and \$184,000, respectively.

**ASIP.** The Company's ASIP allows the Company's Board of Directors to award key associates various forms of equity-based incentive compensation. Under the ASIP, all participants in this plan are eligible to earn an equity award, in the form of performance shares. The Company, under the terms and conditions of the ASIP, created the 2011 Incentive Plan ("2011 Plan"), which has an award tied to an internally established earnings goal. The grant-date fair value of the shares eligible to be awarded in 2011 is approximately \$895,000. A total of 51,952 shares are eligible for issuance. For the first six months of 2011 and 2010, the Company recognized approximately \$319,000 and \$115,000 in expense related to the ASIP.

**Executive Stock Option Agreement.** Prior to 2007, the Company maintained a stock option program for a key executive officer (William G. Smith, Jr. - Chairman, President and CEO, CCBG). The status of the options granted under this arrangement is detailed in the table provided below. In 2007, the Company replaced its practice of entering into an annual stock option arrangement by establishing a Performance Share Unit Plan under the provisions of the ASIP that allows the executive to earn shares based on the compound annual growth rate in diluted earnings per share over a three-year period. For the first six months of 2011, the Company recognized \$72,000 in expense related this plan. No expense was recognized under this plan for the first six months of 2010.

A summary of the status of the Company's options as of June 30, 2011 is presented below:

| Options | Shares | Weighted-Average<br>Exercise Price | Weighted-Average<br>Remaining | Aggregate<br>Intrinsic |
|---------|--------|------------------------------------|-------------------------------|------------------------|
|---------|--------|------------------------------------|-------------------------------|------------------------|

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|                                |        |          | Term | Value |
|--------------------------------|--------|----------|------|-------|
| Outstanding at January 1, 2011 | 60,384 | \$ 32.79 | 3.9  | \$-   |
| Granted                        | -      | -        | -    | -     |
| Exercised                      | -      | -        | -    | -     |
| Forfeited or expired           | -      | -        | -    | -     |
| Outstanding at June 30, 2011   | 60,384 | \$ 32.79 | 3.4  | \$-   |
| Exercisable at June 30, 2011   | 60,384 | \$ 32.79 | 3.4  | \$-   |

Compensation expense associated with the aforementioned option shares was fully recognized as of December 31, 2007.

DSPP. The Company's DSPP allows the directors to purchase the Company's common stock at a price equal to 90% of the closing price on the date of purchase. Stock purchases under the DSPP are limited to the amount of the director's annual cash compensation. For the first six months 2011 and 2010, the Company recognized approximately \$15,000 and \$14,000 in expense related to this plan or its predecessor plan, the 2005 Director Stock Purchase Plan.

ASPP. Under the Company's ASPP, substantially all associates may purchase the Company's common stock through payroll deductions at a price equal to 90% of the lower of the fair market value at the beginning or end of each six-month offering period. Stock purchases under the ASPP are limited to 10% of an associate's eligible compensation, up to a maximum of \$25,000 (fair market value on each enrollment date) in any plan year. Shares are issued at the beginning of the quarter following each six-month offering period. For the first six months of 2011, the Company recognized approximately \$42,000 in expense related to the ASPP plan or its predecessor plan, the 2005 Associate Stock Purchase Plan compared to approximately \$56,000 in expense for the same period in 2010.

#### NOTE 8 - EMPLOYEE BENEFIT PLANS

The Company has a defined benefit pension plan covering substantially all full-time and eligible part-time associates and a Supplemental Executive Retirement Plan ("SERP") covering its executive officers.

The components of the net periodic benefit costs for the Company's qualified benefit pension plan were as follows:

| (Dollars in Thousands)             | Three Months Ended<br>June 30, |          | Six Months Ended June<br>30, |          |
|------------------------------------|--------------------------------|----------|------------------------------|----------|
|                                    | 2011                           | 2010     | 2011                         | 2010     |
| Discount Rate                      | 5.55%                          | 5.75%    | 5.55%                        | 5.75%    |
| Long-Term Rate of Return on Assets | 8.00%                          | 8.00%    | 8.00%                        | 8.00%    |
| Service Cost                       | \$ 1,550                       | \$ 1,525 | \$ 3,100                     | \$ 3,050 |
| Interest Cost                      | 1,325                          | 1,175    | 2,650                        | 2,350    |
| Expected Return on Plan Assets     | (1,650)                        | (1,525)  | (3,300)                      | (3,050)  |
| Prior Service Cost Amortization    | 125                            | 125      | 250                          | 250      |
| Net Loss Amortization              | 550                            | 525      | 1,100                        | 1,050    |
| Net Periodic Benefit Cost          | \$ 1,900                       | \$ 1,825 | \$ 3,800                     | \$ 3,650 |

The components of the net periodic benefit costs for the Company's SERP were as follows:

| (Dollars in Thousands)          | Three Months Ended<br>June 30, |       | Six Months Ended June<br>30, |       |
|---------------------------------|--------------------------------|-------|------------------------------|-------|
|                                 | 2011                           | 2010  | 2011                         | 2010  |
| Discount Rate                   | 5.55%                          | 5.75% | 5.55%                        | 5.75% |
| Service Cost                    | \$ -                           | \$ -  | \$ -                         | \$ -  |
| Interest Cost                   | 40                             | 42    | 80                           | 84    |
| Prior Service Cost Amortization | 45                             | 45    | 90                           | 90    |
| Net Loss Amortization           | (98)                           | (85)  | (196)                        | (170) |
| Net Periodic Benefit Cost       | \$ (13)                        | \$ 2  | \$ (26)                      | \$ 4  |

NOTE 9 - COMMITMENTS AND CONTINGENCIES

Lending Commitments. The Company is a party to financial instruments with off-balance sheet risks in the normal course of business to meet the financing needs of its clients. These financial instruments consist of commitments to extend credit and standby letters of credit.

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The Company's maximum exposure to credit loss under standby letters of credit and commitments to extend credit is represented by the contractual amount of those instruments. The Company uses the same credit policies in establishing commitments and issuing letters of credit as it does for on-balance sheet instruments. As of June 30, 2011, the amounts associated with the Company's off-balance sheet obligations were as follows:

| (Dollars in Millions)           | Amount |
|---------------------------------|--------|
| Commitments to Extend Credit(1) | \$ 308 |
| Standby Letters of Credit       | \$ 11  |

(1) Commitments include unfunded loans, revolving lines of credit, and other unused commitments.

Commitments to extend credit are agreements to lend to clients so long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

Contingencies. The Company is a party to lawsuits and claims arising out of the normal course of business. In management's opinion, there are no known pending claims or litigation, the outcome of which would, individually or in the aggregate, have a material effect on the consolidated results of operations, financial position, or cash flows of the Company.

Indemnification Obligation. The Company is a member of the Visa U.S.A. network. Visa U.S.A believes that its member banks are required to indemnify it for potential future settlement of certain litigation (the "Covered Litigation"). In 2008, the Company, as a member of the Visa U.S.A. network, obtained Class B shares of Visa, Inc. upon its initial public offering. Since its initial public offering, Visa, Inc. has funded a litigation reserve for the Covered Litigation resulting in a reduction in the Class B shares held by the Company. During the first quarter of 2011, the Company sold its remaining Class B shares resulting in a \$3.2 million pre-tax gain. Associated with this sale, the Company entered into a swap contract with the purchaser of the shares that requires a payment to the counterparty in the event that Visa, Inc. makes subsequent revisions to the conversion ratio for its Class B shares. Further information on the swap contract is contained within Note 10 below.

#### NOTE 10 – FAIR VALUE MEASUREMENTS

The fair value of an asset or liability is the price that would be received to sell that asset or paid to transfer that liability in an orderly transaction occurring in the principal market (or most advantageous market in the absence of a principal market) for such asset or liability. In estimating fair value, the Company utilizes valuation techniques that are consistent with the market approach, the income approach and/or the cost approach. Such valuation techniques are consistently applied. Inputs to valuation techniques include the assumptions that market participants would use in pricing an asset or liability. ASC Topic 820 establishes a fair value hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

Level 1 Inputs - Unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.

Level 2 Inputs - Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These might include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (such as interest rates, volatilities, prepayment speeds, credit risks, etc.) or inputs

that are derived principally from or corroborated by market data by correlation or other means.

Level 3 Inputs - Unobservable inputs for determining the fair values of assets or liabilities that reflect an entity's own assumptions about the assumptions that market participants would use in pricing the assets or liabilities.

In general, fair value is based upon quoted market prices, where available. If such quoted market prices are not available, fair value is based upon models that primarily use, as inputs, observable market-based parameters. Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. These adjustments may include amounts to reflect counterparty credit quality, the Company's creditworthiness, among other things, as well as unobservable parameters. Any such valuation adjustments are applied consistently over time. The Company's valuation methodologies may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. While management believes the Company's valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date. A more detailed description of the valuation methodologies used for assets and liabilities measured at fair value is set forth in the Company's 2010 Form 10-K.

Financial Assets and Financial Liabilities. The following table summarizes financial assets and financial liabilities measured at fair value on a recurring basis as of June 30, 2011 segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

| (Dollars in Thousands)                 | Level 1<br>Inputs | Level 2<br>Inputs | Level 3<br>Inputs | Total Fair<br>Value |
|--|-------------------|-------------------|-------------------|---------------------|
| June 30, 2011                          |                   |                   |                   |                     |
| <b>ASSETS:</b>                         |                   |                   |                   |                     |
| Securities available for sale:         |                   |                   |                   |                     |
| US Treasury                            | \$ 170,207        | \$ -              | \$ -              | \$ 170,207          |
| States and Political Subdivisions      | 1,481             | 55,337            | -                 | 56,818              |
| Residential Mortgage-Backed Securities | -                 | 65,438            | -                 | 65,438              |
| Other Securities                       | -                 | 11,850            | -                 | 11,850              |
| <b>LIABILITIES:</b>                    |                   |                   |                   |                     |
| Fair Value Swap                        | -                 | -                 | 445               | 445                 |

Fair Value Swap. During the first quarter of 2011, the Company entered into a stand-alone derivative contract with the purchaser of its Visa Class B shares. The valuation represents an internally developed estimate of the exposure based upon probability-weighted potential Visa litigation losses and related carrying cost obligations required under the contract.

Non-Financial Assets and Non-Financial Liabilities. Certain non-financial assets measured at fair value on a nonrecurring basis are detailed below; that is, the instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment).

Impaired Loans. On a non-recurring basis, certain impaired loans are reported at the fair value of the underlying collateral if repayment is expected solely from the liquidation of collateral. Collateral values are estimated using Level 2 inputs based on customized discounting criteria. Impaired loans had a carrying value of \$77.8 million, with a valuation allowance of \$11.0 million.

Loans Held for Sale. Loans held for sale were \$5.9 million as of June 30, 2011. These loans are carried at the lower of cost or fair value and are adjusted to fair value on a non-recurring basis. Fair value is based on observable markets rates for comparable loan products which is considered a Level 2 fair value measurement.

Other Real Estate Owned. During the first six months of 2011, certain foreclosed assets, upon initial recognition, were measured and reported at fair value through a charge-off to the allowance for loan losses based on the fair value of the foreclosed asset. The fair value of the foreclosed asset, upon initial recognition, is estimated using Level 2 inputs based on observable market data. Foreclosed assets measured at fair value upon initial recognition totaled \$22.9 million during the six months ended June 30, 2011. In addition, the Company recognized subsequent losses totaling \$2.1 million for foreclosed assets that were re-valued during the six months ended June 30, 2011. The carrying value of foreclosed assets was \$61.0 million at June 30, 2011.

FASB ASC Topic 825 requires disclosure of the fair value of financial assets and financial liabilities, including those financial assets and financial liabilities that are not measured and reported at fair value on a recurring or non-recurring basis. A detailed description of the valuation methodologies used in estimating the fair value of financial instruments is set forth in the Company's 2010 Form 10-K.





The Company's financial instruments that have estimated fair values are presented below:

| (Dollars in Thousands)                  | June 30, 2011       |                      | December 31, 2010   |                      |
|---|---------------------|----------------------|---------------------|----------------------|
|   | Carrying Value      | Estimated Fair Value | Carrying Value      | Estimated Fair Value |
| <b>Financial Assets:</b>                |                     |                      |                     |                      |
| Cash                                    | \$ 71,554           | \$ 71,554            | \$ 35,410           | \$ 35,410            |
| Short-Term Investments                  | 223,183             | 223,183              | 200,783             | 200,783              |
| Investment Securities                   | 304,313             | 304,313              | 309,731             | 309,731              |
| Loans, Net of Allowance for Loan Losses | 1,656,522           | 1,558,801            | 1,723,235           | 1,675,997            |
| <b>Total Financial Assets</b>           | <b>\$ 2,255,572</b> | <b>\$ 2,157,851</b>  | <b>\$ 2,269,159</b> | <b>\$ 2,221,921</b>  |
| <b>Financial Liabilities:</b>           |                     |                      |                     |                      |
| Deposits                                | \$ 2,101,011        | \$ 2,101,972         | \$ 2,103,976        | \$ 2,105,568         |
| Short-Term Borrowings                   | 65,237              | 62,744               | 92,928              | 89,287               |
| Subordinated Notes Payable              | 62,887              | 62,890               | 62,887              | 62,884               |
| Long-Term Borrowings                    | 49,196              | 52,106               | 50,101              | 52,302               |
| Derivative Instrument – Fair Value Swap | 445                 | 445                  | -                   | -                    |
| <b>Total Financial Liabilities</b>      | <b>\$ 2,278,776</b> | <b>\$ 2,280,157</b>  | <b>\$ 2,309,892</b> | <b>\$ 2,310,041</b>  |

All non-financial instruments are excluded from the above table. The disclosures also do not include certain intangible assets such as client relationships, deposit base intangibles and goodwill. Accordingly, the aggregate fair value amounts presented do not represent the underlying value of the Company.

#### NOTE 11 – NEW AUTHORITATIVE ACCOUNTING GUIDANCE

ASU No. 2010-20, "Receivables (Topic 310) - Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses." ASU 2010-20 requires entities to provide disclosures designed to facilitate financial statement users' evaluation of (i) the nature of credit risk inherent in the entity's portfolio of financing receivables, (ii) how that risk is analyzed and assessed in arriving at the allowance for credit losses and (iii) the changes and reasons for those changes in the allowance for credit losses. Disclosures must be disaggregated by portfolio segment, the level at which an entity develops and documents a systematic method for determining its allowance for credit losses, and class of financing receivable, which is generally a disaggregation of portfolio segment. The required disclosures include, among other things, a roll-forward of the allowance for credit losses as well as information about modified, impaired, non-accrual and past due loans and credit quality indicators. ASU 2010-20 became effective for the Company's financial statements as of December 31, 2010, as it relates to disclosures required as of the end of a reporting period. Disclosures that relate to activity during a reporting period became effective for the Company's financial statements beginning on January 1, 2011. ASU 2011-01, "Receivables (Topic 310) - Deferral of the Effective Date of Disclosures about Troubled Debt Restructurings in Update No. 2010-20," temporarily deferred the effective date for disclosures related to troubled debt restructurings to coincide with the effective date of the then proposed ASU 2011-02, "Receivables (Topic 310) - A Creditor's Determination of Whether a Restructuring Is a Troubled Debt Restructuring," which is further discussed below. Adoption of ASU 2010-20 is not expected have a significant impact on the Company's financial statements.

ASU No. 2010-28, "Intangibles - Goodwill and Other (Topic 350) - When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts." ASU 2010-28 modifies Step 1 of the goodwill impairment test for reporting units with zero or negative carrying amounts. For those reporting units, an entity is required to perform Step 2 of the goodwill impairment test if it is more likely than not that a goodwill

impairment exists. In determining whether it is more likely than not that a goodwill impairment exists, an entity should consider whether there are any adverse qualitative factors indicating that an impairment may exist such as if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. ASU 2010-28 became effective for the Company on January 1, 2011 and did not have a significant impact on the Company's financial statements.

ASU No. 2011-02, "Receivables (Topic 310) - A Creditor's Determination of Whether a Restructuring Is a Troubled Debt Restructuring." ASU 2011-02 clarifies which loan modifications constitute troubled debt restructurings and is intended to assist creditors in determining whether a modification of the terms of a receivable meets the criteria to be considered a troubled debt restructuring, both for purposes of recording an impairment loss and for disclosure of troubled debt restructurings. In evaluating whether a restructuring constitutes a troubled debt restructuring, a creditor must separately conclude, under the guidance clarified by ASU 2011-02, that both of the following exist: (a) the restructuring constitutes a concession; and (b) the debtor is experiencing financial difficulties. ASU 2011-02 will be effective for the Company on July 1, 2011, and applies retrospectively to restructurings occurring on or after January 1, 2011. Adoption of ASU 2011-02 is not expected have a significant impact on the Company's financial statements.

ASU No. 2011-03, "Transfers and Servicing (Topic 860) - Reconsideration of Effective Control for Repurchase Agreements." ASU 2011-03 is intended to improve financial reporting of repurchase agreements and other agreements that both entitle and obligate a transferor to repurchase or redeem financial assets before their maturity. ASU 2011-03 removes from the assessment of effective control (i) the criterion requiring the transferor to have the ability to repurchase or redeem the financial assets on substantially the agreed terms, even in the event of default by the transferee, and (ii) the collateral maintenance guidance related to that criterion. ASU 2011-03 will be effective for the Company on January 1, 2012 and is not expected to have a significant impact on the Company's financial statements.

ASU 2011-04, "Fair Value Measurement (Topic 820) - Amendments to Achieve Common Fair Value Measurements and Disclosure Requirements in U.S. GAAP and IFRSs." ASU 2011-04 amends Topic 820, "Fair Value Measurements and Disclosures," to converge the fair value measurement guidance in U.S. generally accepted accounting principles and International Financial Reporting Standards. ASU 2011-04 clarifies the application of existing fair value measurement requirements, changes certain principles in Topic 820 and requires additional fair value disclosures. ASU 2011-04 is effective for annual periods beginning after December 15, 2011, and is not expected to have a significant impact on the Company's financial statements.

ASU 2011-05, "Comprehensive Income (Topic 220) - Presentation of Comprehensive Income." ASU 2011-05 amends Topic 220, "Comprehensive Income," to require that all nonowner changes in stockholders' equity be presented in either a single continuous statement of comprehensive income or in two separate but consecutive statements. Additionally, ASU 2011-05 requires entities to present, on the face of the financial statements, reclassification adjustments for items that are reclassified from other comprehensive income to net income in the statement or statements where the components of net income and the components of other comprehensive income are presented. The option to present components of other comprehensive income as part of the statement of changes in stockholders' equity was eliminated. ASU 2011-05 is effective for annual periods beginning after December 15, 2011, and is not expected to have a significant impact on the Company's financial statements.

## QUARTERLY FINANCIAL DATA (UNAUDITED)

| (Dollars and<br>Shares in<br>Thousands)             | 2011      |           |           | 2010      |           |            |            |
|---|-----------|-----------|-----------|-----------|-----------|------------|------------|
|   | Second    | First(1)  | Fourth    | Third     | Second    | First      | Fourth     |
| Summary of Operations:                              |           |           |           |           |           |            |            |
| Interest Income                                     | \$ 25,467 | \$ 25,189 | \$ 26,831 | \$ 27,576 | \$ 27,934 | \$ 28,154  | \$ 29,756  |
| Interest Expense                                    | 2,028     | 2,203     | 2,473     | 2,792     | 3,565     | 4,132      | 4,464      |
| Net Interest Income                                 | 23,439    | 22,986    | 24,358    | 24,784    | 24,369    | 24,022     | 25,292     |
| Provision for Loan Losses                           | 3,545     | 4,133     | 3,783     | 5,668     | 3,633     | 10,740     | 10,834     |
| Net Interest Income After Provision for Loan Losses | 19,894    | 18,853    | 20,575    | 19,116    | 20,736    | 13,282     | 14,458     |
| Noninterest Income                                  | 14,448    | 16,334    | 14,735    | 13,449    | 14,674    | 13,967     | 14,411     |
| Noninterest Expense                                 | 31,167    | 33,331    | 33,540    | 32,363    | 34,629    | 33,384     | 35,313     |
| Income (Loss) Before Income Taxes                   | 3,175     | 1,856     | 1,770     | 202       | 781       | (6,135)    | (6,444)    |
| Income Tax (Benefit) Expense                        | 1,030     | 546       | (148)     | (199)     | 50        | (2,672)    | (3,037)    |
| Net Income (Loss)                                   | \$ 2,145  | \$ 1,310  | \$ 1,918  | \$ 401    | \$ 731    | \$ (3,463) | \$ (3,407) |
| Net Interest Income (FTE)                           | \$ 23,704 | \$ 23,257 | \$ 24,654 | \$ 25,116 | \$ 24,738 | \$ 24,473  | \$ 25,845  |
| Per Common Share:                                   |           |           |           |           |           |            |            |
| Net Income (Loss) Basic                             | \$ 0.12   | \$ 0.08   | \$ 0.12   | \$ 0.02   | \$ 0.04   | \$ (0.20)  | \$ (0.20)  |
| Net Income (Loss) Diluted                           | 0.12      | 0.08      | 0.12      | 0.02      | 0.04      | (0.20)     | (0.20)     |
| Dividends Declared                                  | 0.10      | 0.10      | 0.10      | 0.10      | 0.10      | 0.19       | 0.19       |
| Diluted Book Value                                  | 15.20     | 15.13     | 15.15     | 15.25     | 15.32     | 15.34      | 15.72      |
| Market Price:                                       |           |           |           |           |           |            |            |
| High  | 13.12     | 13.80     | 14.19     | 14.24     | 18.25     | 14.61      | 14.34      |
| Low   | 9.84      | 11.87     | 11.56     | 10.76     | 12.36     | 11.57      | 11.00      |
| Close   | 10.26     | 12.68     | 12.60     | 12.14     | 12.38     | 14.25      | 13.84      |

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Selected  
Average  
Balances:

|                                   |              |              |              |              |              |              |              |
|-----------------------------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Loans, Net                        | \$ 1,704,348 | \$ 1,730,330 | \$ 1,782,916 | \$ 1,807,483 | \$ 1,841,379 | \$ 1,886,367 | \$ 1,944,873 |
| Earning Assets                    | 2,258,931    | 2,278,602    | 2,218,049    | 2,273,198    | 2,329,365    | 2,358,288    | 2,237,561    |
| Total Assets                      | 2,618,287    | 2,643,017    | 2,576,793    | 2,626,758    | 2,678,488    | 2,698,419    | 2,575,250    |
| Deposits                          | 2,107,301    | 2,125,379    | 2,115,867    | 2,172,165    | 2,234,178    | 2,248,760    | 2,090,008    |
| Shareowners' Equity               | 262,371      | 261,603      | 262,622      | 263,742      | 263,873      | 268,555      | 268,556      |
| Common Equivalent Average Shares: |              |              |              |              |              |              |              |
| Basic                             | 17,127       | 17,122       | 17,095       | 17,087       | 17,063       | 17,057       | 17,034       |
| Diluted                           | 17,139       | 17,130       | 17,096       | 17,088       | 17,074       | 17,070       | 17,035       |

Performance  
Ratios:

|  |       |       |       |       |       |         |         |
|--|-------|-------|-------|-------|-------|---------|---------|
| Return on Average Assets                     | %     |       |       |       |       |         |         |
|  | 0.33  | 0.20% | 0.30% | 0.06% | 0.11% | (0.52)% | (0.52)% |
| Return on Average Equity                     | 3.28  | 2.03  | 2.90  | 0.60  | 1.11  | (5.23)  | (5.03)  |
| Net Interest Margin (FTE)                    | 4.21  | 4.14  | 4.41  | 4.38  | 4.26  | 4.21    | 4.59    |
| Noninterest Income as % of Operating Revenue | 38.13 | 41.54 | 37.69 | 35.17 | 37.58 | 36.77   | 36.30   |
| Efficiency Ratio                             | 81.41 | 83.30 | 83.75 | 82.08 | 86.06 | 85.00   | 85.21   |

Asset Quality:

|                                      |         |         |         |         |         |         |         |
|--------------------------------------|---------|---------|---------|---------|---------|---------|---------|
| Allowance for Loan Losses            | 31,080  | 33,873  | 35,436  | 37,720  | 38,442  | 41,199  | 43,999  |
| Allowance for Loan Losses to Loans   | %       |         |         |         |         |         |         |
|                                      | 1.84    | 1.98    | % 2.01  | % 2.10% | 2.11%   | 2.23%   | 2.30%   |
| Nonperforming Assets                 | 145,674 | 153,346 | 145,286 | 145,643 | 149,814 | 153,669 | 144,052 |
| Nonperforming Assets to Loans + ORE  | 8.33    | 8.66    | 8.00    | 7.86    | 8.01    | 8.10    | 7.38    |
| Nonperforming Assets to Total Assets | 5.60    | 5.76    | 5.54    | 5.65    | 5.65    | 5.66    | 5.32    |
| Allowance to Non-Performing Loans    | 36.71   | 34.57   | 40.57   | 39.94   | 37.80   | 38.42   | 40.77   |
| Net Charge-Offs to Average Loans     | 1.49    | 1.33    | 1.35    | 1.40    | 1.39    | 2.91    | 2.42    |

Capital Ratios:

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|                              |   |       |        |        |        |        |        |        |
|------------------------------|---|-------|--------|--------|--------|--------|--------|--------|
| Tier 1 Capital Ratio         | % | 13.83 | 13.46% | 13.24% | 12.93% | 12.78% | 12.81% | 12.76% |
| Total Capital Ratio          |   | 15.19 | 14.82  | 14.59  | 14.29  | 14.14  | 14.16  | 14.11  |
| Tangible Common Equity Ratio |   | 6.96  | 6.73   | 6.82   | 6.98   | 6.80   | 6.62   | 6.84   |
| Leverage Ratio               |   | 9.95  | 9.74   | 10.10  | 9.75   | 9.58   | 9.64   | 10.39  |

(1) Includes a \$2.6 million (net) pre-tax gain from sale of Visa shares – \$3.2 million gain less \$0.6 million related swap liability.

## Item 2.MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Management's discussion and analysis ("MD&A") provides supplemental information, which sets forth the major factors that have affected our financial condition and results of operations and should be read in conjunction with the Consolidated Financial Statements and related notes. The MD&A is divided into subsections entitled "Business Overview," "Financial Overview," "Results of Operations," "Financial Condition," "Market Risk and Interest Rate Sensitivity," "Liquidity and Capital Resources," "Off-Balance Sheet Arrangements," and "Critical Accounting Policies." The following information should provide a better understanding of the major factors and trends that affect our earnings performance and financial condition, and how our performance during 2011 compares with prior years. Throughout this section, Capital City Bank Group, Inc., and subsidiaries, collectively, are referred to as "CCBG," "Company," "we," "us," or "our."

In this MD&A, we present an operating efficiency ratio which is not calculated based on accounting principles generally accepted in the United States ("GAAP"), but that we believe provides important information regarding our results of operations. Our calculation of the operating efficiency ratio is computed by dividing noninterest expense less intangible amortization, by the sum of tax equivalent net interest income and noninterest income. Management uses this non-GAAP measure as part of its assessment of its performance in managing noninterest expenses. We believe that excluding intangible amortization and merger expenses in our calculations better reflect our periodic expenses and is more reflective of normalized operations.

Although we believe the above-mentioned non-GAAP financial measure enhances investors' understanding of our business and performance this non-GAAP financial measure should not be considered an alternative to GAAP. In addition, there are material limitations associated with the use of this non-GAAP financial measure such as the risks that readers of our financial statements may disagree as to the appropriateness of items included or excluded in this measure and that our measure may not be directly comparable to other companies that calculate this measure differently. Our management compensates for this limitation by providing a detailed reconciliation between GAAP information and the non-GAAP financial measure as detailed below.

Reconciliation of operating efficiency ratio to efficiency ratio:

|  | Three Months Ended |    |                   |    | Six Months Ended |    |                  |    |        |    |
|--|--------------------|----|-------------------|----|------------------|----|------------------|----|--------|----|
|  | June 30,<br>2011   |    | March 31,<br>2011 |    | June 30,<br>2010 |    | June 30,<br>2010 |    |        |    |
| Efficiency ratio                             | 81.69              | %  | 84.19             | %  | 87.86            | %  | 82.97            | %  | 87.36  | %  |
| Effect of intangible<br>amortization expense | (0.28)             | )% | (0.89)            | )% | (1.80)           | )% | (0.60)           | )% | (1.82) | )% |
| Operating efficiency ratio                   | 81.41              | %  | 83.30             | %  | 86.06            | %  | 82.37            | %  | 85.54  | %  |



The following discussion should be read in conjunction with the condensed consolidated financial statements and notes thereto included in this Quarterly Report on Form 10-Q.

#### CAUTION CONCERNING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q, including this MD&A section, contains "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements include, among others, statements about our beliefs, plans, objectives, goals, expectations, estimates and intentions that are subject to significant risks and uncertainties and are subject to change based on various factors, many of which are beyond our control. The words "may," "could," "should," "would," "believe," "anticipate," "estimate," "expect," "intend," "plan," "target," "goal," and similar expressions are intended to identify forward-looking statements.

All forward-looking statements, by their nature, are subject to risks and uncertainties. Our actual future results may differ materially from those set forth in our forward-looking statements. Please see the Introductory Note and Item 1A. Risk Factors of our 2010 Report on Form 10-K, as updated in our subsequent quarterly reports filed on Form 10-Q, and in our other filings made from time to time with the SEC after the date of this report.

However, other factors besides those listed in our Quarterly Report or in our Annual Report also could adversely affect our results, and you should not consider any such list of factors to be a complete set of all potential risks or uncertainties. Any forward-looking statements made by us or on our behalf speak only as of the date they are made. We do not undertake to update any forward-looking statement, except as required by applicable law.

#### BUSINESS OVERVIEW

##### Our Business

We are a bank holding company headquartered in Tallahassee, Florida, and we are the parent of our wholly-owned subsidiary, Capital City Bank (the "Bank" or "CCB"). The Bank offers a broad array of products and services through a total of 70 full-service offices located in Florida, Georgia, and Alabama. The Bank offers commercial and retail banking services, as well as trust and asset management, retail securities brokerage and data processing services.

Our profitability, like most financial institutions, is dependent to a large extent upon net interest income, which is the difference between the interest received on earning assets, such as loans and securities, and the interest paid on interest-bearing liabilities, principally deposits and borrowings. Results of operations are also affected by the provision for loan losses, operating expenses such as salaries and employee benefits, occupancy and other operating expenses including income taxes, and noninterest income such as service charges on deposit accounts, asset management and trust fees, retail securities brokerage fees, mortgage banking fees, bank card fees, and data processing fees.

Much of our lending operations are within the State of Florida, which had been particularly hard hit in the recent economic recession. Evidence of the economic downturn in Florida is particularly reflected in current unemployment statistics and realization of real estate property devaluation. According to the U.S. Department of Labor, the Florida unemployment rate (seasonally adjusted) at December 2010 increased to 12.0% from 11.8% at the end of 2009 and 7.6% at the end of 2008. While our Florida markets have generally realized an unemployment rate below the Florida rate, they have been adversely impacted as evidenced by layoffs and business closings, as well as wealth reduction due to depressed real estate markets. Real estate property valuations continue to be depressed during the economic downturn as evidenced by our higher level of problem assets and credit related costs. A second recession in Florida or continued slow recovery would likely exacerbate the adverse effects of these difficult market conditions on our clients, which may have a negative impact on our financial results.



## FINANCIAL OVERVIEW

A summary overview of our financial performance is provided below.

### Financial Performance Highlights –

- Net income for the second quarter of 2011 totaled \$2.1 million, or \$0.12 per diluted share, compared to net income of \$1.3 million, or \$0.08 per diluted share, for the first quarter of 2011 and net income of \$0.7 million, or \$0.04 per diluted share, for the second quarter of 2010. For the first six months of 2011, we realized net income of \$3.5 million, or \$0.20 per diluted share, compared to a net loss of \$2.7 million, or \$0.16 per diluted share, for the comparable period of 2010. Performance in 2011 reflects the sale of our Visa stock in the first quarter which resulted in a net pre-tax gain of \$2.6 million.
- Net income for the second quarter of 2011 reflects total credit related costs (loan loss provision and other real estate owned (“OREO”) costs) of \$6.6 million, compared to \$7.8 million for the first quarter of 2011 and \$7.7 million for the second quarter of 2010. Credit related costs were \$14.4 million for the first half of 2011 compared to \$21.3 million for the same period in 2010.
- Tax equivalent net interest income for the second quarter of 2011 was \$23.7 million compared to \$23.3 million for the first quarter of 2011 and \$24.7 million for the second quarter of 2010. For the first half of 2011, tax equivalent net interest income totaled \$47.0 million compared to \$49.2 million in 2010.
- Loan loss provision for the second quarter of 2011 was \$3.5 million compared to \$4.1 million for the first quarter of 2011 and \$3.6 million for the second quarter of 2010. A decline in impaired loans drove the reduction in the provision for both periods. For the first half of the 2011, the loan loss provision was \$7.7 million compared to \$14.4 million for the same period in 2010. A reduction in impaired loans as well as a decline in general reserves, primarily due to a lower level of internally classified loans and lower loss rates, drove the lower provision. As of June 30, 2011, the allowance for loan losses was 1.84% of total loans and provided coverage of 37% of nonperforming loans compared to 2.01% and 41%, respectively, at year-end 2010.
- Noninterest income for the second quarter of 2011 totaled \$14.4 million, a decrease of \$1.9 million from the first quarter of 2011 and \$0.2 million from the second quarter of 2010. The decrease from the first quarter of 2011 largely reflects the sale of our Visa stock in the first quarter. For the first six months of 2011, noninterest income totaled \$30.8 million, an increase of \$2.1 million over the same period in 2010 driven by the Visa gain, partially offset by deposit service charge fees and merchant fees.
- Noninterest expense for the second quarter of 2011 totaled \$31.2 million, a decrease of \$2.2 million from the first quarter of 2011 and \$3.5 million from the second quarter of 2010. The decline from the first quarter of 2011 quarter primarily reflects lower expense for compensation, OREO costs and, to a lesser extent, FDIC insurance premiums, intangible amortization and miscellaneous expense. For the first six months of 2011, noninterest expense totaled \$64.5 million, a \$3.5 million decline from the same period of 2010 primarily attributable to expense for FDIC insurance, intangible amortization, and interchange fees.
- Average earning assets were \$2.259 billion for the second quarter of 2011, an increase of \$40.9 million from the fourth quarter of 2010 driven by an increase in the overnight funds sold position and a higher investment portfolio, partially offset by a decline in the loan portfolio.
- As of June 30, 2011, we are well-capitalized with a risk based capital ratio of 15.19% and a tangible common equity ratio of 6.96% compared to 14.50% and 6.82%, respectively, at December 31, 2010.



## RESULTS OF OPERATIONS

## Net Income

Net income for the second quarter of 2011 totaled \$2.1 million, or \$0.12 per diluted share, compared to net income of \$1.3 million, or \$0.08 per diluted share, for the first quarter of 2011 and net income of \$0.7 million, or \$0.04 per diluted share, for the second quarter of 2010. For the first six months of 2011, we reported net income of \$3.5 million, or \$0.20 per diluted share, compared to a net loss of \$2.7 million, or \$0.16 per diluted share, for the same period in 2010.

The increase in earnings over the first quarter of 2011 was due to higher net interest income of \$0.4 million, lower loan loss provision of \$0.6 million, and a reduction in noninterest expense of \$2.2 million, partially offset by a decline in noninterest income of \$1.9 million and higher income tax expense of \$0.5 million. Compared to the second quarter of 2010, a \$3.5 million decline in noninterest expense partially offset by a \$1.2 million reduction in operating revenues and higher income tax expense of \$1.0 million drove the improvement in earnings.

The increase in earnings for the first six months of 2011 is attributable to a lower loan loss provision of \$6.7 million, reduction in noninterest expense of \$3.5 million, and higher noninterest income of \$2.1 million, partially offset by lower net interest income of \$2.0 million and higher income tax expense of \$4.1 million.

Performance in 2011 reflects the sale of our Visa Class B shares of stock during the first quarter which resulted in a \$3.2 million pre-tax gain included in noninterest income and a swap liability of \$0.6 million included in noninterest expense.

A condensed earnings summary of each major component of our financial performance is provided below:

| (Dollars in Thousands, except per share data)       | Three Months Ended |                |               | Six Months Ended |               |
|---|--------------------|----------------|---------------|------------------|---------------|
|   | June 30, 2011      | March 31, 2011 | June 30, 2010 | June 30, 2011    | June 30, 2010 |
| Interest Income                                     | \$ 25,467          | \$ 25,189      | \$ 27,934     | \$ 50,656        | \$ 56,088     |
| Taxable equivalent Adjustments                      | 265                | 271            | 369           | 536              | 820           |
| Total Interest Income (FTE)                         | 25,732             | 25,460         | 28,303        | 51,192           | 56,908        |
| Interest Expense                                    | 2,028              | 2,203          | 3,565         | 4,231            | 7,697         |
| Net Interest Income (FTE)                           | 23,704             | 23,257         | 24,738        | 46,961           | 49,211        |
| Provision for Loan Losses                           | 3,545              | 4,133          | 3,633         | 7,678            | 14,373        |
| Taxable Equivalent Adjustments                      | 265                | 271            | 369           | 536              | 820           |
| Net Interest Income After provision for Loan Losses | 19,894             | 18,853         | 20,736        | 38,747           | 34,018        |
| Noninterest Income                                  | 14,448             | 16,334         | 14,674        | 30,782           | 28,641        |
| Noninterest Expense                                 | 31,167             | 33,331         | 34,629        | 64,498           | 68,013        |
| Income (Loss) Before Income Taxes                   | 3,175              | 1,856          | 781           | 5,031            | (5,354)       |
| Income Tax Expense (Benefit)                        | 1,030              | 546            | 50            | 1,576            | (2,622)       |
| Net Income (Loss)                                   | \$ 2,145           | \$ 1,310       | \$ 731        | \$ 3,455         | \$ (2,732)    |
| Basic Net Income (Loss) Per Share                   | \$ 0.12            | \$ 0.08        | \$ 0.04       | \$ 0.20          | \$ (0.16)     |
| Diluted Net Income (Loss) Per Share                 | \$ 0.12            | \$ 0.08        | \$ 0.04       | \$ 0.20          | \$ (0.16)     |
| Return on Average Equity                            | 3.28%              | 2.03%          | 1.11%         | 2.66%            | (2.07)%       |
| Return on Average Assets                            | 0.33%              | 0.20%          | 0.11%         | 0.26%            | (0.20)%       |



## Net Interest Income

Net interest income represents our single largest source of earnings and is equal to interest income and fees generated by earning assets, less interest expense paid on interest bearing liabilities. This information is provided on a "taxable equivalent" basis to reflect the tax-exempt status of income earned on certain loans and investments, the majority of which are state and local government debt obligations. We provide an analysis of our net interest income including average yields and rates in Table I on page 37.

Tax equivalent net interest income for the second quarter of 2011 was \$23.7 million compared to \$23.3 million for the first quarter of 2010 and \$24.7 million for the second quarter of 2010. For the six months of 2011, tax equivalent net interest income totaled \$47.0 million compared to \$49.2 million in 2010.

The increase of \$0.4 million in tax equivalent net interest income compared to the first quarter of 2011 was due to lower cost of funds and one additional calendar day. Lower interest expense reflects a reduction in deposit rates primarily in certificates of deposit. Interest income on earning assets was higher as a result of the one additional calendar day. Additionally, net interest income was impacted by favorable interest income adjustments on nonaccrual loans (i.e. quarter over quarter improvement in the level of interest reversals), which offset lower interest income attributable to a reduction in loans outstanding and unfavorable asset re-pricing.

The decrease in tax equivalent net interest income of \$1.0 million and \$2.2 million, for the three and six month periods ended June 30, 2011, respectively, as compared to the same periods in 2010, resulted from a reduction in loans outstanding, lower earning assets yields reflecting unfavorable asset re-pricing and lower loan fees, partially offset by a reduction in interest expense and favorable interest income adjustments as noted above.

Interest expense for the second quarter of 2011 was \$2.0 million compared to \$2.2 million for the first quarter of 2011 and \$3.6 million for the second quarter in 2010. The lower cost of funds when compared to the first quarter of 2011 was a result of continued rate reductions to certificates of deposits. The lower costs of funds when compared to the second quarter of 2010 resulted from rate reductions on non-maturity deposits, certificates of deposit and subordinated notes. The rate reductions on deposits reflect management's decision not to compete with higher rate paying institutions and to continue our focus on core banking relationships. The lower rate on subordinated notes was due to one note changing to a variable rate from a fixed rate, which occurred in the second half of 2010.

The net interest margin in the second quarter of 2011 was 4.21%, an increase of 7 basis points over the linked quarter and a decline of 6 basis points from the second quarter of 2010. Year over year, for the six month period, the margin declined 7 basis points to 4.17%. The increase in the margin when compared to the first quarter of 2011 reflects a 3 basis point reduction in the cost of funds, and an improvement in the yield on earning assets of 4 basis points. The higher yield on earning assets was primarily attributable to an increase in the loan yield resulting from the favorable interest income adjustments mentioned above, while the lower cost of funds resulted from a reduction in the rates on certificates of deposit, which were significantly reduced in all markets. The 7 basis point decline in the margin for the six months of 2011 is attributable to the shift in our earning asset mix and unfavorable asset repricing, partially offset by a favorable variance in our average cost of funds.

## Provision for Loan Losses

The provision for loan losses for the second quarter of 2011 was \$3.5 million compared to \$4.1 million in the first quarter of 2011 and \$3.6 million for the second quarter of 2010. The reduction in the loan loss provision for both periods primarily reflects a reduction in level of impaired loans and required reserves. For the first six months of 2011, the loan loss provision totaled \$7.7 million compared to \$14.4 million for the same period in 2010. The reduction is attributable to lower impaired loan reserves as well as a decline in general reserves, primarily due to a

reduction in the level of internally classified loans and lower loss rates.

Net charge-offs for the second quarter of 2011 totaled \$6.3 million, or 1.49%, of average loans compared to \$5.7 million, or 1.33% for the first quarter of 2011 and \$6.4 million, or 1.39%, in the second quarter of 2010. For the first six months of 2011, net charge-offs totaled \$12.0 million, or 1.41%, of average loans compared to \$19.9 million, or 2.16%, for the same period of 2010. At quarter-end, the allowance for loan losses of \$31.1 million was 1.84% of outstanding loans (net of overdrafts) and provided coverage of 37% of nonperforming loans compared to 1.98% and 35%, respectively, at March 31, 2011, and 2.01% and 41%, respectively, at December 31, 2010.

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Charge-off activity for the respective periods is set forth below:

| (Dollars in Thousands, except per share data)  | Three Months Ended |                |               | Six Months Ended |               |
|--|--------------------|----------------|---------------|------------------|---------------|
|  | June 30, 2011      | March 31, 2011 | June 30, 2010 | June 30, 2011    | June 30, 2010 |
| <b>CHARGE-OFFS</b>   |                    |                |               |                  |               |
| Commercial, Financial and Agricultural   | \$ 301             | \$ 721         | \$ 405        | \$ 1,022         | \$ 1,247      |
| Real Estate - Construction   | 14                 | -              | 1,220         | 14               | 4,942         |
| Real Estate - Commercial Mortgage  | 2,808              | 430            | 920           | 3,238            | 5,551         |
| Real Estate - Residential  | 3,315              | 4,445          | 4,725         | 7,760            | 8,452         |
| Consumer   | 606                | 620            | 360           | 1,226            | 1,867         |
| Total Charge-offs  | 7,044              | 6,216          | 7,630         | 13,260           | 22,059        |
| <b>RECOVERIES</b>  |                    |                |               |                  |               |
| Commercial, Financial and Agricultural   | 43                 | 63             | 181           | 106              | 258           |
| Real Estate - Construction   | 5                  | 9              | 8             | 14               | 8             |
| Real Estate - Commercial Mortgage  | 115                | 12             | 43            | 127              | 200           |
| Real Estate - Residential  | 170                | 96             | 638           | 266              | 752           |
| Consumer   | 373                | 340            | 370           | 713              | 911           |
| Total Recoveries   | 706                | 520            | 1,240         | 1,226            | 2,129         |
| Net Charge-offs  | \$ 6,338           | \$ 5,696       | \$ 6,390      | \$ 12,034        | \$ 19,930     |
| Net Charge - Offs (Annualized) as a percent of Average Loans Outstanding, Net of Unearned Interest | 1.49%              | 1.33%          | 1.39%         | 1.41%            | 2.16%         |

#### Noninterest Income

Noninterest income for the second quarter of 2011 totaled \$14.4 million, a decrease of \$1.9 million, or 11.5%, from the first quarter of 2011 and \$0.2 million, or 1.5% from the second quarter of 2010. The unfavorable variance compared to the first quarter of 2011 quarter reflects a gain from the sale of our Visa stock during the first quarter of 2011, which resulted in a \$3.2 million pre-tax gain, as well as a \$0.2 million reduction in data processing fees. Favorable variances for deposit fees, retail brokerage fees, and miscellaneous income partially offset the aforementioned unfavorable variances. An increase in other income due to higher gains from the sale of OREO properties, which was partially offset by lower deposit service charge fees, drove the variance versus the second quarter of 2010. For the first six months of 2011, noninterest income totaled \$30.8 million, an increase of \$2.1 million over the same period of 2010. The increase was driven by the gain on the sale of our Visa stock and was partially offset by lower deposit service charge fees and merchant fees.

Noninterest income represented 38.1% of operating revenues for the second quarter of 2011 compared to 41.5% for the first quarter of 2011 and 37.6% for the second quarter of 2010. For the first six months of 2011, noninterest income represented 39.9% of operating revenues compared to 37.2% for the same period of 2010. The higher ratio for the first quarter of 2011 and first half of 2011 reflects the gain from the sale of our Visa stock.



The table below reflects the major components of noninterest income.

| (Dollars in Thousands)              | Three Months Ended |                   |                  | Six Months Ended |                  |
|-------------------------------------|--------------------|-------------------|------------------|------------------|------------------|
|                                     | June 30,<br>2011   | March 31,<br>2011 | June 30,<br>2010 | June 30,<br>2011 | June 30,<br>2010 |
| <b>Noninterest Income:</b>          |                    |                   |                  |                  |                  |
| Service Charges on Deposit Accounts | \$ 6,309           | \$ 5,983          | \$ 7,039         | \$ 12,292        | \$ 13,667        |
| Data Processing Fees                | 764                | 974               | 919              | 1,738            | 1,819            |
| Asset Management Fees               | 1,080              | 1,080             | 1,080            | 2,160            | 2,100            |
| Retail Brokerage Fees               | 939                | 729               | 846              | 1,668            | 1,411            |
| Investment Security Gains           | -                  | -                 | -                | -                | 5                |
| Mortgage Banking Fees               | 568                | 617               | 641              | 1,185            | 1,149            |
| Interchange Fees (1)                | 1,443              | 1,360             | 1,289            | 2,803            | 2,501            |
| ATM/Debit Card Fees (1)             | 1,115              | 1,136             | 1,073            | 2,251            | 2,036            |
| Gain on Sale of Visa Stock          | -                  | 3,172             | -                | 3,172            | -                |
| Other                               | 2,230              | 1,283             | 1,787            | 3,513            | 3,953            |
| <b>Total Noninterest Income</b>     | <b>\$ 14,448</b>   | <b>\$ 16,334</b>  | <b>\$ 14,674</b> | <b>\$ 30,782</b> | <b>\$ 28,641</b> |

(1) Together referred to as "Bank Card Fees"

Significant components of noninterest income are discussed in more detail below.

**Service Charges on Deposit Accounts.** Deposit service charge fees increased \$326,000, or 5.4%, over the first quarter of 2011 and decreased \$729,000, or 10.4%, from the second quarter of 2010. For the first six months of 2011, deposit service charge fees declined by \$1.4 million from the comparable period in 2010. The increase over the first quarter of 2011 is primarily due to a one-day calendar variance and a higher level of overdraft fees. Compared to the three and six month periods of 2010, a lower level of overdraft fees drove the decline, but was partially offset by a lower level of overdraft charge-offs. The decline in overdraft fees was due to reduced activity as well as the implementation of new rules under Regulation E.

**Data Processing Fees.** Fees from data processing services declined by \$210,000, or 21.6%, from the first quarter of 2011 and \$155,000, or 16.9%, from the second quarter of 2010. For the first six months of 2011, fees decreased by \$81,000, or 4.5%. The decline for all periods primarily reflects a reduction in the number of banks we process for. Early in the second quarter of 2011, two of our bank clients were acquired and migrated to a new processor. The annualized impact on our data processing fees will be approximately \$1.2 million.

**Asset Management Fees.** Fees from asset management activities totaled \$1.1 million for the second quarter of 2011, comparable to both the first quarter of 2011 and second quarter of 2010. For the first six months of 2011, fees totaled \$2.2 million, a \$100,000 increase over the comparable period of 2010. At June 30, 2011, assets under management totaled \$677.1 million compared to \$732.3 million at March 31, 2011 and \$678.9 million at June 30, 2010. The distribution of a large estate account during the second quarter of 2011 was the primary reason for the decline in assets under management compared to both the first quarter of 2011 and second quarter of 2010.

**Retail Brokerage Fees.** Fees from the sale of retail investment and insurance products increased \$210,000, or 28.8%, over the first quarter of 2011 and \$93,000, or 11.1%, over the second quarter of 2010. For the first six months of 2011, fees increased by \$257,000, or 18.3%, over the same period in 2010. The increase for all periods reflects both increased trading activity by existing clients and new business. A large annuity account opened in the second quarter

of 2011 also contributed to the favorable variance.

**Mortgage Banking Fees.** Mortgage banking fees decreased \$49,000, or 7.9%, from the first quarter of 2011 and decreased \$73,000, or 11.4%, from the second quarter of 2010. For the first six months of 2011, fees were \$36,000, or 3.1% higher than the comparable period of 2010. New loan production has been impacted by a slowdown in new home purchase activity in our Tallahassee market, attributable in part to consumer uncertainty regarding state government job cuts.

**Bank Card Fees.** Bank card fees (including interchange fees and ATM/debit card fees) increased \$60,000, or 2.5%, over the first quarter of 2011 and \$196,000, or 8.3%, over the second quarter of 2010. For the first six months of 2011, fees increased \$1.4 million, or 38.5%, over the comparable period of 2010. The increase for all periods reflects higher card utilization. An ATM fee increase and a debit card promotion also contributed to the favorable variance versus the periods in 2010.

**Other.** Other income decreased by \$2.2 million, or 49.98%, from the first quarter of 2011 and increased by \$443,000, or 24.8%, over the second quarter of 2010. For the first six months of 2011, other income increased by \$2.7 million, or 69.1%, from the comparable period of 2010. The unfavorable variance compared to the first quarter of 2011 reflects a gain from the sale of our Visa stock during the first quarter of 2011. An increase in gains from the sale of OREO properties partially offset the impact of the Visa gain and also was the primary reason for the favorable variance compared to the second quarter of 2010. For the first six months of 2011, the favorable variance was driven partially by the impact of the Visa gain, but was offset by a lower level of merchant fees. The decline in our merchant fees is substantially offset by a reduction in processing costs, which are reflected as interchange fees in noninterest expense.

## Noninterest Expense

Noninterest expense for the second quarter of 2011 totaled \$31.2 million, a decrease of \$2.2 million, or 6.5%, from the first quarter of 2011 and \$3.5 million, or 10.0%, from the second quarter of 2010. The decline over the first quarter of 2011 reflects lower expense for compensation of \$0.6 million, FDIC insurance of \$0.3 million, intangible amortization of \$0.2 million, OREO costs of \$0.6 million, and miscellaneous expense of \$0.3 million. Recognition of a \$0.6 million swap liability associated with the sale of our Visa stock during the first quarter of 2011 also impacted the variance in miscellaneous expense. Compared to the second quarter of 2010, lower expense for occupancy of \$0.2 million, advertising of \$0.2 million, FDIC insurance of \$0.9 million, intangible amortization of \$0.6 million, OREO costs of \$1.0 million, and interchange fees of \$0.3 million drove the favorable variance.

For the six months of 2011, noninterest expense totaled \$64.5 million, a \$3.5 million or 5.2% decline from the same period of 2010 attributable to lower professional fees of \$0.3 million, advertising expense of \$0.3 million, FDIC insurance of \$0.7 million, intangible amortization expense of \$1.0 million, and interchange fees of \$0.9 million.

The table below reflects the major components of noninterest expense.

| (Dollars in Thousands)           | Three Months Ended |                   |                  | Six Months Ended |                  |
|----------------------------------|--------------------|-------------------|------------------|------------------|------------------|
|                                  | June 30,<br>2011   | March 31,<br>2011 | June 30,<br>2010 | June 30,<br>2011 | June 30,<br>2010 |
| <b>Noninterest Expense:</b>      |                    |                   |                  |                  |                  |
| Salaries                         | \$ 12,509          | \$ 12,936         | \$ 12,533        | \$ 25,445        | \$ 25,582        |
| Associate Benefits               | 3,491              | 3,641             | 3,051            | 7,132            | 6,781            |
| <b>Total Compensation</b>        | <b>16,000</b>      | <b>16,577</b>     | <b>15,584</b>    | <b>32,577</b>    | <b>32,363</b>    |
| <br>                             |                    |                   |                  |                  |                  |
| Premises                         | 2,447              | 2,396             | 2,585            | 4,843            | 4,993            |
| Equipment                        | 2,117              | 2,226             | 2,192            | 4,373            | 4,373            |
| <b>Total Occupancy</b>           | <b>4,564</b>       | <b>4,622</b>      | <b>4,777</b>     | <b>9,186</b>     | <b>9,366</b>     |
| <br>                             |                    |                   |                  |                  |                  |
| Legal Fees                       | 1,048              | 1,107             | 1,109            | 2,155            | 2,156            |
| Professional Fees                | 910                | 845               | 1,047            | 1,755            | 2,095            |
| Processing Services              | 939                | 950               | 974              | 1,889            | 1,861            |
| Advertising                      | 664                | 558               | 877              | 1,222            | 1,555            |
| Travel and Entertainment         | 200                | 211               | 243              | 411              | 474              |
| Printing and Supplies            | 284                | 348               | 320              | 632              | 724              |
| Telephone                        | 498                | 441               | 517              | 939              | 1,067            |
| Postage                          | 387                | 474               | 450              | 861              | 897              |
| Insurance - Other                | 1,076              | 1,380             | 1,982            | 2,456            | 3,172            |
| Intangible Amortization          | 107                | 353               | 710              | 460              | 1,420            |
| Interchange Fees                 | 3                  | 1                 | 329              | 4                | 883              |
| Courier Service                  | 124                | 120               | 115              | 244              | 231              |
| Other Real Estate                | 3,033              | 3,677             | 4,082            | 6,710            | 6,907            |
| Miscellaneous                    | 1,330              | 1,667             | 1,513            | 2,997            | 2,842            |
| <b>Total Other</b>               | <b>10,604</b>      | <b>12,132</b>     | <b>14,268</b>    | <b>22,735</b>    | <b>26,284</b>    |
| <br>                             |                    |                   |                  |                  |                  |
| <b>Total Noninterest Expense</b> | <b>\$ 31,167</b>   | <b>\$ 33,331</b>  | <b>\$ 34,629</b> | <b>\$ 64,498</b> | <b>\$ 68,013</b> |

Significant components of noninterest expense are discussed in more detail below.

Compensation. Compensation expense decreased \$577,000, or 3.5%, over the first quarter of 2011 primarily due to lower expense for performance compensation of \$235,000 and unemployment taxes of \$162,000. The variance in performance compensation reflects lower expense for both individual and company cash incentive plans. The decline in unemployment taxes reflects an expected higher expense for the first quarter of the year as the formula for this tax is based on the first \$7,000 in taxable income per employee. Compared to the second quarter of 2010, compensation expense increased \$416,000, or 2.7%, due to higher stock compensation expense reflecting a higher expected pay-out for this incentive plan.

For the first six months of 2011, compensation expense increased \$214,000, or 0.7%, over the comparable period of 2010 reflecting higher stock compensation expense of \$263,000, pension expense of \$120,000, performance compensation of \$432,000, and realized loan costs of 188,000, partially offset by lower associate base salary expense of \$840,000. A higher expected pay-out drove the increase in stock compensation expense. The increase in pension expense reflects utilization of a lower discount rate in 2011 reflective of lower long-term bond rates. Performance compensation increased due to higher pay-out for both individual and company cash incentive plans versus the prior year. The variance for realized loan cost reflects a lower level of loan production, which for accounting purposes results in an increase in compensation expense. The reduction in associate base salary expense reflects reduction in headcount.

Occupancy. Occupancy expense (including premises and equipment) decreased \$58,000, or 1.3%, from the first quarter of 2011, and \$212,000, or 4.5%, from the second quarter of 2010. For the first six months of 2011, occupancy expense declined by \$180,000, or 1.9%, compared to the same period of 2010. Lower expense for bank premises rental drove the favorable variance compared to the first quarter of 2011. A \$113,000 reduction in furniture and fixture depreciation and bank premises rental expense of \$220,000, which was partially offset by higher property taxes of \$55,000, were the primary reasons for the decline versus the second quarter of 2010. The variance for the first six months of 2011 was primarily due to a \$388,000 decline in bank premises rental expense reflecting the expiration of leases for two re-located offices, which was partially offset by higher depreciation expense of \$138,000 for bank premises and was also reflective of the re-located offices that were constructed during 2010.

Other. Other noninterest expense decreased \$1.5 million, or 12.6%, from the first quarter of 2011 and \$3.7 million, or 25.7%, from the second quarter of 2010. The decrease compared to the first quarter of 2011 was due to lower OREO expense of \$643,000, FDIC insurance expense of \$303,000, intangible amortization expense of \$245,000, and miscellaneous expense of \$328,000. Lower expense for OREO of \$1.0 million, FDIC insurance of \$907,000, intangible amortization of \$602,000, interchange fees of \$327,000, and advertising of \$212,000 drove the reduction compared to the second quarter of 2010. For both periods, the decline in FDIC insurance expense reflects a lower rate due to recent changes to the FDIC premium structure. Intangible amortization expense declined due to the full amortization of core deposit intangibles related to several past acquisitions. Recognition of a \$595,000 swap liability associated with the sale of our Visa stock also impacted the variance in miscellaneous expense versus the first quarter of 2011. The variance in OREO expense compared to the first quarter of 2011 reflects a reduction from losses from the sale of OREO properties. A reduction in OREO carrying costs, primarily property taxes and maintenance, drove the reduction in this expense versus the second quarter of 2010. The variance in advertising fees compared to the second quarter of 2010 was due to a reduction in the marketing costs for our free-checking product. The variance in interchange fees reflects lower processing fees for our merchant processing portfolio due to the migration of our last remaining merchant to another processor.

For the first six months of 2011, other noninterest expense decreased \$3.5 million, or 13.5%, due to lower expense for FDIC insurance of \$715,000, intangible amortization of \$959,000, interchange fees of \$879,000, and advertising of \$333,000 all due to the same reasons previously noted. A reduction in professional fees of \$340,000 reflective of payments to a consulting firm in 2010 for a contract review engagement also contributed to the favorable variance.

Our operating efficiency ratio (expressed as noninterest expense, excluding intangible amortization expense and merger expenses, as a percent of the sum of taxable-equivalent net interest income plus noninterest income) was 81.41% for the second quarter of 2011 compared to 83.30% for the first quarter of 2011 and 86.06% for the second quarter of 2010. For the first six months of 2011, this ratio was 82.37% compared to 85.54% for the comparable period of 2010. The reduction over comparative period's primary reflects the gain on sale of Visa stock.

#### Income Taxes

Income tax expense for the second quarter of 2011 totaled \$1.0 million, an increase of \$0.5 million over the first quarter of 2011 and \$1.0 million over the second quarter of 2010. For the first six months of 2011, income tax expense totaled \$1.6 million compared to an income tax benefit of \$2.6 million for the comparable period of 2010. A higher level of book operating profit drove the higher level of tax expense compared to all prior year periods.

#### FINANCIAL CONDITION

Average earning assets were \$2.259 billion for the second quarter of 2011, a decrease of \$19.7 million, or 0.9%, from the first quarter of 2011 and an increase of \$40.9 million, or 1.8%, from the fourth quarter of 2010. The decline compared to the first quarter of 2011 reflects reduction in the loan portfolio partially offset by higher short-term investments. The increase from the fourth quarter of 2010 is attributable to increases in the overnight funds position and the investment portfolio, which were funded partially through higher repurchases agreement balances. These increases were partially offset by a decrease in the loan portfolio.



## Investment Securities

In the second quarter of 2011, our average investment portfolio of \$305.4 million increased \$0.1 million, or .02%, from the first quarter of 2011 and increased \$43.1 million, or 16.4%, from the fourth quarter of 2010. The average balance of the investment portfolio compared to the first quarter of 2011 was essentially unchanged as a result of a declining municipal bonds portfolio due to maturities which were replaced with purchases of US Treasuries, GNMA mortgage-backed securities, and SBA floating rate securities. The increase in the investment portfolio compared to the fourth quarter of 2010 was a result of an investment strategy which utilized a portion of the Bank's excess liquidity to attain a higher yield than overnight funds. A majority of these investments were US Treasury securities which were also largely used for pledging purposes, and were partially offset by a decline in municipal bond balances. As a percentage of average earning assets, the investment portfolio represented 13.5% in the second quarter of 2011, compared to 13.4% in the first quarter of 2011 and 11.8% in the fourth quarter of 2010. If appropriate, we will continue to look to deploy a portion of the overnight funds position in the investment portfolio during the third quarter.

The investment portfolio is a significant component of our operations and, as such, it functions as a key element of liquidity and asset/liability management. As of June 30, 2011, all securities were classified as available-for-sale, which offers management full flexibility in managing our liquidity and interest rate sensitivity without adversely impacting our regulatory capital levels. It is neither management's intent nor practice to participate in the trading of investment securities for the purpose of recognizing gains and therefore we do not maintain a trading portfolio. Securities in the available-for-sale portfolio are recorded at fair value with unrealized gains and losses associated with these securities recorded net of tax, in the accumulated other comprehensive income (loss) component of shareowners' equity.

At June 30, 2011, the investment portfolio maintained a net pre-tax unrealized gain of \$2.2 million compared to \$1.1 million at both March 31, 2011 and December 31, 2010, respectively. Yields have declined considerably on the short-end of the Treasury curve, particularly on a relative basis, resulting in a higher unrealized gain in the investment portfolio. Approximately \$24.6 million of our investment securities have an unrealized loss totaling \$0.1 million. All positions have been in a loss position for less than 12 months. These positions consist of SBA floating rate and GNMA mortgage-backed securities (MBS), both of which carry the full faith and credit of the US Government, municipal bonds pre-refunded with US Government securities, and US Treasury securities. These positions are not considered impaired, and are expected to mature at par or better. Excluded from these figures is a \$0.6 million unrealized loss on a preferred stock investment held at the holding company that maintained a zero book value as of June 30, 2011, March 31, 2011 and December 31, 2010, respectively. No additional impairment was recorded during the second quarter of 2011, but we continue to closely monitor the fair value of this security as the issuer of this security continues to experience negative operating trends.

## Loans

Average loans decreased \$26.0 million, or 1.5%, from the first quarter of 2011 and \$78.6 million, or 4.4%, from the fourth quarter of 2010. The decline when compared to both periods was primarily driven by reductions in the commercial real estate, residential and construction loan categories. The reduction in these loan categories was due in large part to loan charge-offs and the transfer of loans to OREO. The portfolio continues to be impacted by weak loan demand attributable to the sluggish economy.

During the second quarter, loan charge-offs and transfers to OREO accounted for \$20.8 million, or 76%, of a net reduction in total loans of \$27.2 million from the first quarter 2011. Over the last twelve months, loan charge-offs and migration of loans to OREO accounted for \$54.7 million, or 41%, of the net reduction of \$134.2 million. The aforementioned impact of loan charge-offs and loans transferred to OREO are based on "as of" balances, not averages.

Our bankers continue to try to reach clients who are interested in moving or expanding their banking relationships. While we strive to identify opportunities to increase loans outstanding and enhance the portfolio's overall contribution to earnings, we will only do so by adhering to sound lending principles applied in a prudent and consistent manner. Thus, we will not relax our underwriting standards in order to achieve designated growth goals and, where appropriate, have adjusted our standards to reflect risks inherent in the current economic environment.

#### Nonperforming Assets

Nonperforming assets (including nonaccrual loans, restructured loans (“TDRs”), and OREO) totaled \$145.7 million at the end of the second quarter of 2011, a decrease of \$7.7 million from the first quarter of 2011 and an increase of \$0.4 million over the fourth quarter of 2010. Nonaccrual loans decreased \$12.9 million from the first quarter of 2011 primarily due to the migration of loans through the collection cycle to the OREO category. A slowdown in new additions to the nonaccrual category also contributed to the improvement. Compared to the fourth quarter of 2010, nonaccrual loans declined by \$4.6 million reflecting the movement of loans to the OREO category and, to a lesser extent, migration to the TDR category. TDRs totaled \$23.6 million at the end of the second quarter, a \$0.4 million decrease from the first quarter of 2011 and a \$1.9 million increase over the fourth quarter of 2010. The balance of OREO increased \$5.7 million over the first quarter of 2011 and \$3.1 million over the fourth quarter of 2010 reflective of momentum in working problem loans through the foreclosure process. Overall, a slower pace of loan defaults, momentum in working loans through the collection cycle, and progress in our property disposition efforts has contributed to the overall improvement in our nonperforming asset portfolio.

Through the first six months of 2011, we sold OREO properties totaling \$17.7 million, which approximates the total book value of properties sold for the full year 2010. Nonperforming assets represented 5.60% of total assets at June 30, 2011 compared to 5.76% at March 31, 2011 and 5.54% at December 31, 2010.

Non-performing assets are summarized as follows.

| (Dollars in Thousands)                            | June 30,<br>2011 | March 31,<br>2011 | December 31,<br>2010 |
|---|------------------|-------------------|----------------------|
| Nonaccruing Loans                                 | \$ 61,076        | \$ 73,954         | \$ 65,700            |
| Restructured Loans                                | 23,582           | 24,028            | 21,649               |
| Total Nonperforming Loans                         | 84,658           | 97,982            | 87,349               |
| Other Real Estate Owned                           | 61,016           | 55,364            | 57,937               |
| Total Nonperforming Assets                        | \$ 145,674       | \$ 153,346        | \$ 145,286           |
| Past Due 30-89 Days or More                       | \$ 18,103        | \$ 19,391         | \$ 24,193            |
| Past Due 90 Days or More (and still accruing)     | \$ 271           | \$ -              | \$ 159               |
| Nonperforming Loans/Loans                         | 5.02%            | 5.71%             | 4.97%                |
| Nonperforming Assets/Total Assets                 | 5.60%            | 5.76%             | 5.54%                |
| Nonperforming Assets/Loans Plus Other Real Estate | 8.33%            | 8.66%             | 8.00%                |
| Nonperforming Assets/Capital(1)                   | 49.95%           | 52.31%            | 49.34%               |
| Allowance/Nonperforming Loans                     | 36.71%           | 34.57%            | 40.57%               |

(1) For computation of this percentage, "Capital" refers to shareowners' equity plus the allowance for loan losses.

#### Allowance for Loan Losses

We maintain an allowance for loan losses at a level sufficient to provide for the estimated loan losses inherent in the loan portfolio as of the balance sheet date. Credit losses arise from borrowers' inability or unwillingness to repay, and from other risks inherent in the lending process, including collateral risk, operations risk, concentration risk and economic risk. All related risks of lending are considered when assessing the adequacy of the loan loss reserve. The allowance for loan losses is established through a provision charged to expense. Loans are charged against the allowance when management believes collection of the principal is unlikely. The allowance for loan losses is based on management's judgment of overall loan quality. This is a significant estimate based on a detailed analysis of the loan portfolio. The balance can and will change based on changes in the assessment of the portfolio's overall credit quality. We evaluate the adequacy of the allowance for loan losses on a quarterly basis.

The allowance for loan losses was \$31.1 million at June 30, 2011 compared to \$33.9 million at December 31, 2010. The allowance for loan losses was 1.84% of outstanding loans (net of overdrafts) and provided coverage of 37% of nonperforming loans at June 30, 2011 compared to 2.01% and 41%, respectively, at December 31, 2010. The decline in the allowance is due to a lower level of impaired loan reserves as well as a reduction in general reserves, primarily due to a reduction in the level of internally classified loans and lower loss rates. It is management's opinion that the allowance at June 30, 2011 is adequate to absorb losses inherent in the loan portfolio at quarter-end.

#### Deposits

Average total deposits were \$2.107 billion for the second quarter of 2011, a decrease of \$18.1 million, or 0.9%, from the first quarter of 2011 and a decline of \$8.6 million, or 0.4%, from the fourth quarter of 2010. Deposits decreased in both periods driven primarily by a reduction in certificates of deposit. Additionally, a decrease resulting from existing clients moving from our government guaranteed NOW product to repurchase agreements occurred late in the fourth quarter of 2010 as further discussed below. Public fund balances increased as anticipated from the fourth quarter of 2010, but have declined from the first quarter level which reflects the normal seasonality within this deposit category. Savings and money markets accounts experienced a slight increase in both periods, partially offsetting the above mentioned decline.

Pursuant to changes in the FDIC's Temporary Liquidity Guarantee Program, our government guaranteed NOW product was discontinued during the fourth quarter. As of December 31, 2010, approximately \$95.0 million in balances from this product remained in the NOW category, \$95.0 million migrated to the noninterest bearing DDA category, and \$60.0 million moved into repurchase agreements.

We continue to pursue prudent pricing discipline to manage the mix of our deposits. Therefore, we are not attempting to compete with higher rate paying competitors for deposits.

## MARKET RISK AND INTEREST RATE SENSITIVITY

### Market Risk and Interest Rate Sensitivity

**Overview.** Market risk management arises from changes in interest rates, exchange rates, commodity prices, and equity prices. We have risk management policies to monitor and limit exposure to market risk and do not participate in activities that give rise to significant market risk involving exchange rates, commodity prices, or equity prices. In asset and liability management activities, our policies are designed to minimize structural interest rate risk.

**Interest Rate Risk Management.** Our net income is largely dependent on net interest income. Net interest income is susceptible to interest rate risk to the degree that interest-bearing liabilities mature or re-price on a different basis than interest-earning assets. When interest-bearing liabilities mature or re-price more quickly than interest-earning assets in a given period, a significant increase in market rates of interest could adversely affect net interest income. Similarly, when interest-earning assets mature or re-price more quickly than interest-bearing liabilities, falling interest rates could result in a decrease in net interest income. Net interest income is also affected by changes in the portion of interest-earning assets that are funded by interest-bearing liabilities rather than by other sources of funds, such as noninterest-bearing deposits and shareowners' equity.

We have established a comprehensive interest rate risk management policy, which is administered by management's Asset/Liability Management Committee (ALCO). The policy establishes limits of risk, which are quantitative measures of the percentage change in net interest income (a measure of net interest income at risk) and the fair value of equity capital (a measure of economic value of equity ("EVE") at risk) resulting from a hypothetical change in interest rates for maturities from one day to 30 years. We measure the potential adverse impacts that changing interest rates may have on our short-term earnings, long-term value, and liquidity by employing simulation analysis through the use of computer modeling. The simulation model captures optionality factors such as call features and interest rate caps and floors imbedded in investment and loan portfolio contracts. As with any method of gauging interest rate risk, there are certain shortcomings inherent in the interest rate modeling methodology used by us. When interest rates change, actual movements in different categories of interest-earning assets and interest-bearing liabilities, loan prepayments, and withdrawals of time and other deposits, may deviate significantly from assumptions used in the model. Finally, the methodology does not measure or reflect the impact that higher rates may have on adjustable-rate loan clients' ability to service their debts, or the impact of rate changes on demand for loan, and deposit products.

We prepare a current base case and three alternative simulations, at least once a quarter, and report the analysis to the Board of Directors. In addition, more frequent forecasts may be produced when interest rates are particularly uncertain or when other business conditions so dictate.

Our interest rate risk management goal is to avoid unacceptable variations in net interest income and capital levels due to fluctuations in market rates. Management attempts to achieve this goal by balancing, within policy limits, the volume of floating-rate liabilities with a similar volume of floating-rate assets, by keeping the average maturity of fixed-rate asset and liability contracts reasonably short and matched, by maintaining a pool of administered core deposits, and by adjusting pricing rates to market conditions on a continuing basis.

The balance sheet is subject to testing for interest rate shock possibilities to indicate the inherent interest rate risk. Average interest rates are shocked by plus or minus 100, 200, and 300 basis points ("bp"), although we may elect not to use particular scenarios that we determined are impractical in a current rate environment. It is management's goal to structure the balance sheet so that net interest earnings at risk over a 12-month period and the economic value of equity at risk do not exceed policy guidelines at the various interest rate shock levels.

We augment our quarterly interest rate shock analysis with alternative external interest rate scenarios on a monthly basis. These alternative interest rate scenarios may include non-parallel rate ramps.

Analysis. Measures of net interest income at risk produced by simulation analysis are indicators of an institution's short-term performance in alternative rate environments. These measures are typically based upon a relatively brief period, usually one year. They do not necessarily indicate the long-term prospects or economic value of the institution.

#### Estimated Changes in Net Interest Income (1)

| Changes in Interest Rates | +300 bp | +200 bp | +100 bp | -100 bp |
|---------------------------|---------|---------|---------|---------|
| Policy Limit (±)          | 10.0%   | 7.5%    | 5.0%    | 5.0%    |
| June 30, 2011             | -7.2%   | -3.5%   | -0.8%   | -0.1%   |
| March 31, 2011            | -8.2%   | -4.1%   | -1.0%   | -0.5%   |

The Net Interest Income at Risk position improved for the second quarter of 2011, when compared to the prior quarter-end, for all rate scenarios. Our largest exposure is at the +300 bp level, with a measure of -7.2%, which is still within our policy limit of -10.0%. This is an improvement when compared to the linked quarter, as the favorable variances were attributable to an increase in loan fees and a lower level of interest bearing deposit accounts and repurchase agreements, which were partially offset by a reduction in the overnight funds balance and the lower loan portfolio. All measures of net interest income at risk are within our prescribed policy limits.

The measures of equity value at risk indicate our ongoing economic value by considering the effects of changes in interest rates on all of our cash flows, and discounting the cash flows to estimate the present value of assets and liabilities. The difference between these discounted values of the assets and liabilities is the economic value of equity, which, in theory, approximates the fair value of our net assets.

#### Estimated Changes in Economic Value of Equity (1)

| Changes in Interest Rates | +300 bp | +200 bp | +100 bp | -100 bp |
|---------------------------|---------|---------|---------|---------|
| Policy Limit (±)          | 12.5%   | 10.0%   | 7.5%    | 7.5%    |
| June 30, 2011             | -1.1%   | 2.8%    | 3.9%    | -5.4%   |
| March 31, 2011            | -2.5%   | 1.5%    | 3.0%    | -6.3%   |

Our risk profile, as measured by EVE, improved for the second quarter of 2011 when compared to the linked quarter-end. In the rising rate scenarios, our largest exposure is at the up 300 bp scenario, with a measure of -1.1%, which is still within our policy limit of -12.5%. This is an improvement from the prior quarter primarily attributable to lower Treasury and FHLB curves, reflecting slight decreases in the market value of loans and improvements in the market values of deposits and FHLB borrowings, respectively. All measures of economic value of equity are within our prescribed policy limits.

(1)Down 200 and 300 rate scenarios have been excluded due to the current historically low interest rate environment.

## LIQUIDITY AND CAPITAL RESOURCES

### Liquidity

In general terms, liquidity is a measurement of our ability to meet our cash needs. Our objective in managing our liquidity is to maintain our ability to meet loan commitments, purchase securities or repay deposits and other liabilities in accordance with their terms, without an adverse impact on our current or future earnings. Our liquidity strategy is guided by policies that are formulated and monitored by our ALCO and senior management, and which take into account the marketability of assets, the sources and stability of funding and the level of unfunded commitments. We regularly evaluate all of our various funding sources with an emphasis on accessibility, stability, reliability and cost-effectiveness. Our principal source of funding has been our client deposits, supplemented by our short-term and long-term borrowings, primarily from securities sold under repurchase agreements, federal funds purchased and FHLB borrowings. We believe that the cash generated from operations, our borrowing capacity and our access to capital resources are sufficient to meet our future operating capital and funding requirements.

Overall, we have the ability to generate \$701.3 million in additional liquidity through all of our available resources. In addition to primary borrowing outlets mentioned above, we also have the ability to generate liquidity by borrowing from the Federal Reserve Discount Window and through brokered deposits. Management recognizes the importance of maintaining liquidity and has developed a Contingency Liquidity Plan, which addresses various liquidity stress levels and our response and action based on the level of severity. We periodically test our credit facilities for access to the funds, but also understand that as the severity of the liquidity level increases that certain credit facilities may no longer be available. The liquidity currently available to us is considered sufficient to meet the ongoing needs.



We view our investment portfolio as a liquidity source and have the option to pledge the portfolio as collateral for borrowings or deposits, and/or sell selected securities. The portfolio consists of debt issued by the U.S. Treasury, U.S. governmental agencies, and municipal governments. The weighted average life of the portfolio is approximately 1.71 years and as of quarter-end had a net unrealized pre-tax gain of \$2.2 million.

Our average liquidity (defined as funds sold plus interest bearing deposits with other banks less funds purchased) of \$249.1 million during the second quarter of 2011 compared to an average net overnight funds sold position of \$238.1 million in the first quarter of 2011 and an average overnight funds sold position of \$164.9 million in the fourth quarter of 2010. The higher balance when compared to the linked quarter primarily reflects the declines in the loan portfolio, which was partially offset by a decrease in deposits mentioned above and lower levels of short-term borrowings. The favorable variance as compared to the fourth quarter of 2010 is primarily attributable to an increase in repurchase agreements and a net reduction in loans, which was partially offset by declines in deposits and the deployment of funds to the investment portfolio.

Capital expenditures are expected to approximate \$4.0 million over the next 12 months, which consist primarily of office remodeling, office equipment and furniture, and technology purchases. Management believes that these capital expenditures will be funded with existing resources without impairing our ability to meet our on-going obligations.

#### Borrowings

At June 30, 2011, advances from the FHLB totaled \$59.2 million in outstanding debt and consisted of 50 notes. During the first six months of 2011, the Bank made FHLB advance payments totaling approximately \$1.7 million and obtained one new FHLB advance totaling \$0.8 million. The FHLB notes are collateralized by a blanket floating lien on all of our 1-4 family residential mortgage loans, commercial real estate mortgage loans, and home equity mortgage loans.

We have issued two junior subordinated deferrable interest notes to wholly owned Delaware statutory trusts. The first note for \$30.9 million was issued to CCBG Capital Trust I in November 2004. The second note for \$32.0 million was issued to CCBG Capital Trust II in May 2005. The interest payments for the CCBG Capital Trust I borrowing are due quarterly at a variable rate of LIBOR plus a margin of 1.90%. The rate for the second quarter was 2.15%. This note matures on December 31, 2034. The interest payment for the CCBG Capital Trust II borrowing adjusts quarterly to a variable rate of LIBOR plus a margin of 1.80%. The rate for the second quarter was 2.05%. This note matures on June 15, 2035. The proceeds of these borrowings were used to partially fund acquisitions.

In accordance with certain Federal Reserve Resolutions (discussed in further detail within our 2010 Form 10-K), CCBG must receive approval from the Federal Reserve prior to incurring new debt, refinancing existing debt, or making interest payments on its trust preferred securities. Under the terms of each trust preferred securities note, in the event of default or if we elect to defer interest on the note, we may not, with certain exceptions, declare or pay dividends or make distributions on our capital stock or purchase or acquire any of our capital stock.

#### Capital

Equity capital was \$260.5 million as of June 30, 2011, compared to \$259.0 million as of December 31, 2010. Our leverage ratio was 9.95% and 10.10%, respectively, and our tangible common equity ratio was 6.96% and 6.82%, respectively, for the same periods. Our risk-adjusted capital ratio of 15.19% at June 30, 2011, exceeds the 10% threshold to be designated as "well-capitalized" under the risk-based regulatory guidelines. Management believes our strong capital base has offered protection during the course of the current economic downturn. We chose not to participate in the government's TARP program and, to date, we have not initiated a capital raise.

During the first six months of 2011, shareowners' equity increased \$1.5 million, or 1.2%, on an annualized basis. During this same period, shareowners' equity was positively impacted by net income of \$3.5 million, the issuance of stock totaling approximately \$0.3 million, accrual for performance shares of approximately \$0.4 million, and a change in our net unrealized gain on securities of \$0.7 million. Dividends paid reduced shareowners' equity by approximately \$3.4 million.

At June 30, 2011, our common stock had a book value of \$15.20 per diluted share compared to \$15.15 at December 31, 2010. Book value is impacted by changes in the amount of our net unrealized gain or loss on investment securities available-for-sale and changes to the amount of our unfunded pension liability, both of which are recorded through other comprehensive income. At June 30, 2011, the net unrealized gain on investment securities available for sale was \$1.4 million and the amount of our unfunded pension liability was \$16.4 million.

State and federal regulations place certain restrictions on the payment of dividends by both CCBG and the Bank. The Bank's aggregate net profits for the past two years are significantly less than the dividends declared and paid to CCBG over that same period. In addition, in accordance with the Federal Reserve Resolutions (discussed in further detail within our 2010 Form 10-K), the Bank must seek approval from the Federal Reserve prior to declaring or paying a dividend. As a result, the Bank must obtain approval from its regulators to issue and declare any further dividends to CCBG. The Bank may not receive the required approvals. As of June 30, 2011, we believe we have sufficient cash to fund shareowner dividends in 2011 should the Board choose to declare and pay a quarterly dividend during the year. Even if we have sufficient cash to pay dividends, we must seek approval from the Federal Reserve to pay dividends to our shareowners and may not receive the required approvals. We will continue to evaluate our dividend quarterly and consult with our regulators concerning matters relating to our overall dividend policy.

#### OFF-BALANCE SHEET ARRANGEMENTS

We do not currently engage in the use of derivative instruments to hedge interest rate risks. However, we are a party to financial instruments with off-balance sheet risks in the normal course of business to meet the financing needs of our clients.

At June 30, 2011, we had \$307.9 million in commitments to extend credit and \$11.4 million in standby letters of credit. Commitments to extend credit are agreements to lend to a client so long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Standby letters of credit are conditional commitments issued by us to guarantee the performance of a client to a third party. We use the same credit policies in establishing commitments and issuing letters of credit as we do for on-balance sheet instruments.

If commitments arising from these financial instruments continue to require funding at historical levels, management does not anticipate that such funding will adversely impact its ability to meet on-going obligations. In the event these commitments require funding in excess of historical levels, management believes current liquidity, advances available from the FHLB and the Federal Reserve, and investment security maturities provide a sufficient source of funds to meet these commitments.

## CRITICAL ACCOUNTING POLICIES

The consolidated financial statements and accompanying Notes to Consolidated Financial Statements are prepared in accordance with accounting principles generally accepted in the United States of America, which require us to make various estimates and assumptions (see Note 1 in the Notes to Consolidated Financial Statements). We believe that, of our significant accounting policies, the following may involve a higher degree of judgment and complexity.

**Allowance for Loan Losses.** The allowance for loan losses is established through a charge to the provision for loan losses. Provisions are made to reserve for estimated losses in loan balances. The allowance for loan losses is a significant estimate and is evaluated quarterly by us for adequacy. The use of different estimates or assumptions could produce a different required allowance, and thereby a larger or smaller provision recognized as expense in any given reporting period. A further discussion of the allowance for loan losses can be found in the section entitled "Allowance for Loan Losses" and Note 1 in the Notes to Consolidated Financial Statements in our 2010 Form 10-K.

**Intangible Assets.** Intangible assets consist primarily of goodwill, core deposit assets, and other identifiable intangibles that were recognized in connection with various acquisitions. Goodwill represents the excess of the cost of acquired businesses over the fair market value of their identifiable net assets. We perform an impairment review on an annual basis during the fourth quarter or more frequently if events or changes in circumstances indicate that the carrying value may not be recoverable. Impairment testing requires management to make significant judgments and estimates relating to the fair value of its reporting unit. Significant changes to our estimates, when and if they occur, could result in a non-cash impairment charge and thus have a material impact on our operating results for any particular reporting period. A goodwill impairment charge would not adversely affect the calculation of our risk based and tangible capital ratios.

Because the book value of our equity exceeded our market capitalization as of June 30, 2011, we considered the guidelines set forth in ASC Topic 350 to discern whether further testing for potential impairment was needed. Based on this assessment, we performed an interim impairment test which consists of two steps. Step One compares the estimated fair value of the reporting unit to its carrying amount. If the carrying amount exceeds the estimated fair value, Step Two is performed by comparing the fair value of the reporting unit's implied goodwill to the carrying value of goodwill. If the carrying value of the reporting unit's goodwill exceeds the estimated fair value, an impairment charge is recorded equal to the excess. The Step One test we performed indicated that the carrying amount (including goodwill) of our reporting unit exceeded its estimated fair value. The Step Two test indicated the estimated fair value of our reporting unit's implied goodwill exceeded its carrying amount. Based on the results of the Step Two analysis, we concluded that goodwill was not impaired as of June 30, 2011. We will continue to test goodwill as defined by ASC Topic 350.

**Core deposit assets** represent the premium we paid for core deposits. Core deposit intangibles are amortized on the straight-line method over various periods ranging from 5-10 years. Generally, core deposits refer to nonpublic, non-maturing deposits including noninterest-bearing deposits, NOW, money market and savings. We make certain estimates relating to the useful life of these assets, and rate of run-off based on the nature of the specific assets and the client bases acquired. If there is a reason to believe there has been a permanent loss in value, management will assess these assets for impairment. Any changes in the original estimates may materially affect our operating results.

**Pension Assumptions.** We have a defined benefit pension plan for the benefit of substantially all of our associates. Our funding policy with respect to the pension plan is to contribute amounts to the plan sufficient to meet minimum funding requirements as set by law. Pension expense, reflected in the Consolidated Statements of Income in noninterest expense as "Salaries and Associate Benefits," is determined by an external actuarial valuation based on assumptions that are evaluated annually as of December 31, the measurement date for the pension obligation. The Consolidated Statements of Financial Condition reflect an accrued pension benefit cost due to funding levels and

unrecognized actuarial amounts. The most significant assumptions used in calculating the pension obligation are the weighted-average discount rate used to determine the present value of the pension obligation, the weighted-average expected long-term rate of return on plan assets, and the assumed rate of annual compensation increases. These assumptions are re-evaluated annually with the external actuaries, taking into consideration current market conditions and anticipated long-term market conditions.

The weighted-average discount rate is determined by matching the anticipated Retirement Plan cash flows to a long-term corporate Aa-rated bond index and solving for the underlying rate of return, which investing in such securities would generate. This methodology is applied consistently from year-to-year. We anticipate using a 5.55% discount rate in 2011.

The weighted-average expected long-term rate of return on plan assets is determined based on the current and anticipated future mix of assets in the plan. The assets currently consist of equity securities, U.S. Government and Agency debt securities, and other securities (typically temporary liquid funds awaiting investment). We anticipate using a rate of return on plan assets of 8.0% for 2011.

The assumed rate of annual compensation increases is based on expected trends in salaries and the employee base. We anticipate using a compensation increase of 4.25% for 2011 reflecting current market trends. Information on components of our net periodic benefit cost is provided in Note 8 of the Notes to Consolidated Financial Statements included herein and Note 12 of the Notes to Consolidated Financial Statements in our 2010 Form 10-K.

TABLE I  
AVERAGE BALANCES & INTEREST RATES

| (Taxable<br>Equivalent Basis -<br>Dollars in<br>Thousands) | Three Months Ended June 30, |                     |                 |                     |                     |                 | Six Months Ended June 30, |                     |                 |                     |
|--|-----------------------------|---------------------|-----------------|---------------------|---------------------|-----------------|---------------------------|---------------------|-----------------|---------------------|
|  | 2011                        |                     |                 | 2010                |                     |                 | 2011                      |                     | 2010            |                     |
|  | Average<br>Balances         | Average<br>Interest | Average<br>Rate | Average<br>Balances | Average<br>Interest | Average<br>Rate | Average<br>Balances       | Average<br>Interest | Average<br>Rate | Average<br>Balances |
| <b>Assets:</b>   |                             |                     |                 |                     |                     |                 |                           |                     |                 |                     |
| Loans, Net of<br>Unearned<br>Interest(1)(2)                | \$ 1,704,348                | \$ 24,465           | 5.76%           | \$ 1,841,379        | \$ 26,795           | 5.84%           | \$ 1,717,267              | \$ 48,566           | 5.76%           | \$ 1,841,379        |
| Taxable<br>Investment<br>Securities(2)                     | 244,487                     | 825                 | 1.35            | 128,268             | 708                 | 2.21            | 237,857                   | 1,676               | 1.41            | 128,268             |
| Tax-Exempt<br>Investment<br>Securities                     | 60,963                      | 297                 | 1.95            | 92,140              | 624                 | 2.71            | 67,558                    | 634                 | 1.88            | 92,140              |
| Funds Sold   | 249,133                     | 145                 | 0.23            | 267,578             | 176                 | 0.26            | 246,030                   | 316                 | 0.23            | 267,578             |
| Total Earning<br>Assets                                    | 2,258,931                   | 25,732              | 4.57%           | 2,329,365           | 28,303              | 4.87%           | 2,268,712                 | 51,192              | 4.55%           | 2,329,365           |
| Cash & Due From<br>Banks                                   | 47,465                      |                     |                 | 50,739              |                     |                 | 49,194                    |                     |                 | 50,739              |
| Allowance For<br>Loan Losses                               | (32,993)                    |                     |                 | (41,074)            |                     |                 | (33,903)                  |                     |                 | (41,074)            |
| Other Assets   | 344,884                     |                     |                 | 339,458             |                     |                 | 346,581                   |                     |                 | 339,458             |
| <b>TOTAL ASSETS</b>  | <b>\$ 2,618,287</b>         |                     |                 | <b>\$ 2,678,488</b> |                     |                 | <b>\$ 2,630,584</b>       |                     |                 | <b>\$ 2,678,488</b> |
| <b>Liabilities:</b>  |                             |                     |                 |                     |                     |                 |                           |                     |                 |                     |
| NOW Accounts   | \$ 782,698                  | \$ 259              | 0.13%           | \$ 879,329          | \$ 400              | 0.18%           | \$ 784,806                | \$ 520              | 0.13%           | \$ 879,329          |
| Money Market<br>Accounts                                   | 284,411                     | 136                 | 0.19            | 333,976             | 331                 | 0.40            | 281,503                   | 267                 | 0.19            | 333,976             |
| Savings Accounts   | 152,599                     | 16                  | 0.04            | 131,333             | 17                  | 0.05            | 148,633                   | 34                  | 0.05            | 131,333             |
| Other Time<br>Deposits                                     | 338,723                     | 672                 | 0.80            | 430,571             | 1,615               | 1.50            | 349,589                   | 1,520               | 0.88            | 430,571             |
| Total Interest<br>Bearing Deposits                         | 1,558,431                   | 1,083               | 0.28            | 1,775,209           | 2,363               | 0.53            | 1,564,531                 | 2,341               | 0.30            | 1,775,209           |
| Short-Term<br>Borrowings                                   | 76,754                      | 110                 | 0.58            | 22,694              | 12                  | 0.20            | 81,982                    | 221                 | 0.54            | 22,694              |
| Subordinated Note<br>Payable                               | 62,887                      | 343                 | 2.16            | 62,887              | 639                 | 4.02            | 62,887                    | 683                 | 2.16            | 62,887              |
| Other Long-Term<br>Borrowings                              | 49,650                      | 492                 | 3.97            | 52,704              | 551                 | 4.20            | 49,995                    | 986                 | 3.98            | 52,704              |
| Total Interest<br>Bearing Liabilities                      | 1,747,722                   | 2,028               | 0.47%           | 1,913,494           | 3,565               | 0.75%           | 1,759,395                 | 4,231               | 0.48%           | 1,913,494           |
| Noninterest<br>Bearing Deposits                            | 548,870                     |                     |                 | 458,969             |                     |                 | 551,759                   |                     |                 | 458,969             |

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|   |              |              |              |              |
|---|--------------|--------------|--------------|--------------|
| Other Liabilities                                     | 59,324       | 42,152       | 57,440       |              |
| TOTAL<br>LIABILITIES                                  | 2,355,916    | 2,414,615    | 2,368,594    | 2,414,615    |
| TOTAL<br>SHAREOWNERS'<br>EQUITY                       | 262,371      | 263,873      | 261,990      | 263,873      |
| TOTAL<br>LIABILITIES<br>AND<br>SHAREOWNERS'<br>EQUITY | \$ 2,618,287 | \$ 2,678,488 | \$ 2,688,399 | \$ 2,678,488 |
| Interest Rate<br>Spread                               |              | 4.10%        | 4.12%        | 4.07%        |
| Net Interest<br>Income                                | \$ 23,704    | \$ 24,738    | \$ 49,961    | \$ 49,961    |
| Net Interest<br>Margin(3)                             |              | 4.21%        | 4.26%        | 4.17%        |

(1) Average balances include nonaccrual loans. Interest income includes fees on loans of \$392,000 and \$758,000, for the three and six months ended June 30, 2011 versus \$419,000 and \$782,000 for the comparable periods ended June 30, 2010.

(2) Interest income includes the effects of taxable equivalent adjustments using a 35% tax rate.

(3) Taxable equivalent net interest income divided by average earning assets.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

See “Market Risk and Interest Rate Sensitivity” in Management’s Discussion and Analysis of Financial Condition and Results of Operations, above, which is incorporated herein by reference. Management has determined that no additional disclosures are necessary to assess changes in information about market risk that have occurred since December 31, 2010.

Item 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

As of June 30, 2011, the end of the period covered by this Form 10-Q, our management, including our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934). Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer each concluded that as of June 30, 2011, the end of the period covered by this Form 10-Q, we maintained effective disclosure controls and procedures.

Changes in Internal Control over Financial Reporting

Our management, including the Chief Executive Officer and Chief Financial Officer, has reviewed our internal control over financial reporting (as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934). There have been no significant changes in our internal control over financial reporting during our most recently completed fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

We are party to lawsuits arising out of the normal course of business. In management's opinion, there is no known pending litigation, the outcome of which would, individually or in the aggregate, have a material effect on our consolidated results of operations, financial position, or cash flows.

Item 1A. Risk Factors

In addition to the other information set forth in this Quarterly Report, you should carefully consider the factors discussed in Part I, Item 1A. “Risk Factors” in our 2010 Form 10-K, as updated in our subsequent quarterly reports. The risks described in our 2010 Form 10-K are not the only risks facing us. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results. There have been no material changes in our risk factors from those disclosed in our 2010 Form 10-K, except for the following:

The Federal Reserve’s repeal of the prohibition against payment of interest on demand deposits (Regulation Q) may increase competition for such deposits and ultimately increase interest expense.

On July 14, 2011, the Federal Reserve issued final rules to repeal Regulation Q, which had prohibited the payment of interest on demand deposits by institutions that are member banks of the Federal Reserve System. The final rules implement Section 627 of the Dodd-Frank Act, which repealed Section 19(i) of the Federal Reserve Act in its entirety effective July 21, 2011. As a result, banks and thrifts are now permitted to offer interest-bearing demand deposit



accounts to commercial customers, which were previously forbidden under Regulation Q. The repeal of Regulation Q may cause increased competition from other financial institutions for these deposits. If we decide to pay interest on demand accounts, we would expect interest expense to increase and have a negative impact on our net interest margin.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds  
None.

Item 3. Defaults Upon Senior Securities  
None.

Item 4. [Removed and Reserved]

Item 5. Other Information  
None.

Item 6.

Exhibits

(A) Exhibits

- 10.1 2011 Associate Stock Purchase Plan – incorporated herein by reference to Exhibit 10.1 of the Registrant’s Current Report on Form 8-K (filed 5/2/2011) (No. 0-13358).
- 10.2 2011 Director Stock Purchase Plan – incorporated herein by reference to Exhibit 10.2 of the Registrant’s Current Report on Form 8-K (filed 5/2/2011) (No. 0-13358).
- 10.3 2011 Associate Stock Incentive Plan – incorporated herein by reference to Exhibit 10.3 of the Registrant’s Current Report on Form 8-K (filed 5/2/2011) (No. 0-13358).
- 31.1 Certification of William G. Smith, Jr., Chairman, President and Chief Executive Officer of Capital City Bank Group, Inc., Pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934.
- 31.2 Certification of J. Kimbrough Davis, Executive Vice President and Chief Financial Officer of Capital City Bank Group, Inc., Pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934.
- 32.1 Certification of William G. Smith, Jr., Chairman, President and Chief Executive Officer of Capital City Bank Group, Inc., Pursuant to 18 U.S.C. Section 1350.
- 32.2 Certification of J. Kimbrough Davis, Executive Vice President and Chief Financial Officer of Capital City Bank Group, Inc., Pursuant to 18 U.S.C. Section 1350.
- 101.INS XBRL Instance Document
- 101.SCH XBRL Taxonomy Extension Schema Document
- 101.CALXBRL Taxonomy Extension Calculation Linkbase Document
- 101.LABXBRL Taxonomy Extension Label Linkbase Document
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned Chief Financial Officer hereunto duly authorized.

CAPITAL CITY BANK GROUP, INC.  
(Registrant)

By: /s/ J. Kimbrough Davis  
J. Kimbrough Davis  
Executive Vice President and Chief Financial Officer  
(Mr. Davis is the Principal Financial Officer and has  
been duly authorized to sign on behalf of the Registrant)

Date: August 8, 2011

Exhibit Index

Exhibit Description

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