

Prepared for Opportunity

2008 ANNUAL REPORT

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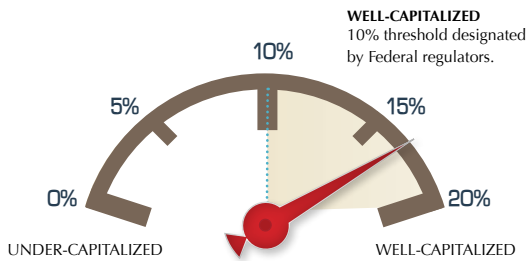
– Michael G. Sanchez, CEO

Coastal Banking Company Inc. is the \$476.8 million-asset bank holding company of CBC National Bank, which operates as Lowcountry National Bank in Beaufort, S.C., First National Bank of Nassau County in Fernandina Beach, Fla., and The Georgia Bank in Meigs, Ga. CBC National Bank, which is headquartered in Fernandina Beach, provides a full range of consumer and business banking services through full-service

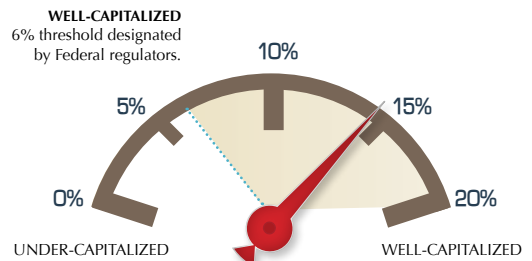
banking offices in Beaufort, Fernandina Beach, Meigs, Hilton Head, S.C., and Port Royal, S.C. The company also operates a wholesale lending division based in Atlanta and commercial loan production offices in Jacksonville, Fla., and Savannah, Ga. The company's common stock is publicly traded on the OTC Bulletin Board under the symbol CBCO. For more information, please visit www.coastalbanking.com.

2008 Highlights

Capital Ratios



Coastal Banking Company
TOTAL RISK-BASED
CAPITAL RATIO 16.10%

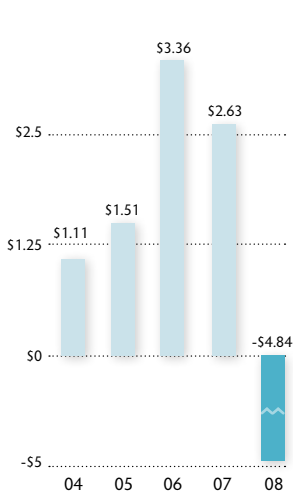


Coastal Banking Company
TIER 1 RISK-BASED
CAPITAL RATIO 14.85%

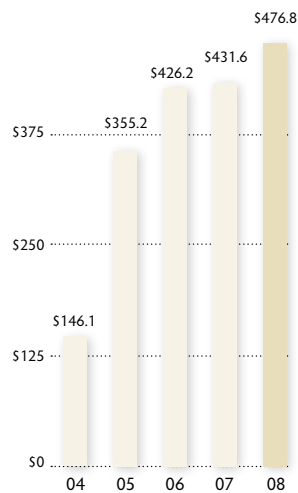
The higher the ratio of capital to risk-weighted assets, the more resources banks have to weather a recession. Coastal Banking Company ended 2008 well-capitalized and with ample liquidity to meet its needs.

Available Liquidity

(from multiple sources) (millions)



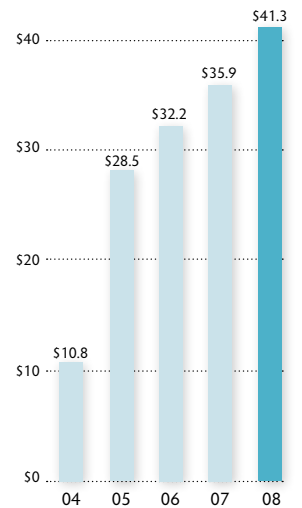
Net Income (in millions)



Assets
(in millions)



Diluted Earnings Per Share



Tangible Shareholders' Equity
(in millions)



Letter to Shareholders

Dear Shareholders:

It goes without saying that 2008 was one of the most difficult banking markets in a generation, and the prospects for 2009 appear to be every bit as challenging. It is important to point out, however, that despite the obstacles that remain ahead of us, our long-term outlook for the company is genuinely positive.

It is not easy to see a silver lining in the current economy. However, our optimism is rooted in several fundamental developments in 2008 that bode well for our company:

- We never originated or purchased any subprime loans, Alt-A loans or option ARM loans. Nor do we hold any investment securities that are collateralized by these types of loans. This has proven to be critical to our ability to weather the economic downturn to date.
- We ended 2008 with strong capital ratios and ample liquidity, despite increasing our loan-loss reserves substantially during the year. This will help us continue to ride out the storm in 2009 while positioning us to take advantage of any strategic growth opportunities that arise.
- The consolidation of our separate banking subsidiaries in 2008 has led to economies of scale and increased efficiency in our operations. This has reduced redundant costs, allowing us more flexible and better uses of our capital.
- Our wholesale lending division far exceeded our performance expectations during the year, both in loan volume and profitability. Our outlook for wholesale lending in 2009 is equally as upbeat, given the fact that low interest rates likely will continue to drive demand for refinancing and purchases. This has given us a valuable source of additional revenue.

Moreover, the attractiveness of our coastal markets continues to draw new residents and visitors despite the struggling economy. Combined, these factors give us confidence that we are “Prepared for Opportunity” – both in our capacity to overcome near-term market hurdles and in our ability to take advantage of the eventual recovery of the economy.

2008 Financial Performance

We certainly experienced our share of difficulties in 2008. While it is true that we did not participate in any subprime or other risky lending practices that ensnared many other institutions, we did have a considerable concentration of loans in the real estate market, which is the primary source of the challenges we now face.

Our participation in real estate lending in recent years was an effort to be good stewards and supporters of the people and small businesses in our local communities. We made sound loans to creditworthy borrowers who had adequate collateral and solid financial backgrounds.

Unfortunately, even our best construction and real estate development customers could not withstand the collapse of the housing market. We quickly began to curtail lending in this sector when we saw signs of the housing market downturn. However, the market sank much faster than we could react.

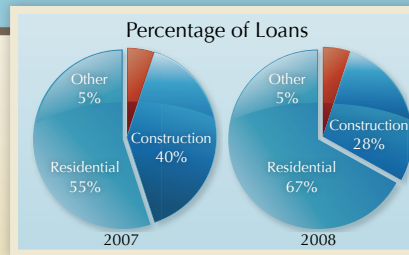
As time passed and the recession deepened, our nonaccrual loans and other real estate owned began to increase substantially. In 2008, the rise in problem loans caused us to significantly raise our provision for loan losses. This negated the growth we generated in loans, deposits and wholesale lending, leaving us with a cumulative loss for the year.

Overall, our financial performance in 2008 included:

- Net loss totaling \$4.8 million;
- Loss per share of \$1.91;
- Total assets of \$476.8 million;
- Net interest income of \$10.1 million, and noninterest income of \$5.1 million;
- Net interest margin of 2.52 percent;
- Net charge-offs as a percentage of total loans of 2.18 percent, nonaccrual loans as a percentage of total loans of 5.98 percent, and allowance for loan losses of \$4.8 million, or 1.59 percent of loans outstanding.

Our task was not made any easier by the Fed’s rate cuts in 2008. At the end of the year, the Fed Funds rate was at its lowest point in history: targeted at 0 to .25 percent.

I cannot overstate the detrimental impact these low rates have had on the ability of all community banks, including ours,



to generate interest income. Net interest margins essentially have been suffocated, and relief is not likely to come until the Fed reverses course and begins to raise rates.

On a brighter note, we were able to make good headway in reducing the concentration of construction lending in our loan portfolio, which in turn reduced the amount of risk we carried. At the same time, we increased the percentage of permanent financing lending, such as residential real estate mortgages, as these types of loans are performing better than construction loans in the current market.

In fact, our wholesale mortgage division was a particularly bright spot for our company in 2008. The lending unit originated \$473.2 million in loans available for sale during the year, the vast majority of which were full-documentation, conforming mortgage loans that were pre-sold into the secondary market, which eliminated nearly all interest-rate risk.

Another significant development in 2008 was our ability to maintain strong capital ratios at both the bank and the holding company. These ratios, which were consistently and significantly above the “well-capitalized” threshold as designated by Federal regulators, are a byproduct of the quality of retained earnings we have generated over the years.

We bolstered our already strong capital position in December when we received \$9.95 million from the U.S. Treasury Department’s TARP Capital Purchase Program. Let me be clear that the funds are not a hand-out. Rather, it is an investment in our bank that we must pay back over time, with interest.

Though we were already well-capitalized, we participated in the program for two simple reasons: one, it allows us to better serve our customers and have a greater impact in our local markets by increasing lending activity; and two, it is a low-cost form of insurance against a prolonged economic downturn.

The TARP has come under considerable scrutiny regarding how the public funding is being utilized by banks. As good stewards of taxpayer financing, it is our firm belief that the most responsible use for this capital is residential mortgage lending. Many experts believe that improving the housing market is the key to economic recovery, and we are committed to doing our part to help the communities we serve.

That is why we funded more than \$130 million of new residential mortgage loans in December 2008 and January 2009 alone, which is an increase of more than 60 percent in average monthly loan originations when compared to the first 11 months of 2008, before we received the TARP investment. Because we are operating from a strong capital position, we can fully leverage the TARP to support our local communities.

A Bumpy 2009

In last year’s annual report, we told you that our most important near-term priorities were stringent adherence to sound credit management policies, controlling past-due loans, quickly resolving credit issues and remaining adequately capitalized.

Though there is still much heavy lifting to be done, we are making great progress toward achieving those objectives, and they remain our focus for 2009. Fortunately, we enter the new year comfortable that we are ahead of the curve in terms of having reserves set aside for nonperforming assets. This is crucial as we don’t anticipate much, if any, improvement in our markets or the overall economy.

We also will continue to search out strategic growth opportunities along the coasts of Florida, Georgia and South Carolina, whether they are merger and acquisition or de novo branching prospects. The fact remains that we operate in attractive markets, and the upheaval in the banking industry is producing some worthwhile opportunities to grow our franchise for the future.

As a shareholder of a community bank, these surely are trying times for you. While I don’t want to minimize the challenges that we face, I hope you will join in my belief, confidence and optimism that we are Prepared for Opportunity and that our best days as a company and an investment are ahead of us.

We greatly appreciate your support.

Sincerely,

Michael G. Sanchez
Chief Executive Officer



Opportunity

The attractiveness of our coastal markets continues to draw tourists and new residents despite the economy. In addition, several important accomplishments in 2008 – continued strong capital ratios and ample liquidity, the consolidation of our separate bank charters, and the ongoing strong performance of our wholesale lending division – make us optimistic looking ahead to 2009 and beyond. In both our ability to overcome market difficulties and to take advantage of the eventual recovery of the economy, we are *Prepared for Opportunity*.



Prepared for Opportunity

Strengthened Capital

Charter Consolidation

Wholesale Lending

Strengthened Capital

Capital has become the lifeblood of today's banking market – the essential building block for near- and long-term success in a struggling economy.

Indeed, many who follow the banking industry today are more concerned about capital reserves than they are about income, earnings or assets. The more capital a bank has, the better its prospects for surviving the recession and taking advantage of the eventual economic recovery.

Federal regulators use the ratio of capital to risk-weighted assets as a key factor in evaluating a bank's health. They focus primarily on a bank's total risk-based capital ratio and its Tier 1 capital ratio (a measurement of a bank's "core capital" that is defined as equity capital plus disclosed reserves).

Regulators consider a bank to be "well-capitalized" when it has a total risk-based capital ratio of at least 10% and a Tier 1 capital ratio of at least 6%.

By both measures, Coastal Banking Company is faring quite well. Despite increasing our loan-loss reserves substantially during 2008, our subsidiary bank ended the year with a total risk-based capital ratio of 14.28% and a Tier 1 risk-based capital ratio of 13.03% – both considerably above the respective well-capitalized thresholds as defined by federal regulators. Our holding company also ended 2008 well-capitalized, with a total risk based capital ratio of 16.10% and Tier 1 risk-based capital ratio of 14.85%.

We strengthened our capital position in the fourth quarter of 2008 through a \$9.95 million investment from the TARP Capital Purchase Program. The TARP is the U.S. Treasury Department's effort to spark economic growth by improving financial institutions' ability to lend money

to businesses and consumers. We were one of only four Florida-based banks approved for the TARP investment.

As you can see in the chart below, the capital position at our CBC National Bank subsidiary was solid even before we received the TARP investment; it became even stronger after the infusion. The additional funding is helping us support our local communities through increased lending efforts.

CBC National Bank Capital Measurements	Pre-TARP capital ratios 9/30/2008	Post-TARP capital ratios 12/31/2008	Threshold for "well-capitalized" designation by Federal regulators
Total risk-based capital ratio	13.50%	14.28%	10.0%
Tier 1 risk-based capital ratio	12.25%	13.03%	6.0%
Tier 1 leverage ratio	9.43%	9.62%	5.0%

The Quality of Capital

Not only is the amount of a bank's capital holdings important, but also the quality of its capital.

Over the past several years, many community banks have turned to wholesale funding sources, such as brokered deposits, to boost capital. Brokered deposits typically are CDs owned by customers of a brokerage firm, which pools investor funds and places them with banks for a fee.

The benefit of such deposits for small banks is that it is much easier and cheaper to simply purchase them from a broker than to mount an expensive and time-consuming marketing campaign to generate core deposits from local customers.

The disadvantage is that brokered deposits can be unstable and historically have been more expensive as they typically offer higher rates than other bank products. Most CD holders are driven solely by yield. Once the

We were successful in decreasing our holdings of brokered deposits to 8 percent of our total deposits by the end of 2008, while increasing growth in more permanent core and municipal deposits.



certificates reach maturity, many customers are quick to leave with their money, chasing higher returns.

Having too high a concentration of brokered deposits in a portfolio invites undue risk. That is why it is vital that banks have other stable sources of liquidity to balance out their portfolios.

We set out to reduce our reliance on wholesale funding in 2008, and established an internal target of limiting our brokered CDs to no more than 10% of total assets. We were successful in decreasing our holdings of brokered deposits to 8% of our total deposits by the end of 2008, while increasing growth in more permanent core and municipal deposits.

In the fourth quarter, rates for brokered CDs actually declined to as much as 1% lower than comparable retail deposit rates as a result of the Fed cutting interest rates to historic lows. Given the frenzied competition among banks for retail deposits, we actually increased our

holdings of these lower cost brokered CDs rather than get into a costly bidding war for retail deposits.

This short-term strategy gave us a significantly lower cost alternative to retail deposits and still kept brokered deposits below our targeted percentage of total assets at the end of 2008.

In addition to improving the quality of our assets, we ended 2008 with \$88.2 million in available funding from a variety of sources. This is a significant increase from the \$63.4 million available to us at the start of the year.

This funding improves our ability both to withstand the effects of a prolonged economic downturn and take advantage of strategic growth opportunities that may arise.

Taken together, our capitalization and available funding are a reflection of our fiscal health and strength, and proof that we are *Prepared for Opportunity*.

Prepared for Opportunity

Strengthened Capital

Charter Consolidation

Wholesale Lending



In 2008, we consolidated our separate bank charters into one, under the name CBC National Bank.



Charter Consolidation

Coastal Banking Company is a stronger organization today than a year ago.

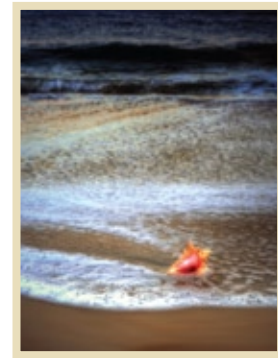
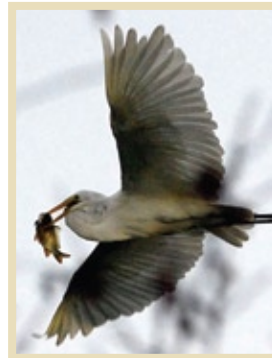
This achievement is the culmination of what began almost four years ago with the merger of Coastal Banking Company in Beaufort, S.C., and First Capital Bank Holding Corp. in Fernandina Beach, Fla.

The merger brought together two nationally chartered banks that were home to talented employees, valuable markets and a conservative, customer-focused approach to community banking. Our mission was to mold the separate organizations into a single, unified institution.

We have worked tirelessly in this effort over the past several years. In last year's annual report, we reported success in uniting our two company cultures in a cohesive team focused on delivering the best products and services to our customers.

In 2008, we consolidated our separate bank charters into one, under the name CBC National Bank, with headquarters in Fernandina Beach. As a result, our operations have become much more efficient and cost-effective.

We reaped near-instantaneous cost savings from the elimination of numerous fees and expenses related to overlapping regulatory reporting and examinations. Also, by merging our back-office operations and combining our separate data operations into one location, we realized economies of scale by reducing our cost of doing business.



Streamlining our operations has freed up valuable capital that we now can use as a buffer against the ongoing difficulties caused by the recession, while taking advantage of any strategic growth opportunities that arise, whether mergers, acquisitions or de novo branching.

Our customers also have benefited from the consolidation. They now can transact any of their banking business at any branch in our three-state network.

Eventually, we will complete the transition from our three operating divisions – Lowcountry National Bank, First National Bank of Nassau County and The Georgia Bank – to a unified identity under the name CBC National Bank.

As we make this transition, we will continue to improve our operations in the best interests of our customers, shareholders and employees.

Prepared for Opportunity

Strengthened Capital

Charter Consolidation

Wholesale Lending

Wholesale Lending

Key to being *Prepared for Opportunity* in today's challenging economic climate is the ability to generate the revenue necessary to fund the bank's operational and strategic growth initiatives.

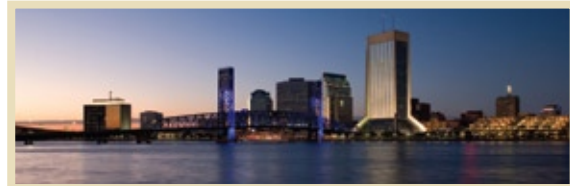
In 2007, we seized upon the chance to create a valuable source of noninterest income by forming a wholesale mortgage lending division, taking advantage of a market largely abandoned by major banks.

The result so far has been an unqualified success.

Since starting operations, our wholesale mortgage lending unit has far exceeded our performance expectations in both loan volume and profitability. We originated \$473.2 million in loans for sale in the secondary market in 2008, and the pipeline for the first quarter of 2009 was quite strong.

The value of this revenue stream is even greater when you consider today's record low interest-rate environment. As with most community banks, interest income comprises the lion's share of our total income. Net interest margins remain squeezed across the industry, and ours is no exception. Having a steady source of noninterest income from our wholesale mortgage division is an invaluable buffer against what will remain an uncertain interest-rate environment in 2009.

What's more, we entered the wholesale mortgage market without any prior risk exposure and implemented a conservative loan product strategy. We limited our offerings primarily to fully documented, fully amortizing loans with a strict lending limit. These loans are pre-sold



- We originated \$473.2 million in loans for sale in the secondary market in 2008.
- The pipeline for wholesale lending in the first quarter of 2009 was quite strong.
- We expanded our wholesale product line to include FHA mortgages.

into the secondary market, virtually eliminating any interest-rate risk.

We expanded our wholesale mortgage lending product line in August 2008 to include FHA mortgages, a key loan program that strives to ensure that the benefits of home ownership are available to as many qualified borrowers as possible. We believe our participation in this program is essential to meeting the housing needs of the communities we serve.

Our volume of FHA lending has grown steadily since we first introduced it, and by December 2008, FHA loans represented 18% of all loans funded.

As we move into 2009, our focus is on building upon our early success in wholesale lending and better positioning our company to seize upon strategic growth opportunities.



Opportunity

“We operate in attractive markets. Our capital position remains strong, and we have ample liquidity. Our organization is streamlined. Our wholesale lending division continues to exceed expectations. I hope that you share in my belief, confidence and optimism that our best days as a company and an investment are ahead of us. We are *Prepared for Opportunity* as we work our way through the current market difficulties and consider worthwhile opportunities to grow our franchise for the future.”

– Michael G. Sanchez, CEO

Directors and Committees

Christina H. Bryan

Co-Owner of various businesses

Suellen Rodeffer Garner, Chairman

Orthodontist; Co-Owner Suellen Rodeffer and David Garner D.D.S., P.A.

Dennis O. Green, CPA

Managing Member, Celadon, LLC

Mark B. Heles

President of H&H Quality Properties, LLC

James W. Holden, Jr., DVM, Secretary

Owner, Director of Holly Hall Animal Hospital

Ladson F. Howell, Vice Chairman

Retired Attorney, Howell, Gibson & Hughes, P.A.

James C. Key

Partner, Shenandoah Group, LLP

Robert B. Pinkerton

President & CEO, Athena Corporation

Michael G. Sanchez

President and CEO of Coastal Banking Company, and President and CEO of CBC National Bank

Edward E. Wilson

Licensed Insurance Agent

Marshall E. Wood

Attorney, Marshall E. Wood, P.A.

Audit and Compliance

Dennis O. Green, CPA, Chairman

Christina H. Bryan

James C. Key

Edward E. Wilson

Marshall E. Wood

Executive Compensation and Management Resources

Edward E. Wilson, Chairman

Christina H. Bryan

Mark Heles

Robert B. Pinkerton

Corporate Governance and Nominating

James W. Holden, Jr., DVM, Chairman

Dennis O. Green, CPA

Ladson F. Howell

James C. Key

