CAPITAL CITY BANK GROUP INC
Form 10-K
March 05, 2019

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-K

[X]	**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934** **For the fiscal year ended December 31, 2018** **OR**
[ ]	**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934** **For the transition period from ____________ to ____________**

(Exact name of Registrant as specified in its charter)

Florida	**0-13358**	**59-2273542**
(State of Incorporation)	(Commission File Number)	(IRS Employer Identification No.)

217 North Monroe Street, Tallahassee, Florida	**32301**
(Address of principal executive offices)	(Zip Code)

(850) 402-7821

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, $0.01 par value	The Nasdaq Stock Market LLC

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes [ ] No [X]

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes [ ] No [X]

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 [X] 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 [X] No [ ]

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [X]

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 definition of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act

Large accelerated filer [ ] Accelerated filer [X] Non-accelerated filer [ ]
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 [X]

The aggregate market value of the registrant's common stock, $0.01 par value per share, held by non-affiliates of the registrant on June 30, 2018, the last business day of the registrant's most recently completed second fiscal quarter, was approximately $270,798,560 (based on the closing sales price of the registrant's common stock on that date). Shares of the registrant's common stock held by each officer and director and each person known to the registrant to own 10% or more of the outstanding voting power of the registrant have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not a determination for other purposes.

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at February 28, 2019
Common Stock, $0.01 par value per share	16,807,883

DOCUMENTS INCORPORATED BY REFERENCE

Portions of our Proxy Statement for the Annual Meeting of Shareowners to be held on April 23, 2019, are incorporated by reference in Part III.

CAPITAL CITY BANK GROUP, INC.

ANNUAL REPORT FOR 2018 ON FORM 10-K

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INTRODUCTORY NOTE

This Annual Report on Form 10-K 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,” “vision,” “goal,” and similar expre 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.

In addition to those risks discussed in this Annual Report under Item 1A Risk Factors, factors that could cause our actual results to differ materially from those in the forward-looking statements, include, without limitation:

- our ability to successfully manage interest rate risk, liquidity risk, and other risks inherent to our industry;
- legislative or regulatory changes;
- the effects of security breaches and computer viruses that may affect our computer systems or fraud related to our debit card products;
- the accuracy of our financial statement estimates and assumptions, including the estimates used for our loan loss reserve and deferred tax asset valuation allowance and pension plan;
- changes in accounting principles, policies, practices or guidelines, including the effects of forthcoming CECL implementation;
- the frequency and magnitude of foreclosure of our loans;
- the effects of our lack of a diversified loan portfolio, including the risks of geographic and industry concentrations;
- the strength of the United States economy in general and the strength of the local economies in which we conduct operations;
- our ability to declare and pay dividends, the payment of which is subject to our capital requirements;
- changes in the securities and real estate markets;

- changes in monetary and fiscal policies of the U.S. Government;
- inflation, interest rate, market and monetary fluctuations;
- 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, including the laws for each jurisdiction where we operate;
- the willingness of clients to accept third-party products and services rather than our products and services and vice versa;
- increased competition and its effect on pricing;
- technological changes;
- negative publicity and the impact on our reputation;
- changes in consumer spending and saving habits;
- growth and profitability of our noninterest income;
- 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;
- 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 listed in *Item 1A Risk Factors* or discussed in this 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.

PART I

Item 1. Business

About Us

General

Capital City Bank Group, Inc. (“CCBG”) is a financial holding company headquartered in Tallahassee, Florida. CCBG was incorporated under Florida law on December 13, 1982, to acquire five national banks and one state bank that all subsequently became part of CCBG’s bank subsidiary, Capital City Bank (“CCB” or the “Bank”). The Bank commenced operations in 1895. In this report, the terms “Company,” “we,” “us,” or “our” mean CCBG and all subsidiaries included in our consolidated financial statements.

We provide traditional deposit and credit services, asset management, trust, mortgage banking, merchant services, bank cards, data processing, and securities brokerage services through 59 banking offices in Florida, Georgia, and Alabama operated by CCB. The majority of our revenue, approximately 88%, is derived from our Florida market areas while approximately 11% and 1% of our revenue is derived from our Georgia and Alabama market areas, respectively.

Below is a summary of our financial condition and results of operations for the past three years. Our financial condition and results of operations are more fully discussed in our management discussion and analysis on page 32 and our consolidated financial statements on page 64.

Dollars in millions

Year Ended December 31,	Assets	Deposits	Shareowners’ Equity	Revenue[(1)]	Net Income
2018	$2,959.2	$2,531.9	$302.6	$151.0	$26.2
2017	$2,898.8	$2,469.9	$284.2	$138.7	$10.9
2016	$2,845.2	$2,412.3	$275.2	$134.8	$11.7

[(1)]Revenue represents interest income plus noninterest income

Dividends and management fees received from the Bank are CCBG’s primary source of income. Dividend payments by the Bank to CCBG depend on the capitalization, earnings and projected growth of the Bank, and are limited by various regulatory restrictions, including compliance with a minimum Common Equity Tier 1 Capital conservation buffer. See the section entitled “Regulatory Matters” in this *Item 1* and Note 14 in the Notes to Consolidated Financial

Statements for a discussion of the restrictions.

We had a total of 819 associates at March 1, 2019. Item 6 contains other financial and statistical information about us.

Subsidiaries of CCBG

CCBG's principal asset is the capital stock of CCB, our wholly owned banking subsidiary, which accounted for nearly 100% of consolidated assets at December 31, 2018, and approximately 100% of consolidated net income for the year ended December 31, 2018. In addition to our banking subsidiary, CCB has two primary subsidiaries, which are wholly owned, Capital City Trust Company and Capital City Investments, Inc. The nature of these subsidiaries is provided below.

Operating Segment

We have one reportable segment with three principal services: Banking Services (CCB), Trust and Asset Management Services (Capital City Trust Company), and Brokerage Services (Capital City Investments, Inc.). Revenues from each of these principal services for the year ended 2018 totaled approximately 95.6%, 3.8%, and 2.5% of our total revenue, respectively. In 2017 and 2016, Banking Services (CCB) revenue was approximately 93.6% and 93.7% of our total revenue for each respective year.

Capital City Bank

CCB is a Florida-chartered full-service bank engaged in the commercial and retail banking business. Significant services offered by CCB include:

- *Business Banking* – We provide banking services to corporations and other business clients. Credit products are available for a wide variety of general business purposes, including financing for commercial business properties, equipment, inventories and accounts receivable, as well as commercial leasing and letters of credit. We also provide treasury management services, and, through a marketing alliance with Elavon, Inc., merchant credit card transaction processing services.

- *Commercial Real Estate Lending* – We provide a wide range of products to meet the financing needs of commercial developers and investors, residential builders and developers, and community development. Credit products are available to purchase land and build structures for business use and for investors who are developing residential or commercial property.

- *Residential Real Estate Lending* – We provide products to help meet the home financing needs of consumers, including conventional permanent and construction/ permanent (fixed, adjustable, or variable rate) financing arrangements, and FHA/VA loan products. We offer both fixed-rate and adjustable-rate residential mortgage (ARM) loans. A portion of our loans originated are sold into the secondary market. We offer these products through our existing network of banking offices. We do not originate subprime residential real estate loans.

- *Retail Credit* – We provide a full-range of loan products to meet the needs of consumers, including personal loans, automobile loans, boat/RV loans, home equity loans, and through a marketing alliance with ELAN, we offer credit card programs.

- *Institutional Banking* – We provide banking services to meet the needs of state and local governments, public schools and colleges, charities, membership and not-for-profit associations including customized checking and savings accounts, cash management systems, tax-exempt loans, lines of credit, and term loans.

- *Retail Banking* – We provide a full-range of consumer banking services, including checking accounts, savings programs, automated teller machines (ITMs/ATMs), debit/credit cards, night deposit services, safe deposit facilities, online banking, and mobile banking.

Capital City Trust Company

Capital City Trust Company (the "Trust Company"). The Trust Company provides asset management for individuals through agency, personal trust, IRA, and personal investment management accounts. Associations, endowments, and other nonprofit entities hire the Trust Company to manage their investment portfolios. Additionally, a staff of well-trained professionals serves individuals requiring the services of a trustee, personal representative, or a guardian. The market value of trust assets under discretionary management exceeded $760.2 million at December 31, 2018, with total assets under administration exceeding $831.2 million.

Capital City Investments, Inc.

We offer our customers access to retail investment products through LPL Financial pursuant to which retail investment products would be offered through LPL. LPL offers a full line of retail securities products, including U.S. Government bonds, tax-free municipal bonds, stocks, mutual funds, unit investment trusts, annuities, life insurance and long-term health care. Non-deposit investment and insurance products are: (i) not FDIC insured; (ii) not deposits, obligations, or guarantees by any bank; and (iii) subject to investment risk, including the possible loss of principal amount invested. We are not an affiliate of LPL Financial.

Underwriting Standards

One of our core goals is to support the communities in which we operate. We seek loans from within our primary market area, which is defined as the counties in which our banking offices are located. We will also originate loans within our secondary market area, defined as counties adjacent to those in which we have banking offices. There may also be occasions when we will have opportunities to make loans that are out of both the primary and secondary market areas, including participation loans. These loans are generally only approved if the applicant is known to us, underwriting is consistent with our criteria, and the applicant's primary business is in or near our primary or secondary market area. Approval of all loans is subject to our policies and standards described in more detail below.

We have adopted comprehensive lending policies, underwriting standards and loan review procedures. Management and our Board of Directors reviews and approves these policies and procedures on a regular basis (at least annually).

Management has also implemented reporting systems designed to monitor loan originations, loan quality, concentrations of credit, loan delinquencies, nonperforming loans, and potential problem loans. Our management and the Credit Risk Oversight Committee periodically review our lines of business to monitor asset quality trends and the appropriateness of credit policies. In addition, total borrower exposure limits are established and concentration risk is monitored. As part of this process, the overall composition of the portfolio is reviewed to gauge diversification of risk, client concentrations, industry group, loan type, geographic area, or other relevant classifications of loans. Specific segments of the portfolio are monitored and reported to our Board on a quarterly basis and we have strategic plans in place to supplement Board approved credit policies governing exposure limits and underwriting standards. We recognize that exceptions to the below-listed policy guidelines may occasionally occur and has established procedures for approving exceptions to these policy guidelines.

Residential Real Estate Loans

We originate 1-4 family, owner-occupied residential real estate loans in its Residential Real Estate line of business. Our policy is to underwrite these loans in accordance with secondary market guidelines in effect at the time of origination, including loan-to-value ("LTV") and documentation requirements. We originate fixed-rate, adjustable-rate and variable- rate residential real estate loans. Over the past five years, the vast majority of residential loan originations have been fixed-rate loans which are sold in the secondary market on a non-recourse basis with related servicing rights (i.e., we generally do not service sold loans). Adjustable rate mortgage ("ARM") loans with an initial fixed interest rate period greater than five years are also sold in the secondary market on a non-recourse basis.

We also originate certain residential real estate loans throughout our banking office network that are generally not eligible for sale into the secondary market due to not meeting a specific secondary market underwriting requirement. This includes our variable rate 3/1 and 5/1 ARM loans which typically have a maximum term of 30 years and maximum LTV of 80%.

Residential real estate loans also include home equity lines of credit ("HELOCs") and home equity loans. Our home equity portfolio includes revolving open-ended equity loans with interest-only or minimal monthly principal payments and closed-end amortizing loans. Open-ended equity loans typically have an interest only 10-year draw period followed by a five year repayment period of 0.75% of principal balance monthly and balloon payment at maturity. As of December 31, 2018, approximately 66% of our residential home equity loan portfolio consisted of first mortgages. Interest rates may be fixed or adjustable. Adjustable-rate loans are tied to the Prime Rate with a typical margin of 1.0% or more.

Commercial Loans

Our policy sets forth guidelines for debt service coverage ratios, LTV ratios and documentation standards. Commercial loans are primarily made based on identified cash flows of the borrower with consideration given to underlying collateral and personal or other guarantees. We have established debt service coverage ratio limits that require a borrower's cash flow to be sufficient to cover principal and interest payments on all new and existing debt. The majority of our commercial loans are secured by the assets being financed or other business assets such as accounts receivable or inventory. Many of the loans in the commercial portfolio have variable interest rates tied to the Prime Rate or U.S. Treasury indices.

Commercial Real Estate Loans

We have adopted guidelines for debt service coverage ratios, LTV ratios and documentation standards for commercial real estate loans. These loans are primarily made based on identified cash flows of the borrower with consideration given to underlying real estate collateral and personal guarantees. Our policy establishes a maximum LTV specific to property type and minimum debt service coverage ratio limits that require a borrower's cash flow to be sufficient to cover principal and interest payments on all new and existing debt. Commercial real estate loans may be fixed or variable-rate loans with interest rates tied to the Prime Rate or U.S. Treasury indices. We require appraisals for loans in excess of $250,000 that are secured by real property.

Consumer Loans

Our consumer loan portfolio includes personal installment loans, direct and indirect automobile financing, and overdraft lines of credit. The majority of the consumer loan portfolio consists of indirect and direct automobile loans. The majority of our consumer loans are short-term and have fixed rates of interest that are priced based on current market interest rates and the financial strength of the borrower. Our policy establishes maximum debt-to-income ratios, minimum credit scores, and includes guidelines for verification of applicants' income and receipt of credit reports.

Lending Limits and Extensions of Additional Credit

We have established an internal lending limit of $10 million for the total aggregate amount of credit that will be extended to a client and any related entities within our Board approved policies. This compares to our legal lending limit of approximately $86 million.

Loan Modification and Restructuring

In the normal course of business, we receive requests from our clients to renew, extend, refinance, or otherwise modify their current loan obligations. In most cases, this may be the result of a balloon maturity that is common in most commercial loan agreements, a request to refinance to obtain current market rates of interest, competitive reasons, or the conversion of a construction loan to a permanent financing structure at the completion or stabilization of the property. In these cases, the request is held to the normal underwriting standards and pricing strategies as any other loan request, whether new or renewal.

In other cases, we may modify a loan because of a reduction in debt service capacity experienced by the client (i.e., a potentially troubled loan whereby the client may be experiencing financial difficulties). To maximize the collection of loan balances, we evaluate troubled loans on a case-by-case basis to determine if a loan modification would be appropriate. We pursue loan modifications when there is a reasonable chance that an appropriate modification would allow our client to continue servicing the debt.

Expansion of Business

Our philosophy is to build long-term client relationships based on quality service, high ethical standards, and safe and sound banking practices. We maintain a locally oriented, community-based focus, which is augmented by experienced, centralized support in select specialized areas. Our local market orientation is reflected in our network of banking office locations, experienced community executives with a dedicated President for each market, and community boards which support our focus on responding to local banking needs. We strive to offer a broad array of sophisticated products and to provide quality service by empowering associates to make decisions in their local markets.

We have sought to build a franchise in small-to medium-sized, less competitive markets, located on the outskirts of the larger metropolitan markets where we are positioned as a market leader. Many of our markets are on the outskirts of these larger markets in close proximity to major interstate thoroughfares such as Interstates I-10 and I-75. Our three largest markets are Tallahassee (Leon County, Florida), Gainesville (Alachua County, Florida), and Macon

(Bibb County, Georgia). In 13 of 18 markets in Florida and two of four markets in Georgia, we rank within the top four banks in terms of market share. Furthermore, in the counties in which we operate, we maintain a 8.30% market share in the Florida counties and 5.11% in the Georgia counties, suggesting that there is significant opportunity to grow market share within these geographic areas. The larger employers in many of our markets are state and local governments, healthcare providers, educational institutions, and small businesses. While we realize that the markets in our footprint do not provide for a level of potential growth that the larger metropolitan markets may provide, our markets do provide good growth dynamics and have historically grown in excess of the national average The value of these markets stems from the fact they are stable and less competitive, secondary markets. We strive to provide value added services to our clients by being not just their bank, but their banker. This element of our strategy distinguishes Capital City Bank from our competitors.

Our long-term vision remains to profitably expand our franchise through a combination of organic growth in existing markets and acquisitions. We have long understood that our core deposit funding base is a predominant driver of our profitability and overall franchise value, and have focused extensively on this component of our organic growth efforts in recent years. While we have not been an active acquirer of banks since 2005, this component of our strategy is still in place. When evaluating potential acquisition opportunities, we will continue to weigh the value of organic growth initiatives versus potential acquisition returns and pursue the strategies that we believe provide the best overall return to our shareowners.

Potential acquisition opportunities will continue to be focused on Florida, Georgia, and Alabama with a particular focus on financial institutions located on the outskirts of larger, metropolitan areas. Five markets have been identified, four in Florida and one in Georgia, in which management intends to proactively pursue expansion opportunities. These markets include Alachua, Marion, Hernando/Pasco counties in Florida, the western panhandle of Florida, and Bibb and surrounding counties in central Georgia. Our focus on some of these markets may change as we continue to evaluate our strategy and the economic conditions and demographics of any individual market. We will also continue to evaluate de novo expansion opportunities in attractive new markets in the event that acquisition opportunities are not feasible. Other expansion opportunities that will be evaluated include asset management, mortgage banking, and other financial businesses that are closely aligned with the business of banking. Embedded in our acquisition strategy is our desire to partner with institutions that are culturally similar, have experienced management and possess either established market presence or have potential for improved profitability through growth, economies of scale, or expanded services. Generally, these target institutions will range in asset size from $100 million to $500 million.

Competition

We operate in a highly competitive environment, especially with respect to services and pricing, that has undergone significant changes since the recent financial crisis. Since January 1, 2009, over 500 financial institutions have failed in the U.S., including 85 in Georgia and 70 in Florida. Nearly all of the failed banks were community banks. The assets and deposits of many of these failed community banks were acquired mostly by larger financial institutions. The banking industry has also experienced significant consolidation through mergers and acquisition, which we expect will continue during 2019. However, we believe that the larger financial institutions acquiring banks in our market areas are less familiar with the markets in which we operate and typically target a different client base. We also believe clients who bank at community banks tend to prefer the relationship style service of community banks compared to larger banks.

As a result, we expect to be able to effectively compete in our markets with larger financial institutions through providing superior customer service and leveraging our knowledge and experience in providing banking products and services in our market areas. Thus, a further reduction of the number of community banks could continue to enhance our competitive position and opportunities in many of our markets. However, larger financial institutions can benefit from economies of scale, so these larger institutions may be able to offer banking products and services at more competitive price. Additionally, these larger financial institutions may offer financial products that we do not offer.

We may also begin to see competition from new banks that are being formed. In late 2016, the first *de novo* bank charter since the downturn was approved for a Florida-based bank and three additional Florida charters were approved in 2018. While the number of new bank formations has not returned to pre-downturn levels, increased *de novo* bank applications could signal additional competition from new community banks.

Our primary market area consists of 18 counties in Florida, four counties in Georgia, and one county in Alabama. In these markets, we compete against a wide range of banking and nonbanking institutions including banks, savings and loan associations, credit unions, money market funds, mutual fund advisory companies, mortgage banking companies, investment banking companies, finance companies and other types of financial institutions. Most of Florida's major banking concerns have a presence in Leon County, where our main office is located. Our Leon County deposits totaled $983 million, or 39% of our consolidated deposits at December 31, 2018.

The table below depicts our market share percentage within each county, based on commercial bank deposits within the county.

County	Market Share as of June 30,[1]		
	2018	2017	2016
Florida			
Alachua	4.7%	4.9%	4.9%
Bradford	41.9%	42.5%	46.1%
Citrus	3.4%	3.5%	3.5%
Clay	2.1%	2.2%	1.9%
Dixie	20.8%	22.1%	15.2%
Gadsden	79.6%	78.9%	77.7%
Gilchrist	46.3%	44.4%	46.8%
Gulf	14.8%	16.4%	15.5%
Hernando	2.5%	2.3%	2.1%
Jefferson	19.7%	21.9%	22.5%
Leon	12.8%	12.5%	13.9%
Levy	26.8%	28.3%	29.2%
Madison	13.6%	14.9%	14.2%
Putnam	22.0%	20.8%	21.3%
St. Johns	0.8%	0.7%	0.8%
Suwannee	7.4%	7.8%	7.6%
Taylor	23.5%	19.7%	18.0%
Wakulla	8.9%	14.2%	14.5%
Washington	12.0%	14.1%	14.2%
Georgia			
Bibb	2.9%	3.2%	3.2%
Grady	14.2%	13.7%	13.4%
Laurens	8.6%	9.3%	9.3%
Troup	5.5%	5.9%	5.4%
Alabama			
Chambers	9.2%	9.1%	9.2%

[1] *Obtained from the FDIC Summary of Deposits Report for the year indicated.*

The following table sets forth the number of commercial banks and offices, including our offices and our competitor's offices,
within each of the respective counties.

County	Number of Commercial Banks	Number of Commercial Bank Offices
Florida		
Alachua	18	63
Bradford	3	3
Citrus	12	39
Clay	12	28
Dixie	3	4
Gadsden	2	3
Gilchrist	4	6
Gulf	3	4
Hernando	13	34
Jefferson	2	2
Leon	18	76
Levy	2	11
Madison	3	3
Putnam	5	10
St. Johns	19	62
Suwannee	5	8
Taylor	3	4
Wakulla	4	4
Washington	6	6
Georgia		
Bibb	13	39
Grady	5	7
Laurens	10	19
Troup	11	20
Alabama		
Chambers	6	8

Data obtained from the FDIC June 30, 2018 Summary of Deposits Report.

Seasonality

We believe our commercial banking operations are not generally seasonal in nature; however, public deposits tend to increase with tax collections in the fourth and first quarters of each year and decline as a result of governmental spending thereafter.

Regulatory Considerations

We must comply with state and federal banking laws and regulations that control virtually all aspects of our operations. These laws and regulations generally aim to protect our depositors, not necessarily our shareowners or our creditors. Any changes in applicable laws or regulations may materially affect our business and prospects. Proposed legislative or regulatory changes may also affect our operations. The following description summarizes some of the laws and regulations to which we are subject. References to applicable statutes and regulations are brief summaries, do not purport to be complete, and are qualified in their entirety by reference to such statutes and regulations.

Capital City Bank Group, Inc.

We are registered with the Board of Governors of the Federal Reserve as a financial holding company under the Bank Holding Company Act of 1956. As a result, we are subject to supervisory regulation and examination by the Federal Reserve. The Gramm-Leach-Bliley Act, the Bank Holding Company Act, and other federal laws subject financial holding companies to particular restrictions on the types of activities in which they may engage, and to a range of supervisory requirements and activities, including regulatory enforcement actions for violations of laws and regulations.

Permitted Activities

The Gramm-Leach-Bliley Act modernized the U.S. banking system by: (i) allowing bank holding companies that qualify as “financial holding companies,” such as CCBG, to engage in a broad range of financial and related activities; (ii) allowing insurers and other financial service companies to acquire banks; (iii) removing restrictions that applied to bank holding company ownership of securities firms and mutual fund advisory companies; and (iv) establishing the overall regulatory scheme applicable to bank holding companies that also engage in insurance and securities operations. The general effect of the law was to establish a comprehensive framework to permit affiliations among commercial banks, insurance companies, securities firms, and other financial service providers. Activities that are financial in nature are broadly defined to include not only banking, insurance, and securities activities, but also merchant banking and additional activities that the Federal Reserve, in consultation with the Secretary of the Treasury, determines to be financial in nature, incidental to such financial activities, or complementary activities that do not pose a substantial risk to the safety and soundness of depository institutions or the financial system generally.

In contrast to financial holding companies, bank holding companies are limited to managing or controlling banks, furnishing services to or performing services for its subsidiaries, and engaging in other activities that the Federal Reserve determines by regulation or order to be so closely related to banking or managing or controlling banks as to be a proper incident thereto. In determining whether a particular activity is permissible, the Federal Reserve must consider whether the performance of such an activity reasonably can be expected to produce benefits to the public that outweigh possible adverse effects. Possible benefits include greater convenience, increased competition, and gains in

efficiency. Possible adverse effects include undue concentration of resources, decreased or unfair competition, conflicts of interest, and unsound banking practices. Despite prior approval, the Federal Reserve may order a bank holding company or its subsidiaries to terminate any activity or to terminate ownership or control of any subsidiary when the Federal Reserve has reasonable cause to believe that a serious risk to the financial safety, soundness or stability of any bank subsidiary of that bank holding company may result from such an activity.

Changes in Control

Subject to certain exceptions, the Bank Holding Company Act and the Change in Bank Control Act, together with the applicable regulations, require Federal Reserve approval (or, depending on the circumstances, no notice of disapproval) prior to any person or company acquiring "control" of a bank or bank holding company. A conclusive presumption of control exists if an individual or company acquires the power, directly or indirectly, to direct the management or policies of an insured depository institution or to vote 25% or more of any class of voting securities of any insured depository institution. A rebuttable presumption of control exists if a person or company acquires 10% or more but less than 25% of any class of voting securities of an insured depository institution and either the institution has registered securities under Section 12 of the Securities Exchange Act of 1934, which we will refer to as the Exchange Act, or no other person will own a greater percentage of that class of voting securities immediately after the acquisition. Our common stock is registered under Section 12 of the Exchange Act.

The Federal Reserve Board maintains a policy statement on minority equity investments in banks and bank holding companies, that generally permits investors to (i) acquire up to 33% of the total equity of a target bank or bank holding company, subject to certain conditions, including (but not limited to) that the investing firm does not acquire 15% or more of any class of voting securities, and (ii) designate at least one director, without triggering the various regulatory requirements associated with control.

As a financial holding company, we are required to obtain prior approval from the Federal Reserve before (i) acquiring all or substantially all of the assets of a bank or bank holding company, (ii) acquiring direct or indirect ownership or control of more than 5% of the outstanding voting stock of any bank or bank holding company (unless we own a majority of such bank's voting shares), or (iii) merging or consolidating with any other bank or bank holding company. In determining whether to approve a proposed bank acquisition, federal bank regulators will consider, among other factors, the effect of the acquisition on competition, the public benefits expected to be received from the acquisition, the projected capital ratios and levels on a post-acquisition basis, and the acquiring institution's record of addressing the credit needs of the communities it serves, including the needs of low and moderate income neighborhoods, consistent with the safe and sound operation of the bank, under the Community Reinvestment Act of 1977.

Under Florida law, a person or entity proposing to directly or indirectly acquire control of a Florida bank must also obtain permission from the Florida Office of Financial Regulation. Florida statutes define "control" as either (i) indirectly or directly owning, controlling or having power to vote 25% or more of the voting securities of a bank; (ii) controlling the election of a majority of directors of a bank; (iii) owning, controlling, or having power to vote 10% or more of the voting securities as well as directly or indirectly exercising a controlling influence over management or policies of a bank; or (iv) as determined by the Florida Office of Financial Regulation. These requirements will affect us because CCB is chartered under Florida law and changes in control of CCBG are indirect changes in control of CCB.

Tying

Financial holding companies and their affiliates are prohibited from tying the provision of certain services, such as extending credit, to other services or products offered by the holding company or its affiliates, such as deposit products.

Capital; Dividends; Source of Strength

The Federal Reserve imposes certain capital requirements on financial holding companies under the Bank Holding Company Act, including a minimum leverage ratio and a minimum ratio of "qualifying" capital to risk-weighted assets. These requirements are described below under "Capital Regulations." Subject to its capital requirements and certain other restrictions, we are generally able to borrow money to make a capital contribution to CCB, and such loans may be repaid from dividends paid from CCB to us. We are also able to raise capital for contributions to CCB by issuing securities without having to receive regulatory approval, subject to compliance with federal and state securities laws.

In accordance with Federal Reserve policy, which has been codified by the Dodd-Frank Act, we are expected to act as a source of financial strength to CCB and to commit resources to support CCB in circumstances in which we might

not otherwise do so. In furtherance of this policy, the Federal Reserve may require a financial holding company to terminate any activity or relinquish control of a nonbank subsidiary (other than a nonbank subsidiary of a bank) upon the Federal Reserve's determination that such activity or control constitutes a serious risk to the financial soundness or stability of any subsidiary depository institution of the financial holding company. Further, federal bank regulatory authorities have additional discretion to require a financial holding company to divest itself of any bank or nonbank subsidiary if the agency determines that divestiture may aid the depository institution's financial condition.

Capital City Bank

Capital City Bank is a state-chartered commercial banking institution that is chartered by and headquartered in the State of Florida, and is subject to supervision and regulation by the Florida Office of Financial Regulation. The Florida Office of Financial Regulation supervises and regulates all areas of our operations including, without limitation, the making of loans, the issuance of securities, the conduct of our corporate affairs, the satisfaction of capital adequacy requirements, the payment of dividends, and the establishment or closing of banking centers. We are also a member bank of the Federal Reserve System, which makes our operations subject to broad federal regulation and oversight by the Federal Reserve. In addition, our deposit accounts are insured by the FDIC up to the maximum extent permitted by law, and the FDIC has certain enforcement powers over us.

As a state-chartered bank in the State of Florida, we are empowered by statute, subject to the limitations contained in those statutes, to take and pay interest on, savings and time deposits, to accept demand deposits, to make loans on residential and other real estate, to make consumer and commercial loans, to invest, with certain limitations, in equity securities and in debt obligations of banks and corporations and to provide various other banking services for the benefit of our clients. Various consumer laws and regulations also affect our operations, including state usury laws, laws relating to fiduciaries, consumer credit and equal credit opportunity laws, and fair credit reporting. In addition, the Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA") prohibits insured state chartered institutions from conducting activities as principal that are not permitted for national banks. A bank, however, may engage in an otherwise prohibited activity if it meets its minimum capital requirements and the FDIC determines that the activity does not present a significant risk to the Deposit Insurance Fund.

Reserves

The Federal Reserve requires all depository institutions to maintain reserves against transaction accounts (noninterest bearing and NOW checking accounts). The balances maintained to meet the reserve requirements imposed by the Federal Reserve may be used to satisfy liquidity requirements. An institution may borrow from the Federal Reserve Bank "discount window" as a secondary source of funds, provided that the institution meets the Federal Reserve Bank's credit standards.

Dividends

CCB is subject to legal limitations on the frequency and amount of dividends that can be paid to CCBG. The Federal Reserve may restrict the ability of CCB to pay dividends if such payments would constitute an unsafe or unsound banking practice. Additionally, as of January 1, 2019, financial institutions are being required to maintain a capital conservation buffer of at least 2.5% of risk-weighted assets in order to avoid restrictions on capital distributions and other payments. If a financial institution's capital conservation buffer falls below the minimum requirement, its maximum payout amount for capital distributions and discretionary payments declines to a set percentage of eligible retained income based on the size of the buffer. See "Capital Regulations," below for additional details on this new capital requirement.

In addition, Florida law and Federal regulation also places restrictions on the declaration of dividends from state chartered banks to their holding companies. Pursuant to the Florida Financial Institutions Code, the board of directors of state-chartered banks, after charging off bad debts, depreciation and other worthless assets, if any, and making provisions for reasonably anticipated future losses on loans and other assets, may quarterly, semi-annually or annually declare a dividend of up to the aggregate net profits of that period combined with the bank's retained net profits for the preceding two years and, with the approval of the Florida Office of Financial Regulation and Federal Reserve, declare a dividend from retained net profits which accrued prior to the preceding two years. Before declaring such dividends, 20% of the net profits for the preceding period as is covered by the dividend must be transferred to the surplus fund of the bank until this fund becomes equal to the amount of the bank's common stock then issued and outstanding. A state-chartered bank may not declare any dividend if (i) its net income (loss) from the current year combined with the retained net income (loss) for the preceding two years aggregates a loss or (ii) the payment of such dividend would cause the capital account of the bank to fall below the minimum amount required by law, regulation, order or any written agreement with the Florida Office of Financial Regulation or a federal regulatory agency.

Insurance of Accounts and Other Assessments

Our deposit accounts are currently insured by the Deposit Insurance Fund generally up to a maximum of $250,000 per separately insured depositor. We pay deposit insurance assessments to the Deposit Insurance Fund, which are

determined through a risk-based assessment system.

Under the current system, deposit insurance assessments are based on a bank's assessment base, which is defined as average total assets minus average tangible equity. The FDIC assigns an institution to one of two categories based on asset size. We fall into the Established Small Institution category. This category has three sub categories based on supervisory ratings (its "CAMELS ratings") designed to measure risk. In determining the applicable assessment rate, the initial base assessment is determined based on the risk-based sub category into which the bank falls. The applicable sub category is determined based on the institution's most recent supervisory and capital evaluations. The total base assessment rate is then determined by adjusting the initial base assessment rate by an unsecured debt adjustment and brokered deposit adjustment, if applicable, and the deposit insurance assessment is calculated by multiplying the bank's assessment base by the total base assessment rate.

In addition, all FDIC-insured institutions are required to pay assessments to the FDIC to fund interest payments on bonds issued by the Financing Corporation, an agency of the federal government established to recapitalize the predecessor to the Savings Association Insurance Fund. The Financing Corporation assessment rate is adjusted quarterly (currently less than 1 basis points for the first quarter of 2019) to reflect changes in the assessment base as determined from the quarterly Call Report submissions. These assessments will continue until the Financing Corporation bonds mature in 2019.

Under the Federal Deposit Insurance Act, or FDIA, the FDIC may terminate deposit insurance upon a finding that the institution has engaged in unsafe and unsound practices, is in an unsafe or unsound condition to continue operations, or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC.

Transactions With Affiliates

Pursuant to Sections 23A and 23B of the Federal Reserve Act and Regulation W, the authority of CCB to engage in transactions with related parties or "affiliates" or to make loans to insiders is limited. Loan transactions with an affiliate generally must be collateralized and certain transactions between CCB and its affiliates, including the sale of assets, the payment of money or the provision of services, must be on terms and conditions that are substantially the same, or at least as favorable to CCB, as those prevailing for comparable nonaffiliated transactions. In addition, CCB generally may not purchase securities issued or underwritten by affiliates.

Loans to executive officers, directors or to any person who directly or indirectly, or acting through or in concert with one or more persons, owns, controls or has the power to vote more than 10% of any class of voting securities of a bank, which we refer to as "10% Shareowners," or to any political or campaign committee the funds or services of which will benefit those executive officers, directors, or 10% Shareowners or which is controlled by those executive officers, directors or 10% Shareowners, are subject to Sections 22(g) and 22(h) of the Federal Reserve Act and their corresponding regulations (Regulation O) and Section 13(k) of the Exchange Act relating to the prohibition on personal loans to executives (which exempts financial institutions in compliance with the insider lending restrictions of Section 22(h) of the Federal Reserve Act). Among other things, these loans must be made on terms substantially the same as those prevailing on transactions made to unaffiliated individuals and certain extensions of credit to those persons must first be approved in advance by a disinterested majority of the entire board of directors. Section 22(h) of the Federal Reserve Act prohibits loans to any of those individuals where the aggregate amount exceeds 15% of an institution's unimpaired capital and surplus plus an additional 10% of unimpaired capital and surplus in the case of loans that are fully secured by readily marketable collateral, or when the aggregate amount on all of the extensions of credit outstanding to all of these persons would exceed our unimpaired capital and unimpaired surplus. Section 22(g) identifies limited circumstances in which we are permitted to extend credit to executive officers.

Community Reinvestment Act

The Community Reinvestment Act and its corresponding regulations are intended to encourage banks to help meet the credit needs of the communities they serve, including low and moderate income neighborhoods, consistent with safe and sound banking practices. These regulations provide for regulatory assessment of a bank's record in meeting the credit needs of its market area. Federal banking agencies are required to publicly disclose each bank's rating under the Community Reinvestment Act. The Federal Reserve considers a bank's Community Reinvestment Act rating when the bank submits an application to establish bank branches, merge with another bank, or acquire the assets and assume the liabilities of another bank. In the case of a financial holding company, the Community Reinvestment Act performance record of all banks involved in a merger or acquisition are reviewed in connection with the application to acquire ownership or control of shares or assets of a bank or to merge with another bank or bank holding company. An unsatisfactory record can substantially delay or block the transaction. We received a satisfactory rating on our most recent Community Reinvestment Act assessment.

Capital Regulations

The federal banking regulators have adopted risk-based, capital adequacy guidelines for financial holding companies and their subsidiary banks based on the Basel III standards, which became effective January 1, 2015 for community banks. Under these guidelines, assets and off-balance sheet items are assigned to specific risk categories each with designated risk weightings. The new risk-based capital guidelines are designed to make regulatory capital requirements more sensitive to differences in risk profiles of banks and bank holding companies, to account for off-balance sheet exposure, to minimize disincentives for holding liquid assets, and to achieve greater consistency in evaluating the capital adequacy of major banks throughout the world. The resulting capital ratios include ratios that represent capital as a percentage of total risk-weighted assets and off-balance sheet items.

In computing total risk-weighted assets, bank and bank holding company assets are assigned risk-weights of 0%, 20%, 50%, 100% and 150%. In addition, certain off-balance sheet items are assigned credit conversion factors to convert them to asset equivalent amounts to which an appropriate risk-weight applied. Most loans are assigned to the 100% risk category, except for performing first mortgage loans fully secured by 1- to 4-family and certain multi-family residential property, which carry a 50% risk rating. Most investment securities (including, general obligation claims on states or other political subdivisions of the United States) are assigned to the 20% category, except for municipal or state revenue bonds, which have a 50% risk-weight, and direct obligations of the U.S. Treasury or obligations backed by the full faith and credit of the U.S. Government, which have a 0% risk-weight. In covering off-balance sheet items, direct credit substitutes, including general guarantees and standby letters of credit backing financial obligations, are assigned a 100% conversion factor. Transaction-related contingencies such as bid bonds, standby letters of credit backing nonfinancial obligations, and undrawn commitments (including commercial credit lines with an initial maturity of more than one year) have a 50% conversion factor. Short-term commercial letters of credit are converted at 20% and certain short-term unconditionally cancelable commitments have a 0% factor.

Under the final rules, minimum requirements increased for both the quality and quantity of capital held by banking organizations. In this respect, the final rules implement strict eligibility criteria for regulatory capital instruments and improved the methodology for calculating risk-weighted assets to enhance risk sensitivity. Consistent with the international Basel III framework, the rules include a new minimum ratio of Common Equity Tier 1 Capital to Risk-Weighted Assets of 4.5% and a Common Equity Tier 1 Capital conservation buffer of 2.5% of risk-weighted assets. The rules also raise the minimum ratio of Tier 1 Capital to Risk-Weighted Assets from 4% to 6% and include a minimum leverage ratio of 4% for all banking organizations. The implementation of the capital conservation buffer began on January 1, 2016 at the 0.625% level and increased by 0.625% each of the next three years until January 1, 2019, when the full 2.5% capital conversion buffer was fully phased in. If a financial institution's capital conservation buffer falls below the minimum, capital distributions and discretionary payments could be limited or prohibited. The types of payments subject to this limitation include dividends, share buybacks, discretionary payments on Tier 1 instruments, and discretionary bonus payments.

The new capital regulations also impacted the treatment of accumulated other comprehensive income ("AOCI") for regulatory capital purposes. Under the new rules, AOCI generally flows through to regulatory capital, however, community banks and their holding companies were permitted to make a one-time irrevocable opt-out election to continue to treat AOCI the same as under the old regulations for regulatory capital purposes. We elected to opt-out in 2015. Additionally, community banks with less than $15 billion in total assets could continue to count certain non-qualifying capital instruments issued prior to May 19, 2010 as Tier 1 capital, including trust preferred securities and cumulative perpetual preferred stock (subject to a limit of 25% of Tier 1 capital). However, non-qualifying capital instruments issued on or after May 19, 2010 do not qualify for Tier 1 capital treatment.

Federal law and regulations also establish a capital-based regulatory scheme designed to promote early intervention for troubled banks and require the FDIC to choose the least expensive resolution of bank failures. The capital-based regulatory framework contains five categories of compliance with regulatory capital requirements, including "well capitalized," "adequately capitalized," "undercapitalized," "significantly undercapitalized," and "critically undercapitalized." T qualify as a "well-capitalized" institution, a bank must have a leverage ratio of not less than 5%, a Tier 1 Common Equity ratio of not less than 6.5%, a Tier 1 Capital ratio of not less than 8%, a total risk-based capital ratio of not less than 10%, and the bank must not be under any order or directive from the appropriate regulatory agency to meet and maintain a specific capital level.

A bank regulatory agency can treat an institution as if it were in the next lower category if the agency determines that the institution is operating in an unsafe or unsound condition or is engaging in an unsafe or unsound practice. The degree of regulatory scrutiny of a financial institution will increase, and the permissible activities of the institution will decrease, as it moves downward through the capital categories. Institutions that fall into one of the three undercapitalized categories may be required to (i) submit a capital restoration plan; (ii) raise additional capital; (iii) restrict their growth, deposit interest rates, and other activities; (iv) improve their management; (v) eliminate management fees; or (vi) divest all or a part of their operations. It should be noted that the minimum ratios referred to above are merely guidelines and the bank regulators may require higher capital ratios at their discretion.

At December 31, 2018, we exceeded the requirements to be classified as "well capitalized" and are unaware of any material violation or alleged violation of these regulations, policies or directives (see table below). Rapid growth, poor loan portfolio performance, or poor earnings performance, or a combination of these factors, could change our capital position in a relatively short period of time, making additional capital infusions necessary. The capital ratios can be found in Note 14 in the Notes to the Consolidated Financial Statements.

Prompt Corrective Action

Immediately upon becoming undercapitalized, a depository institution becomes subject to the provisions of Section 38 of the Federal Deposit Insurance Act, which: (i) restrict payment of capital distributions and management fees; (ii) require that the appropriate federal banking agency monitor the condition of the institution and its efforts to restore its capital; (iii) require submission of a capital restoration plan; (iv) restrict the growth of the institution's assets; and (v) require prior approval of certain expansion proposals. The appropriate federal banking agency for an undercapitalized institution also may take any number of discretionary supervisory actions if the agency determines that any of these actions is necessary to resolve the problems of the institution at the least possible long-term cost to the deposit insurance fund, subject in certain cases to specified procedures. These discretionary supervisory actions include: (i) requiring the institution to raise additional capital; (ii) restricting transactions with affiliates; (iii) requiring divestiture of the institution or the sale of the institution to a willing purchaser; and (iv) any other supervisory action that the agency deems appropriate. These and additional mandatory and permissive supervisory actions may be taken with respect to significantly undercapitalized and critically undercapitalized institutions.

Interstate Banking and Branching

The Bank Holding Company Act permits adequately capitalized and managed financial and bank holding companies to acquire banks in any state and state laws prohibiting interstate banking or discriminating against out-of-state banks are generally preempted. However, states are permitted to adopt a minimum age restriction requiring that target banks located within the state be in existence for a period of time, up to a maximum of five years, before a bank may be acquired by an out-of-state bank holding company. Also, the Dodd-Frank Act, added deposit caps, which prohibit acquisitions that would result in the acquiring company controlling 30% or more of the deposits of insured banks and thrift institutions held in the state in which the target maintains a branch or 10% or more of the deposits nationwide. States have the authority to waive the 30% deposit cap. State-level deposit caps are not preempted as long as they do not discriminate against out-of-state institutions, and the federal deposit caps apply only to initial entry acquisitions.

As a result of the Dodd-Frank Act, national banks and state banks are able to establish branches in any state if that state would permit the establishment of the branch by a state bank chartered in that state. Florida law permits a state bank to establish a branch of the bank anywhere in the state. Accordingly, a bank with its headquarters outside the State of Florida may establish branches anywhere within the state.

Anti-money Laundering

The Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 ("USA PATRIOT Act"), provides the federal government with additional powers to address terrorist threats through enhanced domestic security measures, expanded surveillance powers, increased information sharing and broadened anti-money laundering requirements. By way of amendments to the Bank Secrecy Act ("BSA"), the USA PATRIOT Act puts in place measures intended to encourage information sharing among bank regulatory and law enforcement agencies. In addition, certain provisions of the USA PATRIOT Act impose affirmative obligations on a broad range of financial institutions.

The USA PATRIOT Act and the related Federal Reserve regulations require banks to establish anti-money laundering programs that include, at a minimum:

- internal policies, procedures and controls designed to implement and maintain the savings association's compliance with all of the requirements of the USA PATRIOT Act, the BSA and related laws and regulations;
- systems and procedures for monitoring and reporting of suspicious transactions and activities;
- a designated compliance officer;

- employee training;
- an independent audit function to test the anti-money laundering program;
- procedures to verify the identity of each client upon the opening of accounts; and
- heightened due diligence policies, procedures and controls applicable to certain foreign accounts and relationships.

Additionally, the USA PATRIOT Act requires each financial institution to develop a customer identification program ("CIP") as part of its anti-money laundering program. The key components of the CIP are identification, verification, government list comparison, notice and record retention. The purpose of the CIP is to enable the financial institution to determine the true identity and anticipated account activity of each customer. To make this determination, among other things, the financial institution must collect certain information from customers at the time they enter into the customer relationship with the financial institution. This information must be verified within a reasonable time through documentary and non-documentary methods. Furthermore, all customers must be screened against any CIP-related government lists of known or suspected terrorists. On May 11, 2018, the U.S. Treasury's Financial Crimes Enforcement Network issued a final rule under the BSA requiring banks to identify and verify the identity of the natural persons behind their customers that are legal entities – the beneficial owners. We and our affiliates have adopted policies, procedures and controls designed to comply with the BSA and the USA PATRIOT Act.

Regulatory Enforcement Authority

Federal and state banking laws grant substantial regulatory authority and enforcement powers to federal and state banking regulators. This authority permits bank regulatory agencies to assess civil money penalties, to issue cease and desist or removal orders, and to initiate injunctive actions against banking organizations and institution-affiliated parties. In general, these enforcement actions may be initiated for either violations of laws or regulations or for unsafe or unsound practices. Other actions or inactions may provide the basis for enforcement action, including misleading or untimely reports filed with regulatory authorities.

Federal Home Loan Bank System

CCB is a member of the Federal Home Loan Bank of Atlanta, which is one of 11 regional Federal Home Loan Banks. Each FHLB serves as a quasi-reserve bank for its members within its assigned region. It is funded primarily from funds deposited by member institutions and proceeds from the sale of consolidated obligations of the FHLB system. A FHLB makes loans to members (i.e., advances) in accordance with policies and procedures established by the board of trustees of the FHLB.

As a member of the FHLB of Atlanta, CCB is required to own capital stock in the FHLB in an amount at least equal to 0.09% (or 9 basis points), which is subject to annual adjustments, of CCB's total assets at the end of each calendar year (up to a maximum of $15 million), plus 4.25% of its outstanding advances (borrowings) from the FHLB of Atlanta under the activity-based stock ownership requirement. As of December 31, 2018, CCB was in compliance with this requirement.

Privacy

Under the Gramm-Leach-Bliley Act, federal banking regulators adopted rules limiting the ability of banks and other financial institutions to disclose nonpublic information about consumers to nonaffiliated third parties. The rules require disclosure of privacy policies to consumers and, in some circumstances, allow consumers to prevent disclosure of certain personal information to nonaffiliated third parties.

Overdraft Fee Regulation

The Electronic Fund Transfer Act prohibits financial institutions from charging consumers fees for paying overdrafts on automated teller machines ("ATM") and one-time debit card transactions, unless a consumer consents, or opts in, to the overdraft service for those type of transactions. If a consumer does not opt in, any ATM transaction or debit that overdraws the consumer's account will be denied. Overdrafts on the payment of checks and regular electronic bill payments are not covered by this new rule. Before opting in, the consumer must be provided a notice that explains the financial institution's overdraft services, including the fees associated with the service, and the consumer's choices. Financial institutions must provide consumers who do not opt in with the same account terms, conditions and features (including pricing) that they provide to consumers who do opt in.

Consumer Laws and Regulations

CCB is also subject to other federal and state consumer laws and regulations that are designed to protect consumers in transactions with banks. While the list set forth below is not exhaustive, these laws and regulations include the Truth in Lending Act, the Truth in Savings Act, the Electronic Fund Transfer Act, the Expedited Funds Availability Act, the Check Clearing for the 21st Century Act, the Fair Credit Reporting Act, the Fair Debt Collection Practices Act, the Equal Credit Opportunity Act, the Fair Housing Act, the Home Mortgage Disclosure Act, the Fair and Accurate Credit Transactions Act, the Mortgage Disclosure Improvement Act, and the Real Estate Settlement Procedures Act, among others. These laws and regulations mandate certain disclosure requirements and regulate the manner in which financial institutions must deal with customers when taking deposits or making loans to such customers. CCB must comply with the applicable provisions of these consumer protection laws and regulations as part of its ongoing customer relations.

In addition, the Consumer Financial Protection Bureau issues regulations and standards under these federal consumer protection laws that affect our consumer businesses. These include regulations setting “ability to repay” standards for residential mortgage loans and mortgage loan servicing and originator compensation standards, which generally require creditors to make a reasonable, good faith determination of a consumer’s ability to repay any consumer credit transaction secured by a dwelling (excluding an open-end credit plan, timeshare plan, reverse mortgage, or temporary loan) and establishes certain protections from liability under this requirement for loans that meet the requirements of the “qualified mortgage” safe harbor. Also, in 2015, the new TILA-RESPA Integrated Disclosure (“TRID”) rules for mortgage closings took effect for new loan applications. The new TRID rules were further amended in 2017. These new rules, including the new required loan forms, have generally increased the time it takes to approve mortgage loans.

Future Legislative Developments

Various legislative acts are from time to time introduced in Congress and the Florida legislature. This legislation may change banking statutes and the environment in which our banking subsidiary and we operate in substantial and unpredictable ways. We cannot determine the ultimate effect that potential legislation, if enacted, or implementing regulations with respect thereto, would have upon our financial condition or results of operations or that of our banking subsidiary.

Current Expected Credit Loss Accounting Standard

In June 2016, the Financial Accounting Standards Board ("FASB") issued a new current expected credit loss rule ("CECL") which will require banks to record, at the time of origination, credit losses expected throughout the life of the asset portfolio on loans and held-to-maturity securities, compared to the current practice of recording losses when it is probable that a loss event has occurred. The update also amends the accounting for credit losses on available-for-sale debt securities and financial assets purchased with credit deterioration. The accounting standard change will be effective for us beginning on January 1, 2020. The change in accounting standards could result in an increase in our reserve for loan losses and will require us to book loan losses sooner than under the current requirements. We are taking the necessary steps to be in compliance with the CECL accounting standard which we expect will become a critical accounting policy.

Effect of Governmental Monetary Policies

The commercial banking business is affected not only by general economic conditions, but also by the monetary policies of the Federal Reserve. Changes in the discount rate on member bank borrowing, availability of borrowing at the "discount window," open market operations, changes in the Fed Funds target interest rate, changes in interest rates payable on member banks' reserve accounts, the imposition of changes in reserve requirements against member banks' deposits and assets of foreign banking centers and the imposition of and changes in reserve requirements against certain borrowings by banks and their affiliates are some of the instruments of monetary policy available to the Federal Reserve. These monetary policies are used in varying combinations to influence overall growth and distributions of bank loans, investments and deposits, which may affect interest rates charged on loans or paid on deposits. The monetary policies of the Federal Reserve have had a significant effect on the operating results of commercial banks and are expected to continue to do so in the future. The Federal Reserve's policies are primarily influenced by its dual mandate of price stability and full employment, and to a lesser degree by short-term and long-term changes in the international trade balance and in the fiscal policies of the U.S. Government. Future changes in monetary policy and the effect of such changes on our business and earnings in the future cannot be predicted.

Income Taxes

We are subject to income taxes at the federal level and subject to state taxation based on the laws of each state in which we operate. We file a consolidated federal tax return with a fiscal year ending on December 31. On December 22, 2017, the United States enacted tax reform legislation known as the H.R.1, commonly referred to as the "Tax Cuts and Jobs Act," resulting in significant modifications to existing law. We completed the accounting for the effects of the new law during this period. Our financial statements for the year ended December 31, 2017, reflected certain effects of the new law, which included a reduction in the corporate tax rate from 35% to 21%, as well as other changes. As a result of the changes to tax laws and tax rates under the Act, we incurred an increase in income tax expense during the year ended December 31, 2017, due to a write-down of our net deferred tax asset by $4.1 million in the fourth quarter of 2017 as a result of the reduction to the federal corporate income tax rate. While the new tax law negatively

impacted earnings in the fourth quarter of 2017, the lower corporate tax rate is expected to be a significant ongoing benefit to us in future periods. Absent future discrete events, we anticipate that our effective tax in future periods will be approximately 24% due to a lower federal corporate income tax rate.

Website Access to Company's Reports

Our Internet website is www.ccbg.com. Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, including any amendments to those reports filed or furnished pursuant to section 13(a) or 15(d), and reports filed pursuant to Section 16, 13(d), and 13(g) of the Exchange Act are available free of charge through our website as soon as reasonably practicable after they are electronically filed with, or furnished to, the Securities and Exchange Commission. The information on our website is not incorporated by reference into this report.

Item 1A. Risk Factors

An investment in our common stock contains a high degree of risk. You should consider carefully the following risk factors before deciding whether to invest in our common stock. Our business, including our operating results and financial condition, could be harmed by any of these risks. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially and adversely affect our business. The trading price of our common stock could decline due to any of these risks, and you may lose all or part of your investment. In assessing these risks, you should also refer to the other information contained in our filings with the SEC, including our financial statements and related notes.

Risks Related to Our Business

We may incur losses if we are unable to successfully manage interest rate risk.

Our profitability depends to a large extent on Capital City Bank’s net interest income, which is the difference between income on interest-earning assets, such as loans and investment securities, and expense on interest-bearing liabilities such as deposits and borrowings. We are unable to predict changes in market interest rates, which are affected by many factors beyond our control, including inflation, recession, unemployment, federal funds target rate, money supply, domestic and international events and changes in the United States and other financial markets. Our net interest income may be reduced if: (i) more interest-earning assets than interest-bearing liabilities reprice or mature during a time when interest rates are declining or (ii) more interest-bearing liabilities than interest-earning assets reprice or mature during a time when interest rates are rising.

Changes in the difference between short-term and long-term interest rates may also harm our business. We generally use short-term deposits to fund longer-term assets. When interest rates change, assets and liabilities with shorter terms reprice more quickly than those with longer terms, which could have a material adverse effect on our net interest margin. If market interest rates rise rapidly, interest rate adjustment caps may also limit increases in the interest rates on adjustable rate loans, which could further reduce our net interest income. Additionally, we believe that due to the recent historical low interest rate environment, the effects of the repeal of Regulation Q, which previously had prohibited the payment of interest on demand deposits by member banks of the Federal Reserve System, has not been realized. The increased price competition for deposits that may result upon the return to a historically normal interest rate environment could adversely affect net interest margins of community banks.

Although we continuously monitor interest rates and have a number of tools to manage our interest rate risk exposure, changes in market assumptions regarding future interest rates could significantly impact our interest rate risk strategy, our financial position and results of operations. If we do not properly monitor our interest rate risk management strategies, these activities may not effectively mitigate our interest rate sensitivity or have the desired impact on our results of operations or financial condition.

Our loan portfolio includes loans with a higher risk of loss which could lead to higher loan losses and nonperforming assets.

We originate commercial real estate loans, commercial loans, construction loans, vacant land loans, consumer loans, and residential mortgage loans primarily within our market area. Commercial real estate, commercial, construction, vacant land, and consumer loans may expose a lender to greater credit risk than traditional fixed-rate fully amortizing loans secured by single-family residential real estate because the collateral securing these loans may not be sold as easily as single-family residential real estate. In addition, these loan types tend to involve larger loan balances to a

single borrower or groups of related borrowers and are more susceptible to a risk of loss during a downturn in the business cycle. These loans also have historically had greater credit risk than other loans for the following reasons:

- **Commercial Real Estate Loans**. Repayment is dependent on income being generated in amounts sufficient to cover operating expenses and debt service. These loans also involve greater risk because they are generally not fully amortizing over the loan period, but rather have a balloon payment due at maturity. A borrower's ability to make a balloon payment typically will depend on the borrower's ability to either refinance the loan or timely sell the underlying property. At December 31, 2018, commercial mortgage loans comprised approximately 33.8% of our total loan portfolio.

- **Commercial Loans**. Repayment is generally dependent upon the successful operation of the borrower's business. In addition, the collateral securing the loans may depreciate over time, be difficult to appraise, be illiquid, or fluctuate in value based on the success of the business. At December 31, 2018, commercial loans comprised approximately 13.1% of our total loan portfolio.

- **Construction Loans**. The risk of loss is largely dependent on our initial estimate of whether the property's value at completion equals or exceeds the cost of property construction and the availability of take-out financing. During the construction phase, a number of factors can result in delays or cost overruns. If our estimate is inaccurate or if actual construction costs exceed estimates, the value of the property securing our loan may be insufficient to ensure full repayment when completed through a permanent loan, sale of the property, or by seizure of collateral. At December 31, 2018, construction loans comprised approximately 5.0% of our total loan portfolio.

- **Vacant Land Loans**. Because vacant or unimproved land is generally held by the borrower for investment purposes or future use, payments on loans secured by vacant or unimproved land will typically rank lower in priority to the borrower than a loan the borrower may have on their primary residence or business. These loans are susceptible to adverse conditions in the real estate market and local economy. At December 31, 2018, vacant land loans comprised approximately 2.86% of our total loan portfolio.

- **HELOCs**. Our open-ended home equity loans have an interest-only draw period followed by a five-year repayment period of 0.75% of the principal balance monthly and a balloon payment at maturity. Upon the commencement of the repayment period, the monthly payment can increase significantly, thus, there is a heightened risk that the borrower will be unable to pay the increased payment. Further, these loans also involve greater risk because they are generally not fully amortizing over the loan period, but rather have a balloon payment due at maturity. A borrower's ability to make a balloon payment may depend on the borrower's ability to either refinance the loan or timely sell the underlying property. At December 31, 2018, HELOCs comprised approximately 11.8% of our total loan portfolio.

- **Consumer Loans**. Consumer loans (such as automobile loans and personal lines of credit) are collateralized, if at all, with assets that may not provide an adequate source of payment of the loan due to depreciation, damage, or loss. At December 31, 2018, consumer loans comprised approximately 16.7% of our total loan portfolio, with indirect auto loans making up a majority of this portfolio at approximately 89% of the total balance.

The increased risks associated with these types of loans result in a correspondingly higher probability of default on such loans (as compared to fixed-rate fully amortizing single-family real estate loans). Loan defaults would likely increase our loan losses and nonperforming assets and could adversely affect our allowance for loan losses and our results of operations.

We process, maintain, and transmit confidential client information through our information technology systems, such as our online banking service. Cybersecurity issues, such as security breaches and computer viruses, affecting our information technology systems or fraud related to our debit card products could disrupt our business, result in the unintended disclosure or misuse of confidential or proprietary information, damage our reputation, increase our costs, and cause losses.

We collect and store sensitive data, including our proprietary business information and that of our clients, and personally identifiable information of our clients and employees, in our information technology systems. We also provide our clients the ability to bank online. The secure processing, maintenance, and transmission of this information is critical to our operations. Our network, or those of our clients, could be vulnerable to unauthorized access, computer viruses, phishing schemes and other security problems. Financial institutions and companies engaged in data processing have increasingly reported breaches in the security of their websites or other systems, some of which have involved sophisticated and targeted attacks intended to obtain unauthorized access to confidential information, destroy data, disrupt or degrade service, sabotage systems or cause other damage.

We may be required to spend significant capital and other resources to protect against the threat of security breaches and computer viruses or to alleviate problems caused by security breaches or viruses. Security breaches and viruses could expose us to claims, litigation and other possible liabilities. Any inability to prevent security breaches or computer viruses could also cause existing clients to lose confidence in our systems and could adversely affect our reputation and our ability to generate deposits.

Additionally, fraud losses related to debit and credit cards have risen in recent years due in large part to growing and evolving schemes to illegally use cards or steal consumer credit card information despite risk management practices employed by the debit and credit card industries. Many issuers of debit and credit cards have suffered significant losses in recent years due to the theft of cardholder data that has been illegally exploited for personal gain.

The potential for debit and credit card fraud against us or our clients and our third party service providers is a serious issue. Debit and credit card fraud is pervasive and the risks of cybercrime are complex and continue to evolve. In view of the recent high-profile retail data breaches involving client personal and financial information, the potential impact on us and any exposure to consumer losses and the cost of technology investments to improve security could cause losses to us or our clients, damage to our brand, and an increase in our costs.

An inadequate allowance for loan losses would reduce our earnings.

We are exposed to the risk that our clients may be unable to repay their loans according to their terms and that any collateral securing the payment of their loans may not be sufficient to assure full repayment. This could result in credit losses that are inherent in the lending business. We evaluate the collectability of our loan portfolio and provide an allowance for loan losses that we believe is adequate based upon such factors as:

- the risk characteristics of various classifications of loans;
- previous loan loss experience;
- specific loans that have loss potential;
- delinquency trends;
- estimated fair market value of the collateral;
- current economic conditions; and
- geographic and industry loan concentrations.

As of December 31, 2018, our allowance for loan losses was $14.2 million, which represented approximately 0.80% of our total loans. We had $6.9 million in nonaccruing loans as of December 31, 2018. The allowance is based on management's reasonable estimate and may not prove sufficient to cover future loan losses. Although management uses the best information available to make determinations with respect to the allowance for loan losses, future adjustments may be necessary if economic conditions differ substantially from the assumptions used or adverse developments arise with respect to our nonperforming or performing loans. In addition, regulatory agencies, as an integral part of their examination process, periodically review our estimated losses on loans. Our regulators may require us to recognize additional losses based on their judgments about information available to them at the time of their examination. Accordingly, the allowance for loan losses may not be adequate to cover all future loan losses and significant increases to the allowance may be required in the future if, for example, economic conditions worsen. A material increase in our allowance for loan losses would adversely impact our net income and capital in future periods, while having the effect of overstating our current period earnings.

A new accounting standard will likely require us to increase our allowance for loan losses and may have a material adverse effect on our financial condition and results of operations.

The FASB has adopted a new accounting standard that will be effective for the Company on January 1, 2020. This standard, referred to as Current Expected Credit Loss, or CECL, will require financial institutions to determine periodic estimates of lifetime expected credit losses on loans, and recognize the expected credit losses as allowances for loan losses. CECL will also require us to record credit losses expected throughout the life of other assets in our portfolio, including held-to-maturity securities, as opposed the current practice of recording losses when it is probable that a loss event has occurred. The update also amends the accounting for credit losses on available-for-sale debt securities and financial assets purchased with credit deterioration. This will change the current method of providing allowances for loan losses that are probable, which would likely require us to increase our allowance for loan losses, and to greatly increase the types of data we would need to collect and review to determine the appropriate level of the allowance for loan losses. Any increase in our allowance for loan losses or expenses incurred to determine the appropriate level of the allowance for loan losses could reduce our net income and equity and, as a result, may have a material adverse effect on our financial condition and results of operations.

We may incur significant costs associated with the ownership of real property as a result of foreclosures, which could reduce our net income.

Since we originate loans secured by real estate, we may have to foreclose on the collateral property to protect our investment and may thereafter own and operate such property, in which case we would be exposed to the risks inherent in the ownership of real estate.

The amount that we, as a mortgagee, may realize after a foreclosure is dependent upon factors outside of our control, including, but not limited to:

- general or local economic conditions;
- environmental cleanup liability;
- neighborhood values;
- interest rates;
- real estate tax rates;
- operating expenses of the mortgaged properties;
- supply of and demand for rental units or properties;
- ability to obtain and maintain adequate occupancy of the properties;
- zoning laws;
- governmental rules, regulations and fiscal policies; and
- acts of God.

Certain expenditures associated with the ownership of real estate, including real estate taxes, insurance and maintenance costs, may adversely affect the income from the real estate. Furthermore, we may need to advance funds to continue to operate or to protect these assets. As a result, the cost of operating real property assets may exceed the rental income earned from such properties or we may be required to dispose of the real property at a loss.

Liquidity risk could impair our ability to fund operations and jeopardize our financial condition.

Effective liquidity management is essential for the operation of our business. We require sufficient liquidity to meet client loan requests, client deposit maturities and withdrawals, payments on our debt obligations as they come due and other cash commitments under both normal operating conditions and other unpredictable circumstances causing industry or general financial market stress. If we are unable to raise funds through deposits, borrowings, earnings and other sources, it could have a substantial negative effect on our liquidity. In particular, a majority of our liabilities during 2018 were checking accounts and other liquid deposits, which are generally payable on demand or upon short notice. By comparison, a substantial majority of our assets were loans, which cannot generally be called or sold in the same time frame. Although we have historically been able to replace maturing deposits and advances as necessary, we might not be able to replace such funds in the future, especially if a large number of our depositors seek to withdraw their accounts at the same time, regardless of the reason. Our access to funding sources in amounts adequate to finance our activities on terms that are acceptable to us could be impaired by factors that affect us specifically or the financial services industry or economy in general. Factors that could negatively impact our access to liquidity sources include a decrease in the level of our business activity as a result of a downturn in the markets in which our loans are concentrated, adverse regulatory action against us, or our inability to attract and retain deposits. Our ability to borrow could also be impaired by factors that are not specific to us, such as a disruption in the financial markets or negative views and expectations about the prospects for the financial services industry. If we are unable to maintain adequate liquidity, it could materially and adversely affect our business, results of operations or financial condition.

European Union’s General Data Privacy Regulation

In May 2018, the European Union (“EU“) adopted the General Data Protection Regulation (“GDPR“). The GDPR is focused on the protection of the data and the privacy of individuals within the EU and the European Economic Area. The GDPR extends the scope of EU privacy rules to include organizations outside the EU if they offer goods or services to or monitor behaviors of EU citizens. The penalties and sanctions for noncompliance with the GDPR are difficult to predict and potentially very high. While we believe that the GDPR will have little impact on us, we may be impacted by similar privacy laws that may be adopted by other federal, state, or local governing bodies in the future.

Our future success is dependent on our ability to compete effectively in the highly competitive banking industry.

We face vigorous competition for deposits, loans and other financial services in our market area from other banks and financial institutions, including savings and loan associations, savings banks, finance companies and credit unions. A number of our competitors are significantly larger than we are and have greater access to capital and other resources. Many of our competitors also have higher lending limits, more expansive branch networks, and offer a wider array of financial products and services. To a lesser extent, we also compete with other providers of financial services, such as money market mutual funds, brokerage firms, consumer finance companies, insurance companies and governmental organizations, which may offer financial products and services on more favorable terms than we are able to. Many of

our non-bank competitors are not subject to the same extensive regulations that govern our activities. As a result, these non-bank competitors have advantages over us in providing certain services. The effect of this competition may reduce or limit our margins or our market share and may adversely affect our results of operations and financial condition.

Risks Related to Regulation and Legislation

We are subject to extensive regulation, which could restrict our activities and impose financial requirements or limitations on the conduct of our business.

We are subject to extensive regulation, supervision and examination by our regulators, including the Florida Office of Financial Regulation, the Federal Reserve, and the FDIC. Our compliance with these industry regulations is costly and restricts certain of our activities, including payment of dividends, mergers and acquisitions, investments, lending and interest rates charged on loans, interest rates paid on deposits, access to capital and brokered deposits and locations of banking offices. If we are unable to meet these regulatory requirements, our financial condition, liquidity and results of operations would be materially and adversely affected.

Our activities are also regulated under consumer protection laws applicable to our lending, deposit and other activities. Many of these regulations are intended primarily for the protection of our depositors and the Deposit Insurance Fund and not for the benefit of our shareowners. In addition to the regulations of the bank regulatory agencies, as a member of the Federal Home Loan Bank, we must also comply with applicable regulations of the Federal Housing Finance Agency and the Federal Home Loan Bank.

Our failure to comply with these laws and regulations could subject us to restrictions on our business activities, fines and other penalties, any of which could adversely affect our results of operations, capital base and the price of our securities. Further, any new laws, rules and regulations could make compliance more difficult or expensive or otherwise adversely affect our business and financial condition. Please refer to the Section entitled “Business – Regulatory Considerations” in this Report.

The Economic Growth, Regulatory Relief and Consumer Protection Act of 2018 may affect our business.

On May 24, 2018, the Economic Growth, Regulatory Relief and Consumer Protection Act of 2018 ("EGRRCPA") was enacted to modify or repeal certain provisions of the Dodd-Frank Act. EGRRCPA, among other things: (i) allows smaller banks (with up to $10 billion in assets) to offer certain qualified residential mortgages that are not subject to the ability-to-repay requirements; (ii) exempts from appraisal requirements certain transactions involving real estate in rural areas that is valued at less than $400,000; (iii) amends the Home Mortgage Disclosure Act of 1975 to exempt from certain disclosure requirements banks that originate fewer than 500 closed-end mortgage loans and fewer than 500 open-end lines of credit in each of the last two calendar years; (iv) clarifies that, subject to various conditions, reciprocal deposits of another depository institution obtained using a deposit broker through a deposit placement network for purposes of obtaining maximum deposit insurance would not be considered brokered deposits subject to the FDIC's brokered-deposit regulations; (v) expands the examination cycle for certain banks with less than $3 billion in assets so that on-site examinations must occur not less than once during each 18-month period; (vi) directs federal banking agencies to develop a community bank leverage ratio of not less than 8% and not more than 10% for qualifying community banks; (vii) exempts banks with less than $10 billion in total consolidated assets and with trading assets and liabilities less than or equal to 5% of total consolidated assets from the requirements of the Volcker Rule; and (viii) directs the Federal Reserve Board to expand the definition of a small bank holding company under the Small Bank Holding Company Policy Statement to include banks that, among other conditions, have less than $3 billion in assets. While many of these changes could result in regulatory relief for CCBG, it is difficult to predict how any new standards under EGRRCPA will be applied to us or its ultimate impact on us. This is in part due to the fact that it requires the enactment of multiple implementing regulations that have yet to be written.

Changes in U.S. trade policies and other factors beyond our control may have an adverse impact on our results of operations and financial condition.

There has been recent discussion, imposition, and proposition of revisions to U.S. trade policies and legislation, especially the imposition of tariffs. Such tariffs may cause affected foreign governments to impose their own tariffs in retaliation. It is difficult to predict what the U.S. government or foreign governments will actually do or not do in the future or the impacts such actions will have on CCBG or its customers. Such tariffs, along with other trade restrictions, affecting those items and products used by our customers in their respective businesses could have an adverse impact on our customers' respective financial conditions and their ability to make payments on their loans. This could result in an adverse impact on our business, financial condition, and results of operation.

On October 1, 2018, the United States, Canada and Mexico agreed on a new trade agreement, the United States-Mexico-Canada Agreement ("USMCA"), to replace the North American Free Trade Agreement. The USMCA is still subject to the approval of the Congress and is yet to come into effect. It has yet to be seen what impact the adoption of the USMCA or any subsequent trade agreements made as a response to the USMCA will have on CCBG or its customers. Any such shift in trade policies or agreements could potentially negatively impact the business, financial condition, and results of operations of our customers, and, in turn, that of CCBG.

The increased capital requirements may have an adverse effect on us.

In 2013, the Federal Reserve Board released its final rules which implement in the United States the Basel III regulatory capital reforms from the Basel Committee on Banking Supervision and certain changes required by the Dodd-Frank Act. Under the final rule, minimum requirements increased for both the quality and quantity of capital held by banking organizations. Consistent with the international Basel framework, the rule includes a new minimum ratio of Common Equity Tier 1 Capital (“CET1”) to Risk-Weighted Assets (“RWA”) of 4.5% and a CET1 conservation buffer of 2.5% of RWA (which is being phased in from 2016 through 2019) that apply to all supervised financial institutions. As of January 1, 2019, the CET1conservation buffer requirement was 2.5%, which requires us to hold additional CET1 capital in excess of the minimum required to meet the CET1 to RWA ratio requirement. The rule also, among other things, raised the minimum ratio of Tier 1 Capital to RWA from 4% to 6% and included a minimum leverage ratio of 4% for all banking organizations. The impact of the new capital rules requires us to maintain higher levels of capital, which we expect will lower our return on equity. Additionally, if our CET1 to RWA ratio does not exceed the minimum required plus the additional CET1 conservation buffer, we may be restricted in our ability to pay dividends or make other distributions of capital to our shareowners.

The Tax Cuts and Jobs Act may have an adverse effect on us

The Tax Cuts and Jobs Act enacted in December 2017 has positively impacted us by decreasing our federal corporate tax rate from 35% to 21%, but the act poses potential adverse impacts on the banks financial condition as well. We may suffer as a result of the act (1) eliminating interest deductions for certain home equity loans, (2) limiting the deductibility of business interest expense, (3) limiting the deductibility of property taxes, state income taxes, and local incomes taxes, and (4) lowering the limit on the deductibility of mortgage interest paid on single-family residential mortgage loans. These changes may specifically have an adverse impact on the market for residential homes and borrowers abilities to make payments on their mortgages, which could lower the demand for residential mortgage loans and lower the value of properties securing loans that we hold in our portfolio. Such affects could adversely impact our business and financial condition.

Compliance with the Consumer Financial Protection Bureau’s ability-to-repay rule safe-harbor could adversely impact our growth or profitability.

The Consumer Financial Protection Bureau issued a rule, effective as of January 10, 2014, designed to clarify for lenders how they can avoid monetary damages under the Dodd-Frank Act, which holds lenders accountable for ensuring a borrower’s ability to repay a mortgage at the time the loan is originated. Loans that satisfy the “qualified mortgage” safe-harbor will be presumed to have complied with the new ability-to-repay standard. Under the Consumer Financial Protection Bureau’s rule, a “qualified mortgage” loan must not contain certain specified features, including but not limited to:

- excessive upfront points and fees (those exceeding 3% of the total loan amount, less “bona fide discount points” for prime loans);
- interest-only payments;
- negative-amortization; and
- terms longer than 30 years.

Also, to qualify as a “qualified mortgage,” a borrower’s total monthly debt-to-income ratio may not exceed 43%. Lenders must also verify and document the income and financial resources relied upon to qualify the borrower for the loan and underwrite the loan based on a fully amortizing payment schedule and maximum interest rate during the first five years, taking into account all applicable taxes, insurance and assessments. The Consumer Financial Protection Bureau’s rule on qualified mortgages could limit our ability or desire to make certain types of loans or loans to certain borrowers, or could make it more expensive and/or time consuming to make these loans, which could adversely impact our growth or profitability.

Florida financial institutions, such as CCB, face a higher risk of noncompliance and enforcement actions with the Bank Secrecy Act and other anti-money laundering statutes and regulations.

Since September 11, 2001, banking regulators have intensified their focus on anti-money laundering and Bank Secrecy Act compliance requirements, particularly the anti-money laundering provisions of the USA PATRIOT Act. There is also increased scrutiny of compliance with the rules enforced by the Office of Foreign Assets Control ("OFAC"). Since 2004, federal banking regulators and examiners have been extremely aggressive in their supervision and examination of financial institutions located in the State of Florida with respect to the institution's Bank Secrecy Act/anti-money laundering compliance. Consequently, numerous formal enforcement actions have been instituted against financial institutions.

In order to comply with regulations, guidelines and examination procedures in this area, CCB has been required to adopt new policies and procedures and to install new systems. CCB's policies, procedures and systems are deemed deficient or the policies, procedures and systems of the financial institutions that it has already acquired or may acquire in the future are deficient, CCB would be subject to liability, including fines and regulatory actions such as restrictions on its ability to pay dividends and the necessity to obtain regulatory approvals to proceed with certain aspects of its business plan, including its acquisition plans.

Risks Related to Market Events

Our loan portfolio is heavily concentrated in mortgage loans secured by properties in Florida and Georgia which causes our risk of loss to be higher than if we had a more geographically diversified portfolio.

Our interest-earning assets are heavily concentrated in mortgage loans secured by real estate, particularly real estate located in Florida and Georgia. At December 31, 2018, approximately 70% of our loans included real estate as a primary, secondary, or tertiary component of collateral. The real estate collateral in each case provides an alternate source of repayment in the event of default by the borrower; however, the value of the collateral may decline during the time the credit is extended. If we are required to liquidate the collateral securing a loan during a period of reduced real estate values to satisfy the debt, our earnings and capital could be adversely affected.

Additionally, at December 31, 2018, substantially all of our loans secured by real estate are secured by commercial and residential properties located in Northern Florida and Middle Georgia. The concentration of our loans in these areas subjects us to risk that a downturn in the economy or recession in these areas could result in a decrease in loan originations and increases in delinquencies and foreclosures, which would more greatly affect us than if our lending were more geographically diversified. In addition, since a large portion of our portfolio is secured by properties located in Florida and Georgia, the occurrence of a natural disaster, such as a hurricane, or a man-made disaster could result in a decline in loan originations, a decline in the value or destruction of mortgaged properties and an increase in the risk of delinquencies, foreclosures or loss on loans originated by us. We may suffer further losses due to the decline in the value of the properties underlying our mortgage loans, which would have an adverse impact on our results of operations and financial condition.

Our concentration in loans secured by real estate may increase our credit losses, which would negatively affect our financial results.

Due to the lack of diversified industry within the markets served by CCB Bank and the relatively close proximity of our geographic markets, we have both geographic concentrations as well as concentrations in the types of loans funded. Specifically, due to the nature of our markets, a significant portion of the portfolio has historically been secured with real estate. At December 31, 2018, approximately 34% and 31% of our $1.781 billion loan portfolio was secured by commercial real estate and residential real estate, respectively. As of this same date, approximately 5% was secured by property under construction.

In the event we are required to foreclose on a property securing one of our mortgage loans or otherwise pursue our remedies in order to protect our investment, we may be unable to recover funds in an amount equal to our projected return on our investment or in an amount sufficient to prevent a loss to us due to prevailing economic conditions, real estate values and other factors associated with the ownership of real property. As a result, the market value of the real estate or other collateral underlying our loans may not, at any given time, be sufficient to satisfy the outstanding principal amount of the loans, and consequently, we would sustain loan losses.

The fair value of our investments could decline which would cause a reduction in shareowners' equity.

A large portion of our investment securities portfolio at December 31, 2018 has been designated as available-for-sale pursuant to U.S. generally accepted accounting principles relating to accounting for investments. Such principles require that unrealized gains and losses in the estimated value of the available-for-sale portfolio be "marked to market" and reflected as a separate item in shareowners' equity (net of tax) as accumulated other comprehensive income/losses. Shareowners' equity will continue to reflect the unrealized gains and losses (net of tax) of these investments. The fair value of our investment portfolio may decline, causing a corresponding decline in shareowners' equity.

Management believes that several factors will affect the fair values of our investment portfolio. These include, but are not limited to, changes in interest rates or expectations of changes in interest rates, the degree of volatility in the securities markets, inflation rates or expectations of inflation and the slope of the interest rate yield curve (the yield curve refers to the differences between short-term and long-term interest rates; a positively sloped yield curve means short-term rates are lower than long-term rates). These and other factors may impact specific categories of the portfolio differently, and we cannot predict the effect these factors may have on any specific category.

Risks Related to an Investment in Our Common Stock

We may be unable to pay dividends in the future.

In 2018, our Board of Directors declared four quarterly cash dividends. Declarations of any future dividends will be contingent on our ability to earn sufficient profits and to remain well capitalized, including our ability to hold and generate sufficient capital to comply with the new CET1 conservation buffer requirement. In addition, due to our contractual obligations with the holders of our trust preferred securities, if we defer the payment of accrued interest owed to the holders of our trust preferred securities, we may not make dividend payments to our shareowners.

Further, under applicable statutes and regulations, CCB’s board of directors, after charging-off bad debts, depreciation and other worthless assets, if any, and making provisions for reasonably anticipated future losses on loans and other assets, may quarterly, semi-annually, or annually declare and pay dividends to CCBG of up to the aggregate net income of that period combined with the CCB’s retained net income for the preceding two years and, with the approval of the Florida Office of Financial Regulation and Federal Reserve, declare a dividend from retained net income which accrued prior to the preceding two years. Additional state laws generally applicable to Florida corporations may also limit our ability to declare and pay dividends. Thus, our ability to fund future dividends may be restricted by state and federal laws and regulations.

Limited trading activity for shares of our common stock may contribute to price volatility.

While our common stock is listed and traded on the Nasdaq Global Select Market, there has historically been limited trading activity in our common stock. The average daily trading volume of our common stock over the 12-month period ending December 31, 2018 was approximately 21,082 shares. Due to the limited trading activity of our common stock, relativity small trades may have a significant impact on the price of our common stock.

Securities analysts may not initiate coverage or continue to cover our common stock, and this may have a negative impact on its market price.

The trading market for our common stock will depend in part on the research and reports that securities analysts publish about us and our business. We do not have any control over securities analysts and they may not initiate coverage or continue to cover our common stock. If securities analysts do not cover our common stock, the lack of research coverage may adversely affect its market price. If we are covered by securities analysts, and our common stock is the subject of an unfavorable report, our stock price would likely decline. If one or more of these analysts ceases to cover our Company or fails to publish regular reports on us, we could lose visibility in the financial markets, which may cause our stock price or trading volume to decline.

Our directors, executive officers, and principal shareowners, if acting together, have substantial control over all matters requiring shareowner approval, including changes of control. Because Mr. William G. Smith, Jr. is a principal shareowner and our Chairman, President, and Chief Executive Officer and Chairman of CCB, he has substantial control over all matters on a day to day basis.

Our directors, executive officers, and principal shareowners beneficially owned approximately 21.0% of the outstanding shares of our common stock at December 31, 2018. William G. Smith, Jr., our Chairman, President and Chief Executive Officer, owned 18.1% of our shares as of that date. Accordingly, these directors, executive officers, and principal shareowners, if acting together, may be able to influence or control matters requiring approval by our shareowners, including the election of directors and the approval of mergers, acquisitions or other extraordinary transactions. Moreover, because William G. Smith, Jr. is the Chairman, President, and Chief Executive Officer of CCBG and Chairman of CCB, he has substantial control over all matters on a day-to-day basis, including the nomination and election of directors.

These directors, executive officers, and principal shareowners may also have interests that differ from yours and may vote in a way with which you disagree and which may be adverse to your interests. The concentration of ownership may have the effect of delaying, preventing or deterring a change of control of our company, could deprive our shareowners of an opportunity to receive a premium for their common stock as part of a sale of our Company and might ultimately affect the market price of our common stock. You may also have difficulty changing management,

the composition of the Board of Directors, or the general direction of our Company.

Our Articles of Incorporation, Bylaws, and certain laws and regulations may prevent or delay transactions you might favor, including a sale or merger of CCBG.

CCBG is registered with the Federal Reserve as a financial holding company under the Bank Holding Company Act (“BHCA”). As a result, we are subject to supervisory regulation and examination by the Federal Reserve. The Gramm-Leach-Bliley Act, the BHCA, and other federal laws subject financial holding companies to particular restrictions on the types of activities in which they may engage, and to a range of supervisory requirements and activities, including regulatory enforcement actions for violations of laws and regulations.

Provisions of our Articles of Incorporation, Bylaws, certain laws and regulations and various other factors may make it more difficult and expensive for companies or persons to acquire control of us without the consent of our Board of Directors. It is possible, however, that you would want a takeover attempt to succeed because, for example, a potential buyer could offer a premium over the then prevailing price of our common stock.

For example, our Articles of Incorporation permit our Board of Directors to issue preferred stock without shareowner action. The ability to issue preferred stock could discourage a company from attempting to obtain control of us by means of a tender offer, merger, proxy contest or otherwise. Additionally, our Articles of Incorporation and Bylaws divide our Board of Directors into three classes, as nearly equal in size as possible, with staggered three-year terms. One class is elected each year. The classification of our Board of Directors could make it more difficult for a company to acquire control of us. We are also subject to certain provisions of the Florida Business Corporation Act and our Articles of Incorporation that relate to business combinations with interested shareowners. Other provisions in our Articles of Incorporation or Bylaws that may discourage takeover attempts or make them more difficult include:

- Supermajority voting requirements to remove a director from office;
- Provisions regarding the timing and content of shareowner proposals and nominations;
- Supermajority voting requirements to amend Articles of Incorporation unless approval is received by a majority of “disinterested directors”;
- Absence of cumulative voting; and

- Inability for shareowners to take action by written consent.

Shares of our common stock are not an insured deposit and may lose value.

The shares of our common stock are not a bank deposit and will not be insured or guaranteed by the FDIC or any other government agency. Your investment will be subject to investment risk, and you must be capable of affording the loss of your entire investment.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

We are headquartered in Tallahassee, Florida. Our executive office is in the Capital City Bank building located on the corner of Tennessee and Monroe Streets in downtown Tallahassee. The building is owned by CCB, but is located on land leased under a long-term agreement.

At December 31, 2018, the Bank had 59 banking offices. Of the 59 locations, the Bank leases the land, buildings, or both at five locations and owns the land and buildings at the remaining 54.

Item 3. Legal Proceedings

We are 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 our consolidated results of operations, financial position, or cash flows.

Item 4. Mine Safety Disclosure.

Not applicable.

PART II

Item 5. Market for the Registrant's Common Equity, Related Shareowner Matters, and Issuer Purchases of Equity Securities

Common Stock Market Prices and Dividends

Our common stock trades on the Nasdaq Global Select Market under the symbol “CCBG.” We had a total of 1,312 shareowners of record at February 28, 2019.

The following table presents the range of high and low closing sales prices reported on the Nasdaq Global Select Market and cash dividends declared for each quarter during the past two years.

	2018				**2017**			
	Fourth Quarter	Third Quarter	Second Quarter	First Quarter	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Common stock price:								
High	$ 26.95	$ 25.91	$ 25.99	$ 26.50	$ 26.01	$ 24.58	$ 22.39	$ 21.79
Low	19.92	23.19	22.28	22.80	22.21	19.60	17.68	19.22
Close	23.21	23.34	23.63	24.75	22.94	24.01	20.42	21.39
Cash dividends per share	0.09	0.09	0.07	0.07	0.07	0.07	0.05	0.05

Florida law and Federal regulations impose restrictions on our ability to pay dividends and limitations on the amount of dividends that the Bank can pay annually to us. See Item 1. "Capital; Dividends; Sources of Strength" and "Dividends" in the Business section on page 12 and 13, Item 1A. "Risks Related to an Investment in Our Common Stock" in the Risk Factors section on page 26, Item 7. "Liquidity and Capital Resources – Dividends" – in Management's Discussion and Analysis of Financial Condition and Operating Results on page 55 and Note 14 in the Notes to Consolidated Financial Statements.

Performance Graph

This performance graph compares the cumulative total shareholder return on our common stock with the cumulative total shareholder return of the Nasdaq Composite Index and the SNL Financial LC $1B-$5B Bank Index for the past five years. The graph assumes that $100 was invested on December 31, 2013 in our common stock and each of the above indices, and that all dividends were reinvested. The shareholder return shown below represents past performance and should not be considered indicative of future performance.

Period Ending

Index	**12/31/13**	**12/31/14**	**12/31/15**	**12/31/16**	**12/31/17**	**12/31/18**
Capital City Bank Group, Inc.	$ 100.00	$ 132.87	$ 132.38	$ 178.52	$ 202.21	$ 207.22
Nasdaq Composite	100.00	114.75	122.74	133.62	173.22	168.30
SNL $1B-$5B Bank Index	100.00	104.56	117.04	168.38	179.51	157.27

Purchases of Equity Securities by the Issuer and Affiliated Purchasers

The following table contains information about all purchases made by, or on behalf of, us and any affiliated purchaser (as defined in Rule 10b-18(a)(3) under the Exchange Act) of shares or other units of any class of our equity securities that is registered pursuant to Section 12 of the Exchange Act.

Period	**Total number of shares purchased**	**Average price paid per share**	**Total number of shares purchased as part of our share repurchase program**[(1)]	**Maximum Number of shares that may yet be purchased under our share repurchase program**
October 1, 2018 to October 31, 2018	-	-	-	639,711
November 1, 2018 to November 30, 2018	-	-	-	639,711
December 1, 2018 to December 31, 2018	324,441	$24.75	324,441	315,270
Total	324,441	$24.75	324,441	315,270

(1) This balance represents the number of shares that were repurchased during the fourth quarter of 2018 through the Capital City Bank Group, Inc. Share Repurchase Program (the “Program”), which was approved on February 27, 2014 for a five year period, under which we were authorized to repurchase up to 1,500,000 shares of our common stock. The Program is flexible and shares are acquired from the public markets and other sources using free cash flow. No shares are repurchased outside of the Program.

Item 6. Selected Financial Data

(Dollars in Thousands, Except Per Share Data)	**2018**	**2017**	**2016**	**2015**	**2014**
Interest Income	$ 99,395	$ 86,930	$ 81,154	$ 79,658	$ 78,221
Net Interest Income	92,504	82,982	77,965	76,351	74,641
Provision for Loan Losses	2,921	2,215	819	1,594	1,905
Noninterest Income(4)	51,565	51,746	53,681	54,091	52,536
Noninterest Expense	111,503	109,447	113,214	115,273	114,358
Net Income(5)	26,224	10,863	11,746	9,116	9,260
Per Common Share:					
Basic Net Income	$ 1.54	$ 0.64	$ 0.69	$ 0.53	$ 0.53
Diluted Net Income	1.54	0.64	0.69	0.53	0.53
Cash Dividends Declared	0.32	0.24	0.17	0.13	0.09
Diluted Book Value	18.00	16.65	16.23	15.93	15.53
Diluted Tangible Book Value(2)	12.96	11.68	11.23	11.00	10.70
Performance Ratios:					
Return on Average Assets	0.92%	0.39%	0.43%	0.34%	0.36%
Return on Average Equity	8.89	3.83	4.22	3.31	3.27
Net Interest Margin (FTE)	3.64	3.37	3.25	3.31	3.36
Noninterest Income as % of Operating Revenues	35.79	38.41	40.78	41.47	41.30
Efficiency Ratio	77.05	80.50	85.34	87.94	89.68
Asset Quality:					
Allowance for Loan Losses	$ 14,210	$ 13,307	$ 13,431	$ 13,953	$ 17,539
Allowance for Loan Losses to Loans	0.80%	0.80%	0.86%	0.93%	1.22%
Nonperforming Assets	9,101	11,100	19,171	29,595	52,449
Nonperforming Assets to Assets	0.31	0.38	0.67	1.06	2.00
Nonperforming Assets to Loans plus OREO	0.51	0.67	1.21	1.94	3.55
Allowance to Nonperforming Loans	206.79	185.87	157.40	135.40	104.60
Net Charge-Offs to Average Loans	0.12	0.14	0.09	0.35	0.53
Capital Ratios:					
Tier 1 Capital	16.36%	16.33%	15.51%	16.42%	16.67%
Total Capital	17.13	17.10	16.28	17.25	17.76
Common Equity Tier 1 Capital(1)	13.58	13.42	12.61	12.84	NA
Tangible Common Equity(2)	7.58	7.09	6.90	6.99	7.38
Leverage	10.89	10.47	10.23	10.65	10.99
Equity to Assets	10.23	9.80	9.67	9.81	10.37
Dividend Pay-Out	20.78	37.50	24.64	24.53	16.98
Averages for the Year:					
Loans, Net of Unearned Income	$ 1,718,348	$ 1,618,583	$ 1,542,232	$ 1,474,833	$ 1,414,000
Earning Assets	2,561,884	2,502,231	2,432,392	2,324,854	2,237,623
Total Assets	2,857,148	2,816,096	2,752,309	2,659,317	2,564,176
Deposits	2,422,973	2,371,871	2,282,785	2,163,441	2,093,477
Shareowners' Equity	294,864	283,404	278,335	275,144	283,079

Year-End Balances:					
Loans, Net of Unearned Income	$ 1,781,094	$ 1,658,309	$ 1,572,175	$ 1,503,907	$ 1,442,062
Earning Assets	2,658,539	2,582,922	2,520,053	2,470,444	2,276,781
Total Assets	2,959,183	2,898,794	2,845,197	2,797,860	2,627,169
Deposits	2,531,856	2,469,877	2,412,286	2,302,849	2,146,794
Shareowners' Equity	302,587	284,210	275,168	274,352	272,540
Other Data:					
Basic Average Shares Outstanding	17,029,420	16,951,663	16,988,747	17,273,406	17,424,788
Diluted Average Shares Outstanding	17,072,329	17,012,637	17,061,186	17,318,184	17,488,020
Shareowners of Record(3)	1,312	1,389	1,489	1,559	1,589
Banking Locations(3)	59	59	60	61	63
Full-Time Equivalent Associates(3)	801	789	820	858	895

(1) *Not applicable prior to January 1, 2015*

(2) *Tangible common equity ratio is a non-GAAP financial measure. For additional information, including a reconciliation to GAAP, refer to page 31*

(3) *As of record date. The record date is on or about March 1st of the following year.*

(4) *Includes $2.5 million gain from sale of trust preferred securities in 2016.*

(5) *For 2017, includes $4.1 million, or $0.24 per diluted share, income tax expense adjustment related to the Tax Cuts and Jobs Act of 2017.*

For 2018, includes $3.3 million, or $0.19 per diluted share, income tax benefit for 2017 plan year pension contributions made in 2018.

NON-GAAP FINANCIAL MEASURES

We present a tangible common equity ratio and a tangible book value per diluted share that, in each case, removes the effect of goodwill that resulted from merger and acquisition activity. We believe these measures are useful to investors because it allows investors to more easily compare our capital adequacy to other companies in the industry. The GAAP to non-GAAP reconciliation for selected year-to-date financial data and quarterly financial data is provided below.

Non-GAAP Reconciliation - Selected Financial Data

(Dollars in Thousands, except per share data)		**2018**	**2017**	**2016**	**2015**	**2014**
Shareowners' Equity (GAAP)		$ 302,587	$ 284,210	$ 275,168	$ 274,352	$ 272,540
Less: Goodwill (GAAP)		84,811	84,811	84,811	84,811	84,811
Tangible Shareowners' Equity (non-GAAP)	A	217,776	199,399	190,357	189,541	187,729
Total Assets (GAAP)		2,959,183	2,898,794	2,845,197	2,797,860	2,627,169
Less: Goodwill (GAAP)		84,811	84,811	84,811	84,811	84,811
Tangible Assets (non-GAAP)	B	$ 2,874,372	$ 2,813,983	$ 2,760,386	$ 2,713,049	$ 2,542,358
Tangible Common Equity Ratio (non-GAAP)	**A/B**	**7.58%**	**7.09%**	**6.90%**	**6.99%**	**7.38%**
Actual Diluted Shares Outstanding (GAAP)	C	16,808,542	17,071,107	16,949,359	17,226,178	17,544,306
Tangible Book Value per Diluted Share (non-GAAP)	**A/C**	**12.96**	**11.68**	**11.23**	**11.00**	**10.70**

Non-GAAP Reconciliation - Quarterly Financial Data

(Dollars in Thousands, except per share data)		**2018**				**2017**			
		Fourth	**Third**	**Second**	**First**	**Fourth**	**Third**	**Second**	**First**
Shareowners' Equity (GAAP)		$ 302,587	$ 298,016	$ 293,571	$ 288,360	$ 284,210	$ 285,201	$ 281,513	$ 278,05
Less: Goodwill (GAAP)		84,811	84,811	84,811	84,811	84,811	84,811	84,811	84,81
Tangible Shareowners' Equity (non-GAAP)	A	217,776	213,205	208,760	203,549	199,399	200,390	196,702	193,24
Total Assets (GAAP)		2,959,183	2,819,190	2,880,278	2,924,832	2,898,794	2,790,842	2,814,843	2,895,53
Less: Goodwill (GAAP)		84,811	84,811	84,811	84,811	84,811	84,811	84,811	84,81
Tangible Assets	B	$ 2,874,372	$ 2,734,379	$ 2,795,467	$ 2,840,021	$ 2,813,983	$ 2,706,031	$ 2,730,032	$ 2,810,72

(non-GAAP)									
Tangible Common Equity Ratio (non-GAAP)	**A/B**	**7.58%**	**7.80%**	**7.47%**	**7.17%**	**7.09%**	**7.41%**	**7.21%**	**6.88%**
Actual Diluted Shares Outstanding (GAAP)	C	16,808,542	17,127,846	17,114,380	17,088,419	17,071,107	17,045,326	17,025,148	16,978,68
Tangible Book Value per Diluted Share (non-GAAP)	**A/C**	**12.96**	**12.45**	**12.20**	**11.91**	**11.68**	**11.76**	**11.55**	**11.3**

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Item 7. 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 included in the Annual Report on Form 10-K. The MD&A is divided into subsections entitled "Business Overview," "Executive Overview," "Results of Operations," "Financial Condition," "Liquidity and Capital Resources," "Off-Balance Sheet Arrangements," "Fourth Quarter, 2018 Financial Results," and "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 2018 compares with prior years. Throughout this section, Capital City Bank Group, Inc., and its subsidiaries, collectively, are referred to as "CCBG," "Company," "we," "us," or "our."

CAUTION CONCERNING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K, 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," 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 this Annual Report for a discussion of factors that could cause our actual results to differ materially from those in the forward-looking statements.

However, other factors besides those listed in *Item 1A Risk Factors* or discussed in this 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

General

We are a financial holding company headquartered in Tallahassee, Florida, and we are the parent of our wholly owned subsidiary, Capital City Bank (the "Bank" or "CCB"). We offer a broad array of products and services, including commercial and retail banking services, trust and asset management, and retail securities brokerage through a total of 59 banking offices located in Florida, Georgia, and Alabama. Please see the section captioned "About Us" beginning on page 4 for more detailed information about our business.

Our profitability, like most financial institutions, is dependent to a large extent upon net interest income, which is the difference between the interest and fees received on interest 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 deposit fees, wealth management fees, mortgage banking fees, and bank card fees.

Strategic Review

Our philosophy is to build long-term client relationships based on quality service, high ethical standards, and safe and sound banking practices. We maintain a locally oriented, community-based focus, which is augmented by experienced, centralized support in select specialized areas. Our local market orientation is reflected in our network of banking office locations, experienced community executives with a dedicated President for each market, and community boards which support our focus on responding to local banking needs. We strive to offer a broad array of sophisticated products and to provide quality service by empowering associates to make decisions in their local markets.

We have sought to build a franchise in small-to medium-sized, less competitive markets, located on the outskirts of the larger metropolitan markets where we are positioned as a market leader. Many of our markets are on the outskirts of these larger markets in close proximity to major interstate thoroughfares such as Interstates I-10 and I-75. Our three largest markets are Tallahassee (Leon County, Florida), Gainesville (Alachua County, Florida), and Macon (Bibb County, Georgia). In 13 of 18 markets in Florida and two of four markets in Georgia, we rank within the top four banks in terms of deposit market share. Furthermore, in the counties in which we operate, we maintain a 8.30% deposit market share in the Florida counties and 5.11% in the Georgia counties, suggesting that there is significant opportunity to grow market share within these geographic areas. The larger employers in many of our markets are state and local governments, healthcare providers, educational institutions, and small businesses. While we realize that the markets in our footprint do not provide for potential growth that the larger metropolitan markets may offer, we believe our markets do provide good growth dynamics and have historically grown in excess of the national average The value of these markets stems from the fact they are generally stable and less competitive, secondary markets. We strive to provide value added services to our clients by being not just their bank, but their banker. We believe this element of our strategy distinguishes Capital City Bank from our competitors.

Our long-term vision remains to profitably expand our franchise through a combination of organic growth in existing markets and acquisitions. We have long understood that our core deposit funding base is a predominant driver of our profitability and overall franchise value, and have focused extensively on this component of our organic growth efforts in recent years. While we have not been an active acquirer of banks since 2005, this component of our strategy is still in place. When evaluating potential acquisition opportunities, we will continue to weigh the value of organic growth initiatives versus potential acquisition returns and pursue the strategies that we believe provide the best overall return to our shareowners.

We will continue to evaluate potential acquisition opportunities in Florida, Georgia, and Alabama with a particular focus on financial institutions located on the outskirts of larger, metropolitan areas. The primary areas that we are focusing on for expansion opportunities include Alachua, Marion, Hernando/Pasco counties in Florida, the western panhandle of Florida, and Bibb and surrounding counties in central Georgia. Our focus on some of these markets may change as we continue to evaluate our strategy and the economic conditions and demographics of any individual market. We will also continue to evaluate de novo expansion opportunities in attractive new markets where acquisition opportunities are not feasible. We may also evaluate expansion opportunities including asset management, mortgage banking, and other financial businesses that are closely aligned with the business of banking. Embedded in our acquisition strategy is our desire to partner with institutions that are culturally similar, have experienced management and possess either established market presence or have potential for improved profitability through growth, economies of scale, or expanded services. Generally, these potential target institutions will range in asset size from $100 million to $500 million.

EXECUTIVE OVERVIEW

2018 again produced marked improvement in our financial performance moving us closer to our normal historical performance levels. Record loan growth, a rising rate environment, our strong core deposit base, and tax reform were all major contributors to earnings growth. Our net interest margin increased 27 basis points aided by our

asset-sensitive balance sheet and our ability to manage our cost of funds. Average deposit balances grew 2.1% in 2018, our fifth consecutive year of growth, and have grown approximately $351 million, or 17% since 2013.

For 2018, net income totaled $26.2 million, or $1.54 per diluted share, compared to net income of $10.9 million, or $0.64 per diluted share for 2017. Net income for 2018 included tax benefits totaling $3.3 million, or $0.19 per diluted share related to 2017 plan year pension plan contributions made during 2018. Net income in 2017 reflected a $4.1 million, or $0.24 per diluted share, income tax expense related to the tax reform act commonly known as Tax Cuts and Jobs Act (the “Tax Act”) enacted on December 22, 2017.

Net income for 2018 was driven by higher net interest income of $9.5 million and an $8.8 million reduction in income tax expense, partially offset by a $2.1 million increase in noninterest expense, a $0.7 million increase in the loan loss provision, and lower noninterest income of $0.2 million.

Below are summary highlights that impacted our performance for the year:

- *Continued improvement in operating leverage driven by margin expansion*
  - *Net interest income up $9.5 million, or 11.5%*
  - *Net interest margin up 27 basis points to 3.64%*
  - *Record average loan growth of $100 million, or 6.2%*
- *Average deposit growth of 2% (fifth consecutive year of growth)*
- *Continued reduction in classified assets of 28%*
- *Tangible capital ratio of 7.58%*
- *Tangible book value per share growth of 11%*
- *Repurchased 324,000 shares of common stock*
- *Dividend growth of 33%*

In 2018, we realized record loan growth driven by continued improvement in economic and business conditions in our markets. We again realized meaningful re-composition in our earning asset mix which drove strong growth in net interest income, up 11% over 2017 and our net interest margin which was up 27 basis points to 3.64%.

For 2018, noninterest income declined $0.2 million, or 0.3%, however we made great strides toward stabilizing the downward trend in our noninterest income driven by lower deposit fees, specifically lower utilization of our overdraft service, and the discontinuance of our data processing business in 2016 and 2017. Several initiatives came to fruition in 2018 including the introduction of a new fee based checking account line-up in mid-2018 and improved utilization of our debit card product which drove improvement in service charges and interchange fees, respectively. Higher wealth management fees also contributed and reflected growth in assets under management. We continue to evaluate opportunities to enhance noninterest income, including leveraging our working capital finance platform to all of our markets, a supply chain finance service, and government guaranteed small business lending.

Noninterest expense increased $2.1 million, or 1.9%, over 2017 primarily attributable to higher compensation expense of $1.6 million and occupancy expense of $0.7 million, partially offset by a $0.2 million decline in other expense. The primary drivers of the increase were higher performance based compensation reflective of our improved financial performance and professional fees related to a system conversion and profit enhancement projects that were complete at year-end.

Overall asset quality continued to improve in 2018 as nonperforming and classified asset levels declined by 18% and 28%, respectively. Our ratio of nonperforming assets to total assets was 0.31% at December 31, 2018 compared to 0.38% at December 31, 2017. Loan losses remained low in 2018 at 12 basis points of average loans.

We continue to focus on and implement strategic initiatives that enhance long-term shareowner value and believe we are well positioned to continue improving our operating leverage and returning to our historical norm of profitability.

Key components of our 2018 financial performance are summarized below:

Results of Operations

- For 2018, tax-equivalent net interest income increased $9.0 million, or 10.6%, to $93.2 million driven by higher interest rates and a favorable shift in the earning asset mix. Higher rates were earned on overnight funds, investment securities and loans, partially offset by a higher cost on our negotiated rate deposits. Our net interest margin of 3.64% in 2018 increased 27 basis points over 2017 and reflected a 39 basis point increase in the earning asset yield that was partially offset by a 12 basis point increase in the cost of funds.

- For 2018, our loan loss provision was $2.9 million compared to $2.2 million for 2017 with the increase driven by growth in the loan portfolio. At December 31, 2018, our allowance for loan losses of $14.2 million represented 0.80% of outstanding loans (net of overdrafts) and provided coverage of 207% of nonperforming loans compared to 0.80% and 186%, respectively, at December 31, 2017.

- For 2018, noninterest income totaled $51.6 million, a $0.2 million, or 0.3%, decrease from 2017, and reflected lower mortgage banking fees of $1.0 million, partially offset by higher other income of $0.4 million and wealth management fees of $0.4 million. The lower level of mortgage banking fees reflected a lower level of loans sold in secondary market as adjustable rate loan production has picked up momentum and is being retained in our loan portfolio instead of sold on the secondary market. Total residential loan production (secondary market sales and portfolio) during 2018 was comparable to 2017.

- For 2018, noninterest expense totaled $111.5 million, an increase of $2.1 million, or 1.9%, over 2017 attributable to higher compensation expense of $1.6 million and occupancy expense of $0.7 million, partially offset by lower other expense of $0.2 million.

Financial Condition

- Average assets totaled approximately $2.857 billion for 2018, an increase of $41.1 million, or 1.5%, over 2017. Average earning assets were approximately $2.562 billion for 2018, an increase of $59.7 million, or 2.4% over 2017. Year-over-year, average overnight funds decreased $54.6 million, while investment securities increased $14.5 million and average gross loans were higher by $99.8 million.

- Average gross loans totaled $1.718 billion in 2018, an increase of $99.8 million, or 6.2%, over 2017. Loans as a percentage of average earning assets increased to 67.1% in 2018 compared to 64.7% in 2017. We realized growth in all loan categories except home equity loans. A portion of the increase in 2018 was due to strategic loan pool purchases of approximately $26.1 million in adjustable residential real estate loans and fixed and adjustable rate commercial real estate loans.

- Average total deposits for 2018 were $2.423 billion, an increase of $51.1 million, or 2.2%, over 2017. The increase occurred in noninterest bearing and savings accounts, partially offset by the declines in the remaining product types. 2018 was the fifth consecutive year that we have realized growth in our average deposit balances.

- At December 31, 2018, our nonperforming assets (nonaccrual loans and OREO) totaled $9.1 million, a decrease of $2.0 million, or 18.0% from December 31, 2017. Nonaccrual loans totaled $6.9 million at December 31, 2018, a $0.3 million decrease from December 31, 2017. The balance of OREO totaled $2.2 million at December 31, 2018, a decrease of $1.7 million from December 31, 2017. Nonperforming assets represented 0.31% of total assets at December 31, 2018 compared to 0.38% at December 31, 2017.

- At December 31, 2018, our allowance for loan losses of $14.2 million represented 0.80% of outstanding loans (net of overdrafts) and provided coverage of 207% of nonperforming loans compared to 0.80% and 186%, respectively, at December 31, 2017. For 2018, our net loan charge-offs totaled $2.0 million, or 0.12%, of average loans, compared to $2.3 million, or 0.14%, for 2017.

- Shareowners' equity increased by $18.4 million from $284.2 million at December 31, 2017 to $302.6 million at December 31, 2018. We continue to maintain a strong capital base as evidenced by a risk-based capital ratio of 17.13% and tangible common equity ratio of 7.58% at December 31, 2018 compared to 17.10% and 7.09%, respectively, at December 31, 2017. At December 31, 2018, all of our regulatory capital ratios significantly exceeded the threshold to be well-capitalized.

RESULTS OF OPERATIONS

For 2018, we realized net income of $26.2 million, or $1.54 per diluted share, compared to net income of $10.9 million, or $0.64 per diluted share for 2017, and $11.7 million, or $0.69 per diluted share in 2016.

The increase in net income for 2018 was attributable to a $9.5 million increase in net interest income and an $8.8 million reduction in income tax expense, partially offset by a $2.1 million increase in noninterest expense, a $0.7 million increase in the loan loss provision, and lower noninterest income of $0.2 million. Income tax expense for 2018 reflected the favorable impact of the Tax Act, including a lower federal corporate tax rate and one-time discrete tax benefits totaling $3.3 million, or $0.19 per diluted share related to 2017 plan year pension contributions made during 2018.

The decrease in net income for 2017 reflected higher income tax expense of $6.3 million, primarily due to discrete tax expense of $4.1 million related to the Tax Act, a $1.9 million decrease in noninterest income, and a $1.4 million increase in the loan loss provision, partially offset by higher net interest income of $5.0 million and a $3.8 million reduction in noninterest expense.

A condensed earnings summary for the last three years is presented in Table 1 below:

Table 1
CONDENSED SUMMARY OF EARNINGS

(Dollars in Thousands, Except Per Share Data)		**2018**		**2017**		**2016**
Interest Income	$	99,395	$	86,930	$	81,154
Taxable Equivalent Adjustments		654		1,226		1,011
Total Interest Income (FTE)		100,049		88,156		82,165
Interest Expense		6,891		3,948		3,189
Net Interest Income (FTE)		93,158		84,208		78,976
Provision for Loan Losses		2,921		2,215		819
Taxable Equivalent Adjustments		654		1,226		1,011
Net Interest Income After Provision for Loan Losses		89,583		80,767		77,146
Noninterest Income		51,565		51,746		53,681
Noninterest Expense		111,503		109,447		113,214
Income Before Income Taxes		29,645		23,066		17,613
Income Tax Expense		3,421		12,203		5,867
Net Income	$	26,224	$	10,863	$	11,746
Basic Net Income Per Share	$	1.54	$	0.64	$	0.69
Diluted Net Income Per Share	$	1.54	$	0.64	$	0.69

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. We provide an analysis of our net interest income, including average yields and rates in Tables 2 and 3 below. We provide this information on a "taxable equivalent" basis to reflect the tax-exempt status of income earned on certain loans and investments.

In 2018, our taxable equivalent net interest income increased $9.0 million, or 10.6%. This follows increases of $5.2 million, or 6.6% and $2.0 million, or 2.6%, in 2017 and 2016, respectively. The year-over-year increases generally resulted from growth in our loan and investment portfolios. In 2017 and 2018, the increase also reflected favorable repricing of our adjustable and variable rate earning assets, partially offset by an increase in our negotiated rate deposits.

For 2018, taxable equivalent interest income increased $11.9 million, or 13.5%, over 2017. In 2017, taxable equivalent interest income increased $6.0 million, or 7.3%, over 2016. The increases in both comparisons were primarily due to higher balances in the loan and investment portfolios coupled with higher rates.

Interest expense increased $2.9 million, or 74.5%, from 2017 to 2018, and increased $0.8 million, or 23.8%, from 2016 to 2017. The increase over both prior periods primarily reflected increases to our negotiated rate deposits which are tied to an adjustable rate index. Our cost of funds increased 11 basis points to 27 basis points in 2018 compared to 2017 and increased three basis points over 2016 to 16 basis points in 2017. The increased cost of funds over both prior periods was primarily due to higher interest rates paid on our negotiated rate products due to the recent rising interest rate environment.

Our interest rate spread (defined as the taxable-equivalent yield on average earning assets less the average rate paid on interest bearing liabilities) increased 18 basis points in 2018 compared to 2017 and increased nine basis points in 2017 compared to 2016. Our net interest margin (defined as taxable-equivalent interest income less interest expense divided by average earning assets) of 3.64% in 2018 was a 27 basis point increase over 2017. The net interest margin of 3.37% in 2017 was a 12 basis point increase over 2016. The increase in interest rate spread and net interest margin over both prior year periods is attributable to rising rates and an improving mix of earning assets driven by loan growth.

The Federal Open Market Committee (FOMC) increased the federal funds target rate four times in 2018 to end the year with a target rate in the range of 2.25%-2.50%, which followed three rate increases in 2017. These rate increases have positively affected our net interest income due to favorable repricing of our variable and adjustable rate earning assets, and our asset sensitive balance sheet. Although these rate increases resulted in higher rates paid on our negotiated rate deposit products, we continue to monitor and manage our overall cost of funds. Despite highly competitive loan pricing across most markets, the yield of the overall loan portfolio has increased year-over-year.

We continue to review and implement various loan strategies that align with our overall risk appetite to enhance our performance. We continue to maintain short duration portfolios on both sides of the balance sheet and believe we are well positioned to respond to changing market conditions.

Table 2
AVERAGE BALANCES AND INTEREST RATES

	2018			**2017**			**2016**		
(Taxable Equivalent Basis - Dollars in Thousands)	**Average Balance**	**Interest**	**Average Rate**	**Average Balance**	**Interest**	**Average Rate**	**Average Balance**	**Interest**	**Avera Rat**
ASSETS									
Loans, Net of Unearned Income[(1)(2)]	$ 1,718,348	$ 84,550	4.92%	$ 1,618,583	$ 76,385	4.72%	$ 1,542,232	$ 73,417	4.76
Taxable Investment Securities	641,120	12,083	1.88	595,790	8,095	1.36	586,284	6,317	1.08
Tax-Exempt Investment Securities[(2)]	67,037	1,006	1.50	97,867	1,610	1.65	91,059	1,327	1.46
Funds Sold	135,379	2,410	1.78	189,991	2,066	1.09	212,817	1,104	0.52
Total Earning Assets	2,561,884	100,049	3.91%	2,502,231	88,156	3.52%	2,432,392	82,165	3.38
Cash & Due From Banks	51,222			51,091			47,447		
Allowance for Loan Losses	(13,993)			(13,541)			(14,080)		
Other Assets	258,035			276,315			286,550		
TOTAL ASSETS	$ 2,857,148			$ 2,816,096			$ 2,752,309		
LIABILITIES									
NOW Accounts	$ 781,026	$ 3,152	0.40%	$ 805,861	$ 1,094	0.14%	$ 779,764	$ 292	0.04
Money Market Accounts	251,175	675	0.27	258,304	252	0.10	256,265	120	0.05
Savings Accounts	351,341	172	0.05	323,928	159	0.05	292,326	144	0.05
Time Deposits	131,860	244	0.18	151,301	284	0.19	168,741	323	0.19
Total Interest Bearing Deposits	1,515,402	4,243	0.29%	1,539,394	1,789	0.12%	1,497,096	879	0.06
Short-Term Borrowings	10,992	110	0.99	9,927	82	0.82	36,762	148	0.40
Subordinated Notes Payable	52,887	2,167	4.04	52,887	1,634	3.05	55,729	1,434	2.53
Other Long-Term Borrowings	12,387	371	3.00	15,174	443	2.92	23,880	728	3.05
Total Interest Bearing Liabilities	1,591,668	6,891	0.45%	1,617,382	3,948	0.25%	1,613,467	3,189	0.20
Noninterest Bearing Deposits	907,571			832,477			785,689		
Other Liabilities	63,045			82,833			74,818		
TOTAL LIABILITIES	2,562,284			2,532,692			2,473,974		
SHAREOWNERS' EQUITY									
TOTAL SHAREOWNERS' EQUITY	294,864			283,404			278,335		
TOTAL LIABILITIES & EQUITY	$ 2,857,148			$ 2,816,096			$ 2,752,309		
Interest Rate Spread			3.46%			3.27%			3.18
Net Interest Income		$ 93,158			$ 84,208			$ 78,976	
Net Interest Margin[(3)]			3.64%			3.37%			3.25

(1) *Average balances include nonaccrual loans. Interest income includes loan fees of $1.0 million for 2018, $0.7 million for 2017, and $0.8 million for 2016.*
(2) *Interest income includes the effects of taxable equivalent adjustments using a 21% tax rate for 2018 and a 35% tax rate for 2017 and 2016.*
(3) *Taxable equivalent net interest income divided by average earning assets.*

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Table 3
RATE/VOLUME ANALYSIS[1]

	2018 vs. 2017 Increase (Decrease) Due to Change In			2017 vs. 2016 Increase (Decrease) Due to Change In			
(Taxable Equivalent Basis - Dollars in Thousands)	**Total**	**Volume**	**Rate**	**Total**	**Calendar**[3]	**Volume**	**Rate**
Earnings Assets:							
Loans, Net of Unearned Interest[2]	$ 8,165	$ 4,708	$ 3,457	$ 2,968	$ (201)	$ 3,836	$ (667)
Investment Securities:							
Taxable	3,988	616	3,372	1,778	(14)	119	1,673
Tax-Exempt[2]	(604)	(507)	(97)	283	(3)	103	183
Funds Sold	344	(594)	938	962	(2)	(115)	1,079
Total	11,893	4,223	7,670	5,991	(220)	3,943	2,268
Interest Bearing Liabilities:							
NOW Accounts	2,058	(34)	2,092	802	(1)	11	792
Money Market Accounts	423	(7)	430	132	-	1	131
Savings Accounts	13	13	-	15	-	16	(1)
Time Deposits	(40)	(36)	(4)	(39)	(1)	(32)	(6)
Short-Term Borrowings	28	9	19	(66)	-	(108)	42
Subordinated Notes Payable	533	-	533	200	(4)	(69)	273
Other Long-Term Borrowings	(72)	(81)	9	(285)	(3)	(262)	(20)
Total	2,943	(136)	3,079	759	(9)	(443)	1,211
Changes in Net Interest Income	$ 8,950	$ 4,359	$ 4,591	$ 5,232	$ (211)	$ 4,386	$ 1,057

(1) *This table shows the change in taxable equivalent net interest income for comparative periods based on either changes in average volume or changes in average rates for interest earning assets and interest-bearing liabilities. Changes which are not solely due to volume changes or solely due to rate changes have been attributed to rate changes.*

(2) *Interest income includes the effects of taxable equivalent adjustments using a 21% tax rate to adjust interest for 2018 and a 35% tax rate for 2017 to adjust interest on tax-exempt loans and securities to a taxable equivalent basis.*

(3) Reflects change due to one extra calendar day in 2016.

Provision for Loan Losses

Our provision for loan loss was $2.9 million for 2018 compared to $2.2 million for 2017 and $0.8 million in 2016. The increase in 2018 was driven by growth of our loan portfolio. The increase in 2017 reflected higher net loan charge-offs and growth of our loan portfolio. We discuss these trends in further detail below under Risk Element Assets and Allowance for Loan Losses.

Noninterest Income

For 2018, noninterest income totaled $51.6 million, a $0.2 million, or 0.3%, decrease from 2017, and reflected lower mortgage banking fees of $1.0 million, partially offset by higher other income of $0.4 million and wealth management fees of $0.4 million. The lower level of mortgage banking fees was due to a reduction in the volume of loans sold in secondary market as adjustable rate loan production picked up momentum and is being retained in our loan portfolio instead of sold on the secondary market. Total residential loan production (secondary market sales and portfolio) during 2018 was comparable to 2017. The increase in other income reflected higher signing bonus income from processing contracts and miscellaneous income. The increase in wealth management fees was attributable to higher trust fees and reflected growth in assets under management.

For 2017, noninterest income totaled $51.7 million, a decrease of $1.9 million, or 3.6%, from 2016 attributable to lower other income of $2.7 million and deposit fees of $1.0 million, partially offset by higher wealth management fees of $1.2 million and mortgage banking fees of $0.6 million. The decrease in other income was attributable to a $2.5 million gain from the partial retirement of our trust preferred securities in the second quarter of 2016. Lower fees related to data processing services provided to third parties also contributed to the decrease and reflected the discontinuance of this line of business over the past two years with our last client discontinuing service in the fourth quarter of 2017. The reduction in deposit fees reflected lower utilization of our overdraft service product. Growth in assets under management as well as improved sales efforts have resulted in strong growth in wealth management fees. Strong home sales in our markets and a growing market share of residential loan production drove the improvement in mortgage banking fees.

Noninterest income as a percent of total operating revenues (net interest income plus noninterest income) was 35.79% in 2018, 38.41% in 2017, and 40.78% in 2016. The decline in this metric over the last three years was attributable to growth in net interest income as a component of operating revenues.

The table below reflects the major components of noninterest income.

(Dollars in Thousands)	**2018**	**2017**	**2016**
Deposit Fees	$ 20,093	$ 20,335	$ 21,332
Bank Card Fees	11,378	11,191	11,221
Wealth Management Fees	8,711	8,284	7,029
Mortgage Banking Fees	4,735	5,754	5,192
Other	6,648	6,182	8,907
Total Noninterest Income	$ 51,565	$ 51,746	$ 53,681

Various significant components of noninterest income are discussed in more detail below.

Deposit Fees. For 2018, deposit fees (service charge fees, insufficient fund/overdraft fees (“NSF/OD”), and business account analysis fees) totaled $20.1 million compared to $20.3 million in 2017 and $21.3 million in 2016. The $0.2 million, or 1.2%, decrease in 2018 reflected lower NSF/OD fees that were significantly offset by higher service charge fees. In mid-2018, we introduced a new fee-based checking account line-up which has enhanced our service charge fees and stabilized our total deposit fee revenues. The decrease in 2017 was due to a lower level of NSF/OD fees attributable to a reduction in the number of accounts using our overdraft protection service and lower utilization by existing users reflecting improved financial management by our clients.

Bank Card Fees. Bank card fees totaled $11.4 million in 2018 compared to $11.2 million in 2017 and 2016. We have implemented initiatives over the past three years aimed at stabilizing our bank card fee revenues and in 2018 realized growth. The aforementioned new checking account line-up introduced in mid-2018 will continue to have a favorable

impact on this fee source as well as strategies aimed at acquiring new deposit relationships.

Wealth Management Fees. Wealth management fees including both trust fees (i.e., managed accounts and trusts/estates) and retail brokerage fees (i.e., investment, insurance products, and retirement accounts) totaled $8.7 million in 2018 compared to $8.3 million in 2017 and $7.0 million in 2016. The growth in fees for both 2018 and 2017 was attributable to growth in assets under management. At December 31, 2018, total assets under management were approximately $1.500 billion compared to $1.418 billion at December 31, 2017 and $1.192 billion at December 31, 2016.

Mortgage Banking Fees. Mortgage banking fees totaled $4.7 million in 2018 compared to $5.8 million in 2017 and $5.2 million in 2016. The decrease in 2018 was attributable to a reduction in the volume of loans sold in secondary market as adjustable rate loan production has picked up momentum and is being retained in our loan portfolio instead of sold on the secondary market. Total residential loan production (secondary market sales and portfolio) during 2018 was comparable to 2017. The increase in 2017 reflected strong home sales in our markets and a growing market share of residential loan production. Refinancing activity represented 11% of our loan production in 2018 and 2017compared to 20% for 2016. Market conditions, housing activity, the level of interest rates and the mix of our fixed-rate and variable rate production have significant impacts on our mortgage banking fees.

Other. Other noninterest income totaled $6.6 million in 2018 compared to $6.2 million in 2017 and $8.9 million in 2016. The $0.4 million, or 7.5%, increase over 2017 reflected higher signing bonus income from processing contracts that have been renegotiated and miscellaneous income. The decrease in 2017 was attributable to a $2.5 million gain from the partial retirement of our trust preferred securities in the second quarter of 2016. Lower fees related to data processing services provided to third parties also contributed to the decrease and reflected the discontinuance of this line of business over the two year period (2016-2017) with our last client discontinuing service in the fourth quarter of 2017.

Noninterest Expense

For 2018, noninterest expense totaled $111.5 million, an increase of $2.1 million, or 1.9%, over 2017 attributable to higher compensation expense of $1.6 million and occupancy expense of $0.7 million, partially offset by lower other expense of $0.2 million. Higher salary expense, primarily cash incentives, drove the increase in compensation expense. Occupancy expense increased due to higher equipment/software maintenance agreement expense and to a lesser extent an increase in building maintenance costs (partly related to Hurricane Michael). The decrease in other expense was primarily attributable to lower OREO expense of $1.6 million, partially offset by higher professional fees of $1.3 million. Higher net gains from property sales drove the improvement in OREO expense. The increase in professional fees reflected costs associated with several consulting projects, including both profit enhancements projects and the upgrading of ancillary systems, all of which were complete at the end of the third quarter of 2018.

For 2017, noninterest expense totaled $109.4 million, a decrease of $3.8 million, or 3.3%, from 2016 attributable to lower other expense of $2.9 million (primarily OREO, legal, and FDIC insurance), occupancy expense of $0.5 million, and compensation expense of $0.4 million. All OREO expense categories (gain/loss on sale, carrying costs, and valuation adjustments) declined as we continued efforts to liquidate our remaining properties. Legal and FDIC insurance expense declined as expected as these categories return closer to our historical norm, post-recession. The decrease in occupancy expense reflected our continuing efforts to optimize our banking office structure and operational processes. The decrease in compensation expense reflected lower salary expense of $1.2 million, partially offset by higher associate benefit expense of $0.8 million.

Our operating efficiency ratio (expressed as noninterest expense as a percent of taxable equivalent net interest income plus noninterest income) was 77.05%, 80.50% and 85.34% in 2018, 2017 and 2016, respectively. Improved operating leverage primarily attributable to growth in net interest income has driven the improvement for all respective years.

Expense management is an important part of our culture and strategic focus. We will continue to review and evaluate opportunities to optimize our operations, reduce operating costs and manage our discretionary expenses.

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The table below reflects the major components of noninterest expense.

(Dollars in Thousands)	**2018**	**2017**	**2016**
Salaries	$ 48,087	$ 46,421	$ 47,610
Associate Benefits	15,834	15,892	15,124
Total Compensation	63,921	62,313	62,734
Premises	8,913	8,790	9,047
Equipment	9,590	9,047	9,249
Total Occupancy	18,503	17,837	18,296
Legal Fees	2,055	1,933	2,311
Professional Fees	5,003	3,689	3,424
Processing Services	5,978	6,253	6,471
Advertising	1,611	1,731	1,702
Travel and Entertainment	974	868	889
Printing and Supplies	642	631	710
Telephone	2,224	2,405	2,296
Postage	703	764	891
Insurance – Other	1,625	1,626	2,060
Other Real Estate, Net	(442)	1,135	3,649
Miscellaneous	8,706	8,262	7,781
Total Other Expense	29,079	29,297	32,184
Total Noninterest Expense	$ 111,503	$ 109,447	$ 113,214

Various significant components of noninterest expense are discussed in more detail below.

Compensation. Compensation expense totaled $63.9 million in 2018, $62.3 million in 2017, and $62.7 million in 2016. For 2018, the $1.6 million, or 2.6%, increase over 2017 reflected higher salary expense of $1.7 million, partially offset by lower associate benefit expense of $0.1 million. A higher level of cash incentives which reflected improved financial performance drove a significant portion of the increase in salary expense. Slightly higher base salaries and contractual employment also contributed to the increase, but to a lesser extent.

For 2017, the $0.4 million, or 0.7%, decrease from 2016 reflected lower salary expense of $1.2 million, partially offset by higher associate benefit expense of $0.8 million. Continued headcount attrition drove the decline in salary expense and the increase in associate benefit expense reflected higher pension plan expense attributable to utilization of a lower discount rate for plan liabilities and to a lesser extent higher associate insurance expense and stock compensation expense.

Occupancy. Occupancy expense (including premises and equipment) totaled $18.5 million for 2018, $17.8 million for 2017, and $18.3 million for 2016. For 2018, the $0.7 million, or 3.7%, increase over 2017 was attributable to higher equipment/software maintenance agreement expense and to a lesser extent an increase in building maintenance costs (partly related to Hurricane Michael). For 2017, the $0.5 million, or 2.5%, decrease from 2016 generally reflected our continuing efforts to optimize our banking office structure and operational processes.

Other. Other noninterest expense totaled $29.1 million in 2018, $29.3 million in 2017, and $32.2 million in 2016. For 2018, the $0.2 million, or 0.7%, decrease primarily reflected lower OREO expense of $1.6 million, partially offset by higher professional fees of $1.3 million. A higher level of net gains (higher gains of $1.2 million and lower losses of $0.2 million) from the sale of properties drove the reduction in OREO expense. During 2018, we sold a banking office in our Tallahassee market which resulted in a $2.0 million gain. The increase in professional fees reflected costs associated with several consulting projects, including both profit enhancements projects and the upgrading of ancillary systems, all of which were essentially complete at the end of the third quarter of 2018.

For 2017, the $2.9 million, or 9.0%, decrease was primarily attributable to lower OREO expense of $2.5 million, FDIC insurance fees of $0.4 million, and legal fees of $0.4 million. Lower valuation adjustments of $1.0 million, and net gains from the sale of properties of $1.4 million (higher gains of $0.6 million and lower losses of $0.8 million) drove the reduction in OREO expense. The reduction in FDIC insurance fees reflected a reduction in our premium. Legal expense declined due to a lower level of support needed for problem loan resolutions.

Income Taxes

For 2018, we realized income tax expense of $3.4 million (12% effective rate) compared to $12.2 million (53% effective rate) for 2017 and $5.9 million (33% effective rate) for 2016. On December 22, 2017, the Tax Act was signed into law. Among other things, the Tax Act reduced our corporate federal tax rate from 35% to 21% effective January 1, 2018. As a result, we were required to re-measure, through income tax expense, our deferred tax assets and liabilities using the enacted rate at which we expect them to be recovered or settled. We recorded an adjustment in the amount of $4.1 million in the fourth quarter of 2017 for the re-measurement of our deferred tax inventory. Income tax expense for 2017 also included a $0.3 million write-off of a deferred tax asset related to a cancelled stock award as well as income tax benefits of $0.2 million related to stock-based compensation awards. During 2018, income tax expense included four discrete tax benefit items totaling $3.6 million resulting from the effect of the Tax Act. Three discrete items totaling $3.3 million related to pension plan contributions made in 2018 for the plan year 2017. In addition, we realized a discrete tax item for $0.3 million related to a tax accounting method change, for a cost segregation and depreciation analysis for various properties we own which was filed with the extended 2017 tax return. Excluding discrete items, our effective tax rate was 24% for 2018 and 36% for 2017. Absent future discrete events, we anticipate that our effective tax will approximate 24%.

FINANCIAL CONDITION

Average assets totaled approximately $2.857 billion for 2018, an increase of $41.1 million, or 1.5%, over 2017. Average earning assets were approximately $2.562 billion for 2018, an increase of $59.7 million, or 2.4% over 2017. Year-over-year, average overnight funds decreased $54.6 million, while investment securities increased $14.5 million and average loans were higher by $99.8 million. We discuss these variances in more detail below.

Table 2 provides information on average balances and rates, Table 3 provides an analysis of rate and volume variances and Table 4 highlights the changing mix of our interest earning assets over the last three years.

Loans

In 2018, average loans increased $99.8 million, or 6.2%, compared to an increase of $76.4 million, or 5.0%, in 2017. Loans as a percentage of average earning assets increased to 67.1% in 2018 compared to 64.7% in 2017 and 63.4% in 2016. Year-over-year average balances in the loan portfolio experienced increases in all loan categories except home equity loans. Over the course of 2018, we purchased both adjustable rate residential loans and fixed and adjustable rate commercial real estate loan pools totaling $26.1 million based on principal balances at the time of purchase.

We continue to make minor modifications on some of our lending programs to try and mitigate the impact that consumer and business deleveraging has had on our portfolio. These programs, coupled with economic improvements in our anchor markets and loan purchases, have helped to increase overall loan growth.

We originate mortgage loans secured by 1-4 family residential properties through our Residential Real Estate line of business, a majority of which are fixed-rate loans that are sold into the secondary market to third party purchasers on a best efforts delivery basis with servicing released. A majority of our adjustable rate loans are retained in our loan portfolio.

Table 4
SOURCES OF EARNING ASSET GROWTH

(Average Balances – Dollars In Thousands)	2017 to 2018 Change	Percentage Total Change	Components of Average Earning Assets 2018	2017	2016
Loans:					
Commercial, Financial, and Agricultural	$ 1,729	2.9%	8.7%	8.8%	8.5%
Real Estate – Construction	19,438	32.6	3.3	2.6	2.1
Real Estate – Commercial Mortgage	52,978	88.7	22.1	20.5	20.3
Real Estate – Residential	19,814	33.2	13.2	12.7	12.5
Real Estate – Home Equity	(11,225)	(18.8)	8.5	9.2	9.6
Consumer	17,031	28.6	11.3	10.9	10.4
Total Loans	$ 99,765	167.2%	67.1%	64.7%	63.4%
Investment Securities:					
Taxable	$ 45,330	76.0%	25.0%	23.8%	24.1%
Tax-Exempt	(30,830)	(51.7)	2.6	3.9	3.8
Total Securities	14,500	24.3	27.6	27.7	27.9
Funds Sold	(54,612)	(91.5)	5.3	7.6	8.7
Total Earning Assets	$ 59,653	100.0%	100.0%	100.0%	100.0%

Our average loan-to-deposit ratio increased to 70.9% in 2018 from 67.1% in 2017. The higher loan-to-deposit ratio reflects stronger growth in our average loan balances relative to the growth in average deposit balances.

The composition of our loan portfolio at December 31st for each of the past five years is shown in Table 5. Table 6 arrays our total loan portfolio as of December 31, 2018, by maturity period. As a percentage of the total portfolio, loans with fixed interest rates represented 38.6% as of December 31, 2018, compared to 37.2% on December 31, 2017. The higher ratio was primarily due to increases in fixed rate commercial mortgage and residential loans and, to a lesser extent, a decline in variable rate home equity lines of credit.

Table 5
LOANS BY CATEGORY

(Dollars in Thousands)	2018	2017	2016	2015	2014
Commercial, Financial and Agricultural	$ 233,689	$ 218,166	$ 216,404	$ 179,816	$ 136,925
Real Estate – Construction	89,527	77,966	59,147	47,402	43,472
Real Estate – Commercial Mortgage	602,061	535,707	503,978	499,813	510,120
Real Estate – Residential(1)	349,084	316,723	291,691	301,299	304,781
Real Estate – Home Equity	210,111	229,513	236,512	233,901	229,572

Consumer		296,622		280,234		264,443		241,676		217,192
Total Loans, Net of Unearned Income	$	1,781,094	$	1,658,309	$	1,572,175	$	1,503,907	$	1,442,062

(1) *Includes loans held for sale*

Table 6
LOAN MATURITIES

	Maturity Periods			
(Dollars in Thousands)	**One Year or Less**	**Over One Through Five Years**	**Over Five Years**	**Total**
Commercial, Financial and Agricultural	$ 56,382	$ 139,281	$ 38,026	$ 233,689
Real Estate – Construction	52,388	6,725	30,414	89,527
Real Estate – Commercial Mortgage	46,032	92,132	463,897	602,061
Real Estate – Residential	20,094	26,410	302,580	349,084
Real Estate – Home Equity	2,903	47,304	159,904	210,111
Consumer[1]	12,435	260,317	23,870	296,622
Total	$ 190,234	$ 572,169	$ 1,018,691	$ 1,781,094
Loans with Fixed Rates	$ 87,575	$ 447,213	$ 153,475	$ 688,263
Loans with Floating or Adjustable Rates	102,659	124,956	865,216	1,092,831
Total	$ 190,234	$ 572,169	$ 1,018,691	$ 1,781,094

[1]Demand loans and overdrafts are reported in the category of one year or less.

Risk Element Assets

Risk element assets consist of nonaccrual loans, OREO, troubled debt restructurings (“TDRs”), past due loans, potential problem loans, and loan concentrations. Table 7 depicts certain categories of our risk element assets as of December 31st for each of the last five years. Activity within our nonperforming asset portfolio is provided below in Table 8.

Nonperforming assets (nonaccrual loans and OREO) totaled $9.1 million at December 31, 2018 compared to $11.1 million at December 31, 2017. Nonaccrual loans totaled $6.9 million at December 31, 2018, a $0.3 million decrease from December 31, 2017. Nonaccrual loan additions totaled $12.2 million for 2018 compared to $14.1 million for 2017. The balance of OREO totaled $2.2 million at December 31, 2018, a decrease of $1.7 million December 31, 2017. For 2018, we disposed of properties totaling $2.8 million compared to $7.5 million in 2017. Nonperforming assets represented 0.31% of total assets at December 31, 2018 compared to 0.38% at December 31, 2017.

General

Table 7
RISK ELEMENT ASSETS

(Dollars in Thousands)	**2018**	**2017**	**2016**	**2015**	**2014**
Nonaccruing Loans:					
Commercial, Financial and Agricultural	$ 267	$ 629	$ 468	$ 96	$ 507
Real Estate – Construction	722	298	311	97	424
Real Estate – Commercial Mortgage	2,860	2,370	3,410	4,191	5,806
Real Estate – Residential	2,119	1,938	2,330	4,739	6,737
Real Estate – Home Equity	584	1,748	1,774	1,017	2,544
Consumer	320	176	240	165	751
Total Nonperforming Loans (“NPLs”[1])	$ 6,872	$ 7,159	$ 8,533	$ 10,305	$ 16,769
Other Real Estate Owned	2,229	3,941	10,638	19,290	35,680
Total Nonperforming Assets (“NPAs”)	$ 9,101	$ 11,100	$ 19,171	$ 29,595	$ 52,449
Past Due Loans 30 – 89 Days	$ 4,757	$ 4,543	$ 6,438	$ 5,775	$ 6,792
Past Due Loans 90 Days or More (accruing)	-	36	-	-	-
Performing Troubled Debt Restructurings	$ 22,084	$ 32,164	$ 38,233	$ 35,634	$ 44,409
Nonperforming Loans/Loans	0.39%	0.43%	0.54%	0.69%	1.16%
Nonperforming Assets/Total Assets	0.31	0.38	0.67	1.06	2.00
Nonperforming Assets/Loans Plus OREO	0.51	0.67	1.21	1.94	3.55
Allowance/Nonperforming Loans	206.79%	185.87%	157.40%	135.40%	104.60%

[1] Nonaccrual TDRs totaling $2.6 million, $2.3 million, and $1.7 million are included in NPLs for December 31, 2018,
December 31, 2017 and December 31, 2016, respectively.

Table 8
NONPERFORMING ASSET ACTIVITY

(Dollars in Thousands)	**2018**	**2017**
NPA Beginning Balance:	$ 11,100	$ 19,171
Change in Nonaccrual Loans:		
Beginning Balance	7,159	8,533
Additions	12,229	14,122
Charge-Offs	(2,649)	(2,912)
Transferred to OREO	(1,452)	(1,402)
Paid Off/Payments	(3,400)	(4,440)
Restored to Accrual	(5,015)	(6,742)
Ending Balance	6,872	7,159

Change in OREO:				
Beginning Balance		3,941		10,638
Additions[1]		2,140		2,384
Valuation Write-downs		(1,046)		(1,318)
Sales		(2,793)		(7,496)
Other		(13)		(267)
Ending Balance		2,229		3,941
NPA Net Change		(1,999)		(8,071)
NPA Ending Balance	$	9,101	$	11,100

[1] *The difference in OREO additions and nonaccrual loans transferred to OREO represents loans migrating to OREO status that were not in a nonaccrual status in prior period.*

Nonaccrual Loans. Nonaccrual loans totaled $6.9 million at December 31, 2018, a decrease of $0.3 million from December 31, 2017. Gross additions to nonaccrual status during 2018 totaled $12.2 million compared to $14.1 million in 2017.

Generally, loans are placed on nonaccrual status if principal or interest payments become 90 days past due or management deems the collectability of the principal and interest to be doubtful. Once a loan is placed in nonaccrual status, all previously accrued and uncollected interest is reversed against interest income. Interest income on nonaccrual loans is recognized when the ultimate collectability is no longer considered 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. If interest on our loans classified as nonaccrual during 2018 had been recognized on a fully accruing basis, we would have recorded an additional $0.4 million of interest income for the year ended December 31, 2018.

Other Real Estate Owned. OREO represents property acquired as the result of borrower defaults on loans or by receiving a deed in lieu of foreclosure. OREO is recorded at the lower of cost or estimated fair value, less estimated selling costs, at the time of foreclosure. Write-downs occurring at foreclosure are charged against the allowance for loan losses. On an ongoing basis, properties are either revalued internally or by a third party appraiser as required by applicable regulations. Subsequent declines in value are reflected as other noninterest expense. Carrying costs related to maintaining the OREO properties are expensed as incurred and are also reflected as other noninterest expense.

OREO totaled $2.2 million at December 31, 2018 versus $3.9 million at December 31, 2017. During 2018, we added properties totaling $2.1 million, sold properties totaling $2.8 million, and recorded valuation adjustments totaling $1.0 million. For 2017, we added properties totaling $2.4 million, sold properties totaling $7.5 million, recorded valuation adjustments totaling $1.3 million, and miscellaneous adjustments totaling $0.3 million.

The composition of our OREO portfolio as of December 31 is provided in the table below.

(Dollars in Thousands)		**2018**		**2017**
Lots/Land	$	1,030	$	2,435
Residential 1-4		655		187
Commercial Building		64		450
Other		480		869
Total OREO	$	2,229	$	3,941

Troubled Debt Restructurings. TDRs are loans on which, due to the deterioration in the borrower's financial condition, the original terms have been modified and deemed a concession to the borrower. From time to time we will modify a loan as a workout alternative. Most of these instances involve an extension of the loan term, an interest rate reduction, or a principal moratorium. A TDR classification can be removed if the borrower's financial condition

improves such that the borrower is no longer in financial difficulty, the loan has not had any forgiveness of principal or interest, and the loan is subsequently refinanced or restructured at market terms and qualifies as a new loan.

Loans classified as TDRs at December 31, 2018 totaled $24.7 million compared to $34.5 million at December 31, 2017. Accruing TDRs made up approximately $22.1 million, or 89%, of our TDR portfolio at December 31, 2018 of which $0.5 million was over 30 days past due. The weighted average rate for the loans within the accruing TDR portfolio was 5.5%. During 2018, we modified 6 loan contracts totaling approximately $0.7 million. Our TDR default rate (default balance as a percentage of average TDRs) in 2017 and 2018 was 7% and 4%, respectively.

The composition of our TDR portfolio as of December 31 is provided in the table below.

	2018		2017	
(Dollars in Thousands)	**Accruing**	**Nonaccruing[(1)]**	**Accruing**	**Nonaccruing[(1)]**
Commercial, Financial and Agricultural	$ 873	$ -	$ 822	$ -
Real Estate – Construction	59	-	64	-
Real Estate – Commercial Mortgage	9,910	1,239	17,058	1,636
Real Estate – Residential	9,234	1,222	11,666	503
Real Estate – Home Equity	1,920	179	2,441	186
Consumer	88	-	113	-
Total TDRs	$ 22,084	$ 2,640	$ 32,164	$ 2,325

[(1)] *Nonaccruing TDRs are included in NPL totals and NPA/NPL ratio calculations.*

Activity within our TDR portfolio is provided in the table below.

(Dollars in Thousands)	**2018**	**2017**
TDR Beginning Balance:	$ 34,489	$ 39,976
Additions	676	643
Charge-Offs	(555)	(529)
Paid Off/Payments	(7,327)	(5,476)
Removal Due to Change in TDR Status	(2,451)	-
Transferred to OREO	(108)	(125)
TDR Ending Balance	$ 24,724	$ 34,489

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. Past due loans at December 31, 2018 totaled $4.8 million compared to $4.6 million at December 31, 2017.

Potential Problem Loans. Potential problem loans are defined as those loans which are now current but where management has doubt as to the borrower's ability to comply with present loan repayment terms. At December 31, 2018, we had $4.0 million in loans of this type which were not included in either of the nonaccrual, TDR or 90 day past due loan categories compared to $1.9 million at December 31, 2017. Management monitors these loans closely and reviews their performance on a regular basis.

Loan Concentrations. Loan concentrations exist when there are amounts loaned to multiple borrowers engaged in similar activities which cause them to be similarly impacted by economic or other conditions and such amount exceeds 10% of total loans. Due to the lack of diversified industry within our markets and the relatively close proximity of the markets, we have both geographic concentrations as well as concentrations in the types of loans funded. Specifically, due to the nature of our markets, a significant portion of our loan portfolio has historically been secured with real estate, approximately 70% at December 31, 2018 and December 31, 2017. The primary types of real estate collateral are commercial properties and 1-4 family residential properties. At December 31, 2018, commercial

real estate and residential real estate mortgage loans (including home equity loans) accounted for 33.9% and 33.1%, respectively, of the total loan portfolio.

The following table summarizes our real estate loan portfolio as segregated by the type of property. Property type concentrations are stated as a percentage of December 31st total real estate loans.

	2018		2017	
	Investor Real Estate	**Owner Occupied Real Estate**	**Investor Real Estate**	**Owner Occupied Real Estate**
Vacant Land, Construction, and Land Development	11.0%	-	11.2%	-
Improved Property	26.0	63.0%	23.6	65.2%
Total Real Estate Loans	37.0%	63.0%	34.8%	65.2%

A major portion of our real estate loan portfolio is centered in the owner occupied category which carries a lower risk of non-collection than certain segments of the investor category. Approximately 59% of the land/construction category was secured by residential real estate at December 31, 2018.

Allowance for Loan Losses

We believe that we maintain our allowance for loan losses at a level sufficient to provide for probable credit losses inherent in the loan portfolio as of the balance sheet date. Credit losses arise from the 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. We consider all of these risks of lending when assessing the adequacy of our allowance. The allowance for loan losses is established through a provision charged to expense. Loans are charged-off against the allowance when losses are probable and reasonably quantifiable. Our allowance for loan losses is based on management's judgment of overall credit quality, which is a significant estimate based on a detailed analysis of the loan portfolio. Our allowance can and will change based on revisions to our assessment of our loan portfolio's overall credit quality and other risk factors both internal and external to us.

We evaluate the adequacy of the allowance for loan losses on a quarterly basis. The allowance consists of two components. The first component consists of amounts reserved for impaired loans. A loan is deemed impaired when, based on current information and events, it is probable that the bank will not be able to collect all amounts due (principal and interest payments), according to the contractual terms of the loan agreement. Loans are monitored for potential impairment through our ongoing loan review procedures and portfolio analysis. Classified loans and past due loans over a specific dollar amount, and all troubled debt restructurings are individually evaluated for impairment.

The approach for assigning reserves for the impaired loans is determined by the dollar amount of the loan and loan type. Impairment measurement for loans over a specific dollar are assigned on an individual loan basis with the amount reserved dependent on whether repayment of the loan is dependent on the liquidation of collateral or from some other source of repayment. If repayment is dependent on the sale of collateral, the reserve is equivalent to the recorded investment in the loan less the fair value of the collateral after estimated sales expenses. If repayment is not dependent on the sale of collateral, the reserve is equivalent to the recorded investment in the loan less the estimated cash flows discounted using the loan's effective interest rate. The discounted value of the cash flows is based on the anticipated timing of the receipt of cash payments from the borrower. The reserve allocations for individually measured impaired loans are sensitive to the extent market conditions or the actual timing of cash receipts change. Impairment reserves for smaller-balance loans under a specific dollar amount are assigned on a pooled basis utilizing loss factors for impaired loans of a similar nature.

The second component is a general reserve on all loans other than those identified as impaired. General reserves are assigned to various homogenous loan pools, including commercial, commercial real estate, construction, residential 1-4 family, home equity, and consumer. General reserves are assigned based on historical loan loss ratios determined by loan pool and internal risk ratings that are adjusted for various internal and external risk factors unique to each loan pool.

Table 9 analyzes the activity in the allowance over the past five years.

For 2018, our net loan charge-offs totaled $2.0 million, or 0.12%, of average loans, compared to $2.3 million, or 0.14%, for 2017, and $1.3 million, or 0.09%, for 2016. The slight decrease in 2018 reflected a higher level of loan loss recoveries as gross loan losses remained stable. The increase in 2017 was primarily attributable to a lower level of loan loss recoveries which fluctuate over time. At December 31, 2018, the allowance for loan losses of $14.2 million was 0.80% of outstanding loans (net of overdrafts) and provided coverage of 207% of nonperforming loans compared to 0.80% and 186%, respectively, at December 31, 2017, and 0.86% and 157%, respectively, at December 31, 2016.

Table 10 provides an allocation of the allowance for loan losses to specific loan types for each of the past five years.

The allowance for loan losses totaled $14.2 million at December 31, 2018 compared to $13.3 million at December 31, 2017 and $13.4 million at December 31, 2016. The increase in 2018 reflected a $2.6 million increase in general reserves partially offset by a $1.7 million decrease in impaired loan reserves. Growth in our loan portfolio drove the increase in general reserves and lower impaired loan balances drove the reduction in impaired loan reserves. The slight decrease in 2017 was primarily attributable to a decline in general reserves due to favorable problem loan migration and improving risk factors within our loan portfolio. We believe our allowance at December 31, 2018 was adequate to absorb probable losses inherent in our loan portfolio.

Table 9
ANALYSIS OF ALLOWANCE FOR LOAN LOSSES

(Dollars in Thousands)	**2018**	**2017**	**2016**	**2015**	**2014**
Balance at Beginning of Year	$ 13,307	$ 13,431	$ 13,953	$ 17,539	$ 23,095
Charge-Offs:					
Commercial, Financial and Agricultural	644	1,357	861	1,029	871
Real Estate – Construction	7	-	-	-	28
Real Estate – Commercial	315	685	349	1,250	3,788
Real Estate – Residential	780	411	899	1,852	2,160
Real Estate – Home Equity	533	190	450	1,403	1,379
Consumer	2,395	2,193	2,127	1,901	1,820
Total Charge-Offs	4,674	4,836	4,686	7,435	10,046
Recoveries:					
Commercial, Financial and Agricultural	459	313	337	239	214
Real Estate – Construction	26	50	-	-	9
Real Estate – Commercial	373	174	408	183	468
Real Estate – Residential	643	616	1,231	705	752
Real Estate – Home Equity	191	219	409	136	141
Consumer	964	1,125	960	992	1,001
Total Recoveries	2,656	2,497	3,345	2,255	2,585
Net Charge-Offs	2,018	2,339	1,341	5,180	7,461
Provision for Loan Losses	2,921	2,215	819	1,594	1,905
Balance at End of Year	$ 14,210	$ 13,307	$ 13,431	$ 13,953	$ 17,539
Ratio of Net Charge-Offs to Average Loans					
Outstanding	0.12%	0.14%	0.09%	0.35%	0.53%
Allowance for Loan Losses as a Percent of					
Loans at End of Year	0.80%	0.8%	0.86%	0.93%	1.22%
Allowance for Loan Losses as a Multiple of					
Net Charge-Offs	7.04x	5.69x	10.02x	2.69x	2.35x

Table 10
ALLOCATION OF ALLOWANCE FOR LOAN LOSSES

	2018		2017		2016		2015		2014	
(Dollars in Thousands)	Allow-ance Amount	Percent of Loans in Each Category To Total Loans	Allow-ance Amount	Percent of Loans in Each Category To Total Loans	Allow-ance Amount	Percent of Loans in Each Category To Total Loans	Allow-ance Amount	Percent of Loans in Each Category To Total Loans	Allow-ance Amount	Percent of Loans in Each Category To Total Loans
Commercial, Financial and Agricultural	$ 1,434	13.1%	$ 1,191	13.2%	$ 1,198	13.8%	$ 905	12.0%	$ 784	9.5%
Real Estate:										
Construction	280	5.0	122	4.7	168	3.7	101	3.1	843	3.0
Commercial	4,181	33.8	4,346	32.3	4,315	32.1	4,498	33.2	5,287	35.4
Residential	3,400	19.6	3,206	19.1	3,445	18.6	4,409	20.0	6,520	21.1
Home Equity	2,301	11.8	2,506	13.8	2,297	15.0	2,473	15.6	2,882	15.9
Consumer	2,614	16.7	1,936	16.9	2,008	16.8	1,567	16.1	1,223	15.1
Total	$ 14,210	100.0%	$ 13,307	100.0%	$ 13,431	100.0%	$ 13,953	100.0%	$ 17,539	100.0%

Investment Securities

In 2018, our average investment portfolio balance increased $14.5 million, or 2.1%, from 2017 and increased $16.3 million, or 2.4%, from 2016 to 2017. As a percentage of average earning assets, our investment portfolio represented 27.6% in 2018, compared to 27.7% in 2017. In both 2017 and 2018, we strategically grew the portfolio to better deploy our liquidity. We currently believe a relatively short duration investment portfolio offers the flexibility to provide additional liquidity from maturing bonds, if necessary.

In 2018, average taxable investments increased $45.3 million, or 7.6%, while tax-exempt investments decreased $30.8 million, or 31.5%. Non-taxable investments decreased as the tax-equivalent yield was generally unattractive throughout 2018 given the changes from the Tax Act in late 2017. We primarily purchased taxable investments as part of our overall investment strategy in 2018. High quality, short-term taxable bonds offered attractive yields during the year, resulting in favorable repricing in the investment portfolio. At December 31, 2018, municipal securities (taxable and non-taxable) comprised 7.4% of the portfolio. We may consider the purchase of municipal issues if the yields are attractive given the lower federal tax rate related to the recent changes under the Tax Act. We may also consider municipal issues that are CRA-eligible investments.

Our investment portfolio is a significant component of our operations and, as such, it functions as a key element of liquidity and asset/liability management. Two types of classifications are approved for investment securities which are Available-for-Sale ("AFS") and Held-for-Maturity ("HTM"). In 2017 and 2018, we purchased securities under both the AFS and HTM designations. At December 31, 2018, $446.2 million, or 67.2% of our investment portfolio was classified as AFS, with the remaining $217.3 million, or 32.8%, classified as HTM. At December 31, 2017, the AFS and HTM portfolio comprised 68.9% and 31.1%, respectively. Table 11 provides the composition of our investment securities portfolio.

Table 11

INVESTMENT SECURITES COMPOSITION

	2018		2017		2016	
(Dollars in Thousands)	**Carrying Amount**	**Percent**	**Carrying Amount**	**Percent**	**Carrying Amount**	**Percent**
Available for Sale						
U.S. Government Treasury	$ 261,849	39.5%	$ 235,341	33.7%	$ 286,278	40.9%
U.S. Government Agency	133,206	20.1	144,644	20.7	131,640	18.8
States and Political Subdivisions	42,365	6.4	91,157	13.1	94,839	13.5
Mortgage-Backed Securities	943	0.1	1,185	0.2	1,430	0.2
Equity Securities	7,794	1.2	8,584	1.2	8,547	1.2
Total	446,157	67.2	480,911	68.9	522,734	74.7
Held to Maturity						
U.S. Government Treasury	35,088	5.3	98,256	14.1	119,131	17.0
States and Political Subdivisions	6,512	1.0	6,996	1.0	8,175	1.2
Mortgage-Backed Securities	175,720	26.5	111,427	16.0	50,059	7.2
Total	217,320	32.8	216,679	31.1	177,365	25.3
Total Investment Securities	$ 663,477	100%	$ 697,590	100%	$ 700,099	100%

The classification of a security is determined upon acquisition based on how the purchase will affect our asset/liability strategy and future business plans and opportunities. Classification determinations will also factor in regulatory capital requirements, volatility in earnings or other comprehensive income, and liquidity needs. Securities in the AFS 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. Securities designated as HTM are those acquired or owned with the intent of holding them to maturity (final payment date). HTM investments are measured at amortized cost. It is neither management's current 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.

At December 31, 2018, there were 492 positions (combined AFS and HTM) with unrealized losses totaling $6.4 million. GNMA mortgage-backed securities, U.S. Treasuries, and SBA securities carry the full faith and credit guarantee of the U.S. Government, and are 0% risk-weighted assets. SBA securities float monthly or quarterly with

the prime rate and are uncapped. None of these positions with unrealized losses are considered impaired, and all are expected to mature at par. The table below provides a break-down of our unrealized losses by security type.

	Less Than 12 months			12 months or Longer			Total		
(Dollars in Thousands)	**Count**	**Market Value**	**Unrealized Losses**	**Count**	**Market Value**	**Unrealized Losses**	**Count**	**Market Value**	**Unrealized Losses**
GNMA	55	$ 51,337	389	136	$ 84,705	$ 2,235	191	$ 136,042	$ 2,624
UST	6	28,420	80	47	228,113	3,013	53	256,533	3,093
SBA	86	53,237	271	15	9,539	87	101	62,776	358
FHLB and FFCB	-	-	-	10	19,196	157	10	19,196	157
States and Political Subdivisions	21	8,447	12	116	37,698	158	137	46,145	170
Total	168	$ 141,441	$ 752	324	$ 379,251	$ 5,650	492	$ 520,692	$ 6,402

The average maturity of our investment portfolio at December 31, 2018 was 2.11 years compared to 1.96 years at December 31, 2017. Balances of SBA and GNMA securities increased compared to the prior year, and were partially offset by declines in U.S. Treasuries and municipal bonds. The average life of our investment portfolio increased slightly as GNMA securities purchased had longer average lives than the existing portfolio. See Table 12 for a break-down of maturities by investment type.

The weighted average taxable equivalent yield of our investment portfolio at December 31, 2018 was 2.20% versus 1.68% in 2017. This increase in yield reflected the reinvestment of proceeds from lower yielding securities into higher yielding securities during 2018 as market rates increased. Our bond portfolio contained no investments in obligations, other than U.S. Governments, of any state, municipality, political subdivision or any other issuer that exceeded 10% of our shareowners' equity at December 31, 2018.

Table 12 and Note 2 in the Notes to Consolidated Financial Statements present a detailed analysis of our investment securities as to type, maturity and yield at December 31.

Table 12
MATURITY DISTRIBUTION OF INVESTMENT SECURITIES

	Within 1 year		**1 - 5 years**		**5 - 10 years**		**After 10 years**		**Total**	
(Dollars in Thousands)	**Amount**	**WAY[(3)]**	**Amount**	**WAY[(3)]**	**Amount**	**WAY[(3)]**	**Amount**	**WAY[(3)]**	**Amount**	**WAY[(3)]**
Available for Sale										
U.S. Government Treasury	$ 62,040	1.17%	$ 199,809	1.84%	$ -	-%	$ -	-%	$ 261,849	1.68%
U.S. Government Agency	20,410	1.28	112,796	3.46	-	-	-	-	133,206	3.13
States and Political Subdivisions	35,927	1.57	6,438	1.86	-	-	-	-	42,365	1.61
Mortgage-Backed Securities[(1)]	-	-	596	4.64	347	5.46	-	-	943	4.94
Other Securities[(2)]	-	-	-	-	-	-	7,794	6.07	7,794	6.07
Total	$ 118,377	1.30%	$ 319,639	2.42%	$ 347	5.46%	$ 7,794	6.07%	$ 446,157	2.18%
Held to Maturity										
U.S. Government Treasury	$ 15,015	1.23%	$ 20,073	1.65%	$ -	-%	$ -	-%	$ 35,088	1.47%
States and Political Subdivisions	5,090	1.66	1,422	1.80	-	-	-	-	6,512	1.69
Mortgage-Backed Securities[(1)]	438	2.78	160,571	2.32	13,234	3.11	1,477	3.71	175,720	2.39
Total	$ 20,543	1.37%	$ 182,066	2.24%	$ 13,234	3.11%	$ 1,477	3.71%	$ 217,320	2.22%
Total Investment Securities	$ 138,920	1.31%	$ 501,705	2.36%	$ 13,581	3.17%	$ 9,271	5.70%	$ 663,477	2.20%

[(1)] *Based on weighted-average maturity.*

[2] Federal Home Loan Bank Stock and Federal Reserve Bank Stock are included in this category for weighted average yield, but do not have stated maturities.
[3] Weighted average yield calculated based on current amortized cost balances – not presented on a tax equivalent basis.

Deposits and Funds Purchased

Average total deposits for 2018 were $2.423 billion, an increase of $51.1 million, or 2.2%, over 2017. Average deposits increased $89.1 million, or 3.9%, from 2016 to 2017. The year-over-year increase compared to 2017 occurred in noninterest bearing and savings accounts, partially offset by the decreases in the remaining product types. Increases in 2017 compared to 2016 were experienced in all deposit types except certificates of deposit.

The seasonal inflow of public funds started in the fourth quarter of 2018 and is expected to continue into the first quarter of 2019. Deposit levels remain strong as we continue to see growth in our non-maturity deposits. Our mix of deposits continues to improve as certificates of deposit are replaced with noninterest bearing demand accounts.

We continue to closely monitor several metrics such as the sensitivity of our deposit rates, our overall liquidity position, and competitor rates when pricing deposits. This strategy is consistent with previous rate cycles, and allows us to manage the mix of our deposits rather than compete on rate. We believe this enabled us to maintain a low cost of funds of 27 basis points for 2018 and 16 basis points for 2017.

Table 2 provides an analysis of our average deposits, by category, and average rates paid thereon for each of the last three years. Table 13 reflects the shift in our deposit mix over the last year and Table 14 provides a maturity distribution of time deposits in denominations of $100,000 and over at December 31, 2018.

Average short-term borrowings, which include federal funds purchased, securities sold under agreements to repurchase, FHLB advances (maturing in less than one year), and other borrowings, increased $1.1 million, or 10.7% in 2018. The higher balance was primarily attributable to increases in repurchase agreements. See Note 8 in the Notes to Consolidated Financial Statements for further information on short-term borrowings.

We continue to focus on the value of our deposit franchise, which produces a strong base of core deposits with minimal reliance on wholesale funding.

Table 13

SOURCES OF DEPOSIT GROWTH

(Average Balances - Dollars in Thousands)		**2017 to 2018 Change**	**Percentage of Total Change**	**Components of Total Deposits 2018**	**2017**	**2016**
Noninterest Bearing Deposits	$	75,094	147.0%	37.5%	35.1%	34.4%
NOW Accounts		(24,835)	(48.6)	32.2	34.0	34.2
Money Market Accounts		(7,129)	(14.0)	10.4	10.9	11.2
Savings		27,413	53.6	14.5	13.6	12.8
Time Deposits		(19,441)	(38.0)	5.4	6.4	7.4
Total Deposits	$	51,102	100.0%	100.0%	100.0%	100.0%

Table 14
MATURITY DISTRIBUTION OF CERTIFICATES OF DEPOSIT $100,000 AND OVER

(Dollars in Thousands)		**2018 Time Certificates of Deposit**	**Percent**
Three months or less	$	8,284	27.1%
Over three through six months		8,816	28.8
Over six through twelve months		13,502	44.1
Over twelve months		-	-
Total	$	30,602	100.0%

Market Risk and Interest Rate Sensitivity

Overview. Market risk arises from changes in interest rates, exchange rates, commodity prices, and equity prices. We have risk management policies designed to monitor and limit exposure to market risk and we 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 reprice on a different basis than interest-earning assets. When interest-bearing liabilities mature or reprice 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 reprice more quickly than interest-bearing liabilities, falling market 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 what we believe to be 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.

The balance sheet is subject to testing for interest rate shock possibilities to indicate the inherent interest rate risk. We prepare a current base case and several alternative interest rate simulations (-200, -100,+100, +200, +300, and +400 basis points (bp)), at least once per quarter, and report the analysis to ALCO, our Market Risk Oversight Committee ("MROC"), our Enterprise Risk Oversight Committee ("EROC") and the Board of Directors. (The -200bp rate scenario was re-established in the third quarter 2018). We augment our interest rate shock analysis with alternative interest rate scenarios on a quarterly basis that may include ramps, parallel shifts, and a flattening or steepening of the yield curve (non-parallel shift). In addition, more frequent forecasts may be produced when interest rates are particularly uncertain or when other business conditions so dictate.

Our goal is to structure the balance sheet so that net interest earnings at risk over 12-month and 24-month periods and the economic value of equity at risk do not exceed policy guidelines at the various interest rate shock levels. We attempt 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 matched, by managing the mix of our core deposits, and by adjusting our rates to market conditions on a continuing basis. During the third and fourth quarters of 2018, instantaneous rate shocks of down 200 bp were outside of desired parameters due to limited repricing of deposits relative to the decline in rates.

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, and do not necessarily indicate the long-term prospects or economic value of the institution.

ESTIMATED CHANGES IN NET INTEREST INCOME[1]

	+400 bp	+300 bp	+200 bp	+100 bp	-100 bp	-200 bp

Percentage Change (12-month shock)						
Policy Limit	-15.0%	-12.5%	-10.0%	-7.5%	-7.5%	-10.0%
December 31, 2018	8.9%	6.6%	4.3%	2.3%	-5.0%	-12.4%
December 31, 2017	13.4%	9.9%	6.4%	3.1%	-8.5%	N/A%

Percentage Change (24-month shock)	+400 bp	+300 bp	+200 bp	+100 bp	-100 bp	-200 bp
Policy Limit	-17.5%	-15.0%	-12.5%	-10.0%	-10.0%	-12.5%
December 31, 2018	37.2%	29.1%	21.0%	13.4%	-6.4%	-20.0%
December 31, 2017	39.9%	30.4%	20.9%	11.8%	-12.0%	N/A%

The Net Interest Income (“NII”) at Risk position was less favorable for the period ending December 31, 2018 compared to December 31, 2017 for the 12-month shock for all rate scenarios except the down 100 bp scenario, where it improved. The year-over-year unfavorable changes were primarily driven by fixed rate loan growth and elevated rate sensitive deposit balances. Due to these changes, NII benefits to a lesser degree as a per cent change from the base as rates rise. . The model indicates that in the short-term, all rising rate environments will positively impact the net interest margin of the Company, while a declining rate environment of 100bp and -200bp will have a negative impact on the net interest margin. A down 200bp rate scenario was added in the third quarter of 2018.

All measures of Net Interest Income at Risk are within our prescribed policy limits over both the 12-month and 24-month periods, with the exception of rates down 200bp. We are out of compliance in the rates down 200 bp scenarios as we have a limited ability to lower our deposit rates the full 200 bp relative to the decline in market rate. In addition, this analysis incorporates an instantaneous, parallel shock and assumes we move with market rates and do not lag our deposit rates.

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 by 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	+400 bp	+300 bp	+200 bp	+100 bp	-100 bp	-200 bp
Policy Limit	-30.0%	-25.0%	-20.0%	-15.0%	-15.0%	-20.0%
December 31, 2018	24.6%	19.7%	13.9%	8.0%	-13.8%	-36.8%
December 31, 2017	31.1%	24.7%	17.5%	9.7%	-21.0%	n/a

At December 31, 2018, the economic value of equity was less favorable in all rate scenarios except the down 100 bp scenario when compared to December 31, 2017. The year-over-year unfavorable changes were primarily driven by fixed rate loan growth and elevated rate sensitive deposit balances. Due to these changes, EVE benefits to a lesser degree as a percent change from the base as rates rise. A down 200 bp rate scenario was added in the third quarter 2018. This scenario is currently out of compliance as exposure to falling rates is more extreme due to the low interest rates paid on deposits and our limited capacity to reduce those rates relative to the reduction in discount rates used to value them. At this time, we do not plan to take any immediate action to address the out-of-compliance situation in the down 200 bp scenario because we do not believe this scenario is likely to materialize over the short-run. All other rate scenarios are in compliance.

As the interest rate environment and the dynamics of the economy continue to change, additional simulations will be analyzed to address not only the changing rate environment, but also the changing balance sheet mix, measured over multiple years, to help assess the risk to the Company.

(1) Down 300, and 400 bp rate scenarios have been excluded due to the current 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 fund loan commitments, purchase securities, accommodate deposit withdrawals or repay 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. For the years ended December 31, 2018 and 2017, our principal source of funding has been our clients' deposits, supplemented by our short-term and long-term borrowings, primarily from our trust-preferred securities, 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.

At December 31, 2018, we had the ability to generate approximately $1.324 billion in additional liquidity through all of our available resources beyond our overnight funds sold position. In addition to the 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. We recognize the importance of maintaining liquidity and has developed a Contingent 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 certain credit facilities may no longer be available. We conduct quarterly liquidity stress tests and the results are reported to ALCO, MROC, EROC and the Board of Directors. We believe the liquidity available to us is sufficient to meet our ongoing needs.

We also view our investment portfolio as a liquidity source and have the option to pledge securities in our portfolio as collateral for borrowings or deposits, and/or sell selected securities. Our portfolio consists of debt issued by the U.S. Treasury, U.S. governmental agencies, and municipal governments. The weighted-average maturity of our portfolio was 2.11 years at December 31, 2018 and had a net unrealized pre-tax loss of $2.5 million in the AFS portfolio.

Our average net overnight funds sold position (defined as funds sold plus interest-bearing deposits with other banks less funds purchased) was $135.4 million during 2018 compared to an average net overnight funds sold position of $190.0 million in 2017. The decrease in this position compared to the prior year reflected higher growth in both the investment and loan portfolios, partially offset by an increase in average deposits.

We expect capital expenditures over the next 12 months to be approximately $7.0 million, which will consist primarily of technology purchases for banking offices, business applications, and information technology security needs as well as furniture and fixtures and banking office remodels. We expect that these capital expenditures will be funded with existing resources without impairing our ability to meet our ongoing obligations.

Borrowings

At December 31, 2018, total advances from the FHLB consisted of $9.9 million in outstanding debt comprised of 11 notes. In 2018, the Bank made FHLB advance payments totaling $1.6 million. Two advances matured, and no new fixed rate advances were obtained in 2018. 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. See Note 9 in the Notes to Consolidated Financial Statements for additional information on these borrowings.

On April 12, 2016, we retired $10 million in face value of trust preferred securities that were auctioned as part of a liquidation of a pooled collateralized debt obligation fund. The trust preferred securities were originally issued through CCBG Capital Trust I. Our winning bid equated to approximately 75% of the $10 million par value, with the 25% discount resulting in a pre-tax gain of approximately $2.5 million. We utilized internal resources and a $3.75 million draw on a short-term borrowing facility to fund the repurchase.

Table 15

CONTRACTUAL CASH OBLIGATIONS

Table 15 sets forth certain information about contractual cash obligations at December 31, 2018.

	Payments Due By Period				
(Dollars in Thousands)	**< 1 Yr**	**> 1 – 3 Yrs**	**> 3 – 5 Yrs**	**> 5 Yrs**	**Total**
Federal Home Loan Bank Advances	$ 4,467	$ 2,284	$ 2,852	$ 314	$ 9,917
Note Payable	296	592	592	620	2,100
Subordinated Notes Payable	-	-	-	52,887	52,887
Operating Lease Obligations	468	852	791	1,127	3,238
Time Deposit Maturities	98,960	18,608	3,175	1	120,744
Total Contractual Cash Obligations	$ 104,191	$ 22,336	$ 7,410	$ 54,949	$ 188,886

Capital

Shareowners' equity was $302.6 million at December 31, 2018, compared to $284.2 million at December 31, 2017. During 2018, shareowners' equity was positively impacted by net income of $26.2 million, stock compensation accretion of $1.4 million, net adjustments totaling $1.0 million related to transactions under our stock compensation plans, and $3.5 million decrease in the accumulated other comprehensive loss for our pension plan. Shareowners' equity was reduced by common stock dividends of $5.4 million ($0.32 per share), a net increase of $0.3 million in the unrealized loss on investment securities, and share repurchases (324,441 shares) of $8.0 million.

Shareowners' equity as of December 31, for each of the last three years is presented below:

(Dollars in Thousands)	**2018**	**2017**	**2016**
Common Stock	$ 167	$ 170	$ 168
Additional Paid-in Capital	31,058	36,674	34,188
Retained Earnings	300,177	279,410	267,037
Subtotal	331,402	316,254	301,393
Accumulated Other Comprehensive Loss, Net of Tax	(28,815)	(32,044)	(26,225)
Total Shareowners' Equity	$ 302,587	$ 284,210	$ 275,168

We continue to maintain a strong capital position. The ratio of shareowners' equity to total assets at year-end was 10.23%, 9.80%, and 9.67%, in 2018, 2017, and 2016, respectively. We believe our strong capital base offers protection during an economic downturn and provides sufficient capacity to meet our current strategic objectives.

We are subject to risk-based capital guidelines that measure capital relative to risk-weighted assets and off-balance sheet financial instruments. At December 31, 2018, we had a total risk-based capital ratio of 17.13% and a Tier 1 capital ratio of 16.36%, compared to 17.10% and 16.33%, respectively, at December 31, 2017. At December 31, 2018, our common equity tier 1 ratio was 13.58%, compared to 13.42% at December 31, 2017. Our leverage ratio at December 31, 2018, was 10.89% compared to 10.47% at December 31, 2017. For a detailed discussion of our regulatory capital requirements, refer to the "Regulatory Considerations – Capital Regulations" section on page 14. See Note 14 in the Notes to Consolidated Financial Statements for additional information as to our capital adequacy.

At December 31, 2018, our common stock had a book value of $18.00 per diluted share compared to $16.65 at December 31, 2017. Book value is impacted by the net unrealized gains and losses on investment securities. At December 31, 2018, the net unrealized loss was $2.0 million compared to a $1.7 million net unrealized loss at December 31, 2017. Book value is also impacted by the recording of our unfunded pension liability through other comprehensive income in accordance with Accounting Standards Codification Topic 715. At December 31, 2018, the net pension liability reflected in other comprehensive loss was $26.8 million compared to $30.3 million at December 31, 2017.

In February 2014, our Board of Directors authorized the repurchase of up to 1,500,000 shares of our outstanding common stock over a five-year period. Repurchases may be made in the open market or in privately negotiated transactions; however, we are not obligated to repurchase any specified number of shares. A total of 1,184,730 shares of our outstanding common stock have been repurchased at an average price of $17.37 under the plan. 324,441 shares were repurchased during 2018 at an average price of $24.75. No shares were repurchased in 2017. During 2016, 435,461 shares were repurchased at an average price $14.49 per share. In January, 2019, the 2014 plan was terminated and our Board of Directors approved a new share repurchase plan that authorizes the repurchase of up to 750,000 shares of our outstanding common stock over a five-year period. Terms of this plan are substantially similar to the 2014 plan.

Dividends

Adequate capital and financial strength is paramount to our stability and the stability of our subsidiary bank. Cash dividends declared and paid should not place unnecessary strain on our capital levels. When determining the level of dividends the following factors are considered:

- Compliance with state and federal laws and regulations;
- Our capital position and our ability to meet our financial obligations;
- Projected earnings and asset levels; and
- The ability of the Bank and us to fund dividends.

Inflation

The impact of inflation on the banking industry differs significantly from that of other industries in which a large portion of total resources are invested in fixed assets such as property, plant and equipment. Assets and liabilities of financial institutions are virtually all monetary in nature, and therefore are primarily impacted by interest rates rather than changing prices. While the general level of inflation underlies most interest rates, interest rates react more to changes in the expected rate of inflation and to changes in monetary and fiscal policy. Net interest income and the interest rate spread are good measures of our ability to react to changing interest rates and are discussed in further detail in the section entitled “Results of Operations.”

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. See Note 18 in the Notes to Consolidated Financial Statements.

At December 31, 2018, we had $468.0 million in commitments to extend credit and $5.0 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 may 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 our ability to meet on-going obligations. In the event these commitments require funding in excess of historical levels, management believes current liquidity, investment security maturities, available advances from the FHLB and Federal Reserve Bank provide a sufficient source of funds to meet these commitments.

FOURTH QUARTER, 2018 FINANCIAL RESULTS

Results of Operations

We realized net income of $8.5 million, or $0.50 per diluted share for the fourth quarter of 2018 compared to net income of $6.0 million, or $0.35 per diluted share for the third quarter of 2018. The growth in earnings reflected a $2.2 million decrease in noninterest expense, a $0.7 million increase in net interest income, and a $0.5 million reduction in the loan loss provision, partially offset by higher income tax expense of $0.8 million and lower noninterest income of $0.1 million. During the fourth quarter of 2018, we sold a banking office and realized a $2.0 million gain, which was reflected in noninterest expense (other real estate).

Tax-equivalent net interest income for the fourth quarter of 2018 was $24.5 million compared to $23.8 million for the third quarter of 2018. Our net interest margin for the fourth quarter of 2018 was 3.81% (annualized), an increase of nine basis points over the third quarter of 2018. The increase in both net interest income and the net interest margin were driven by higher interest rates and a favorable shift in the average earning asset mix reflective of loan growth.

Our provision for loan losses for the fourth quarter of 2018 was $0.5 million compared to $0.9 million for the third quarter of 2018. The reduction in our provision was primarily attributable to a decrease in impaired loan reserves. Net loan charge-offs for the fourth quarter of 2018 totaled $0.5 million compared to net loan charge-offs of $0.2 million for the third quarter of 2018.

Noninterest income for the fourth quarter of 2018 totaled $13.2 million, a decrease of $0.1 million, or 0.5%, from the third quarter of 2018 attributable to lower mortgage banking fees of $0.2 million partially offset by higher wealth management fees.

Noninterest expense for the fourth quarter of 2018 totaled $26.5 million, a decrease of $2.2 million, or 7.6%, from the third quarter of 2018. The decrease was primarily attributable to lower OREO expense of $2.0 million and other expense of $0.7 million, partially offset by higher compensation expense of $0.4 million. The lower OREO expense reflected a $2.0 million gain from the sale of a banking office in the fourth quarter of 2018. The reduction in other expense was attributable to a decline in other losses, lower professional fees and processing fees. Higher cash incentive expense drove the increase in compensation expense.

We realized income tax expense of $2.2 million for the fourth quarter of 2018 compared to income tax expense of $1.3 million for the third quarter of 2018. Income tax expense for the fourth quarter of 2018 included a $0.3 million discrete tax benefit related to a property cost segregation analysis that provided benefits from the effects of federal tax reform. Income tax expense for the third quarter of 2018 included a $0.4 million discrete tax benefit related to a pension plan contribution made during the third quarter of 2018 for the plan year 2017. Absent these discrete items, our effective tax rate was approximately 24% for each respective quarter.

Discussion of Financial Condition

Average earning assets were $2.554 billion for the fourth quarter of 2018, an increase of $19.2 million, or 0.8%, over the third quarter of 2018 attributable to a higher level of deposits. Average loans increased $38.5 million, or 2.2% compared to the third quarter of 2018 and reflected growth in all loan types except home equity loans and construction loans.

Nonperforming assets (nonaccrual loans and OREO) totaled $9.1 million at December 31, 2018, representing a decrease of $0.5 million, or 5.1%, from September 30, 2018. Nonaccrual loans totaled $6.9 million at December 31, 2018, comparable to September 30, 2018. The balance of OREO totaled $2.2 million at December 31, 2018, a decrease of $0.5 million from September 30, 2018. Nonperforming assets represented 0.31% of total assets at December 31, 2018 compared to 0.34% at September 30, 2018.

Average total deposits were $2.412 billion for the fourth quarter of 2018, an increase of $20.1 million, or 0.8%, over the third quarter of 2018 and reflected higher noninterest bearing deposit and savings accounts, partially offset by lower money market accounts and certificates of deposit balances.

ACCOUNTING POLICIES

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 a reserve established through a provision for loan losses charged to expense, which represents management's best estimate of probable losses within the existing portfolio of loans. The allowance is the amount considered adequate to absorb losses inherent in the loan portfolio based on management's evaluation of credit risk as of the balance sheet date.

Our allowance for loan losses includes allowance allocations calculated in accordance with U.S. GAAP. The level of the allowance reflects management's continuing evaluation of specific credit risks, loss experience, loan portfolio quality, economic conditions and unidentified losses inherent in the current loan portfolio, as well as trends in the foregoing. This evaluation is inherently subjective, as it requires estimates that are susceptible to significant revision as information becomes available.

The Company's allowance for loan losses consists of two components: (i) specific reserves established for probable losses on impaired loans; and (ii) general reserves for non-homogenous loans not deemed impaired and homogenous loan pools based on, but not limited to, historical loan loss experience, current economic and market conditions, levels of past due loans, and levels of problem loans.

Our financial results are affected by the changes in and the absolute level of the allowance for loan losses. This estimation process is judgmental and requires an estimate of the loss severity rates that we apply to our unimpaired loan portfolio.

Goodwill. 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 or more frequently if events or changes in circumstances indicate that the carrying value may not be recoverable. Adverse changes in the economic environment, declining operations, or other factors could result in a decline in the estimated implied fair value of goodwill. If the estimated implied fair value of goodwill is less than the carrying amount, a loss would be recognized to reduce the carrying amount to the estimated implied fair value.

We evaluate goodwill for impairment on an annual basis and in 2017 adopted ASU 2017-04, Intangibles – Goodwill and Other (Topic 350): Simplifying Accounting for Goodwill Impairment which allows for a qualitative assessment of goodwill impairment indicators. If the assessment indicates that impairment has more than likely occurred, the Company must compare the estimated fair value of the reporting unit to its carrying amount. If the carrying amount of the reporting unit exceeds its estimated fair value, an impairment charge is recorded equal to the excess.

During the fourth quarter, we performed our annual impairment testing. We proceeded with qualitative assessment by evaluating impairment indicators and concluded that a below peer return on average assets warranted movement to a fair value assessment. We estimated the fair value of the reporting unit utilizing a market approach that was supplemented with a reconciliation of the resulting equity value of the Company with our market capitalization. The market approach utilized the guideline company valuation (“GLC”) method to determine the overall equity valuation. A book and tangible book multiple was developed to determine a market value of equity on a controlling basis. The multiples that resulted from the GLC method were validated by comparing to peer companies. A control premium was then applied to the minority value to calculate a fair value indication for the Company. The control premium selected was validated by reviewing recent bank merger and acquisition transactions. Based on the outcome of the fair value assessment, the estimated fair value of our reporting unit exceeded the carrying value of goodwill and therefore, no impairment existed at December 31, 2018. For the fair value assessment, both economic conditions and observable bank purchase transactions can impact the outcome of the market valuation approach.

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, at a minimum, amounts sufficient to meet minimum funding requirements as set by law. Pension expense 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 service cost component of pension expense is reflected as “Compensation Expense” in the Consolidated Statements of Income. All other components of pension expense are reflected as “Other Expense”.

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 both current market conditions and anticipated long-term market conditions.

The discount rate is determined by matching the anticipated defined pension plan cash flows to the spot rates of a corporate Aa-rated bond index/yield curve and solving for the single equivalent discount rate which would produce the same present value. This methodology is applied consistently from year-to-year. The discount rate utilized in 2018 was 3.71%. The estimated impact to 2018 pension expense of a 25 basis point increase or decrease in the discount rate would have been a decrease and increase of approximately $812,000 and $857,000, respectively. We anticipate using a 4.43% discount rate in 2019.

Based on the balances as of the December 31, 2018 measurement date, the estimated after tax impact in accumulated other comprehensive income of a 25 basis point increase or decrease in the discount rate is a decrease or increase of approximately $4.7 million.

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 Government agency debt securities, and other securities (typically temporary liquid funds awaiting investment). The weighted-average expected long-term rate of return on plan assets utilized for 2018 was 7.25%. The estimated impact to 2018 pension expense of a 25 basis point increase or decrease in the rate of return would have been an approximate $330,000 increase or decrease, respectively. We anticipate using a rate of return on plan assets for 2019 of 7.25%.

The assumed rate of annual compensation increases of 3.25% in 2018 reflected expected trends in salaries and the employee base. We anticipate using a compensation increase of 4.00% for 2019 reflecting current market trends.

Detailed information on the pension plan, the actuarially determined disclosures, and the assumptions used are provided in Note 12 of the Notes to Consolidated Financial Statements.

Income Taxes. Income tax expense is the total of the current year income tax due or refundable and the change in deferred tax assets and liabilities. Deferred tax assets and liabilities are the expected future tax amounts for the temporary differences between carrying amounts and tax bases of assets and liabilities, computed using enacted tax rates. A valuation allowance, if needed, reduces deferred tax assets to the amount expected to be realized.

A tax position is recognized as a benefit only if it is "more likely than not" that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50% likely of being realized on examination. For tax positions not meeting the "more likely than not" test, no tax benefit is recorded.

We recognize interest and/or penalties related to income tax matters in other expenses.

Recent Accounting Pronouncements

The Financial Accounting Standards Board, the SEC, and other regulatory bodies have enacted new accounting pronouncements and standards that either have impacted our results in prior years presented, or will likely impact our results in 2018. Please refer to Note 1 of the Notes to our Consolidated Financial Statements.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

See "Financial Condition - 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.

Item 8. Financial Statements and Supplementary Data

Table 16
QUARTERLY FINANCIAL DATA (Unaudited)

	2018				**2017**			
(Dollars in Thousands, Except Per Share Data)	**Fourth**	**Third**	**Second**	**First**	**Fourth**	**Third**	**Second**	**First**
Summary of Operations:								
Interest Income	$ 26,370	$ 25,392	$ 24,419	$ 23,214	$ 22,627	$ 22,341	$ 21,422	$ 20,540
Interest Expense	2,022	1,769	1,649	1,451	1,138	1,080	926	804
Net Interest Income	24,348	23,623	22,770	21,763	21,489	21,261	20,496	19,736
Provision for Loan Losses	457	904	815	745	826	490	589	310
Net Interest Income After Provision for Loan Losses	23,891	22,719	21,955	21,018	20,663	20,771	19,907	19,426
Noninterest Income	13,238	13,308	12,542	12,477	12,897	12,996	13,135	12,718
Noninterest Expense	26,505	28,699	28,393	27,906	26,897	26,707	27,921	27,922
Income Before Income Taxes	10,624	7,328	6,104	5,589	6,663	7,060	5,121	4,222
Income Tax Expense[(2)(3)]	2,166	1,338	101	(184)	6,660	2,505	1,560	1,478
Net Income	8,458	5,990	6,003	5,773	3	4,555	3,561	2,744
Net Interest Income (Tax Equivalent)	$ 24,513	$ 23,785	$ 22,917	$ 21,943	$ 21,808	$ 21,595	$ 20,799	$ 20,006
Per Common Share:								
Basic Net Income	$ 0.50	$ 0.35	$ 0.35	$ 0.34	$ 0.00	$ 0.27	$ 0.21	$ 0.16
Diluted Net Income	0.50	0.35	0.35	0.34	0.00	0.27	0.21	0.16
Cash Dividends Declared	0.09	0.09	0.07	0.07	0.07	0.07	0.05	0.05
Diluted Book Value	18.00	17.40	17.15	16.87	16.65	16.73	16.54	16.38
Diluted Tangible Book Value[(1)]	12.96	12.45	12.20	11.91	11.68	11.76	11.55	11.38

Market Price:								
High	26.95	25.91	25.99	26.50	26.01	24.58	22.39	21.79
Low	19.92	23.19	22.28	22.80	22.21	19.60	17.68	19.22
Close	23.21	23.34	23.63	24.75	22.94	24.01	20.42	21.39
Selected Average Balances:								
Loans, Net	$ 1,785,570	$ 1,747,093	$ 1,691,287	$ 1,647,612	$ 1,640,738	$ 1,638,578	$ 1,608,629	$ 1,585,561
Earning Assets	2,554,482	2,535,292	2,566,006	2,592,465	2,511,985	2,466,287	2,502,030	2,529,207
Total Assets	2,849,245	2,826,924	2,861,104	2,892,120	2,822,451	2,779,960	2,817,479	2,845,140
Deposits	2,412,375	2,392,272	2,431,956	2,456,106	2,378,411	2,329,162	2,373,423	2,407,278
Shareowners' Equity	302,196	297,757	291,806	287,502	288,044	285,296	281,661	278,489
Common Equivalent Average Shares:								
Basic	16,989	17,056	17,045	17,028	16,967	16,965	16,955	16,919
Diluted	17,050	17,125	17,104	17,073	17,050	17,044	17,016	16,944
Performance Ratios:								
Return on Average Assets	1.18%	0.84%	0.84%	0.81%	0.00%	0.65%	0.51%	0.39
Return on Average Equity	11.10	7.98	8.25	8.14	0.00	6.33	5.07	4.00
Net Interest Margin (FTE)	3.81	3.72	3.58	3.43	3.45	3.48	3.33	3.21
Noninterest Income as % of Operating Revenue	35.22	36.04	35.52	36.44	37.51	37.94	39.05	39.19
Efficiency Ratio	70.21	77.37	80.07	81.07	77.50	77.21	82.28	85.33
Asset Quality:								
Allowance for Loan Losses	$ 14,210	$ 14,219	$ 13,563	$ 13,258	$ 13,307	$ 13,339	$ 13,242	$ 13,335
Allowance for Loan Losses to Loans	0.80%	0.80%	0.78%	0.80%	0.80%	0.82%	0.81%	0.84
Nonperforming Assets ("NPA's")	9,101	9,587	9,114	10,644	11,100	12,545	15,934	17,799
NPA's to Total Assets	0.31	0.34	0.32	0.36	0.38	0.45	0.57	0.61
NPA's to Loans plus ORE	0.51	0.54	0.52	0.64	0.67	0.76	0.97	1.11
Allowance to Non-Performing Loans	206.79	207.06	236.25	181.26	185.87	203.39	166.23	160.70
Net Charge-Offs to Average	0.10	0.06	0.12	0.20	0.21	0.10	0.17	0.10

Loans

Capital Ratios:								
Tier 1 Capital	16.36%	16.17%	16.25%	16.31%	16.33%	16.19%	15.58%	15.68
Total Capital	17.13	16.94	17.00	17.05	17.10	16.96	16.32	16.44
Common Equity Tier 1 Capital	13.58	13.43	13.46	13.44	13.42	13.26	12.72	12.77
Leverage	10.89	10.99	10.69	10.36	10.47	10.48	10.20	9.95
Tangible Common Equity[1]	7.58	7.80	7.47	7.17	7.09	7.41	7.21	6.88

[1] Diluted tangible book value and tangible common equity ratio is a non-GAAP financial measure. For additional information, including a reconciliation to GAAP, refer to page 31.
[2] For fourth quarter 2017, includes $4.1 million, or $0.24 per diluted share, income tax expense adjustment related to the Tax Cuts and Jobs Act of 2017.
[3] Includes $0.4 million, $1.4 million and $1.5 million income tax benefit in the third, second, and first quarter of 2018, respectively, for 2017 plan year pension contributions made in 2018.

CAPITAL CITY BANK GROUP, INC.

CONSOLIDATED FINANCIAL STATEMENTS

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Report of Independent Registered Public Accounting Firm

To the Shareowners and Board of Directors of Capital City Bank Group, Inc.

Opinion on the Financial Statements

We have audited the accompanying consolidated statements of financial condition of Capital City Bank Group, Inc. (the Company) as of December 31, 2018 and 2017, the related consolidated statements of income, comprehensive income, changes in shareowners' equity, and cash flows for each of the three years in the period ended December 31, 2018, and the related notes (collectively referred to as the "consolidated financial statements"). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company at December 31, 2018 and 2017, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2018, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company's internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) and our report dated March 5, 2019 expressed an unqualified opinion thereon.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates

made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Ernst & Young LLP

We have served as the Company's auditor since 2007.

Tallahassee, Florida

March 5, 2019

CAPITAL CITY BANK GROUP, INC.
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

	As of December 31,	
(Dollars in Thousands)	**2018**	**2017**
ASSETS		
Cash and Due From Banks	$ 62,032	$ 58,419
Federal Funds Sold and Interest Bearing Deposits	213,968	227,023
Total Cash and Cash Equivalents	276,000	285,442
Investment Securities, Available for Sale, at fair value	446,157	480,911
Investment Securities, Held to Maturity, at amortized cost (fair value of $214,413 and $215,007)	217,320	216,679
Total Investment Securities	663,477	697,590
Loans Held For Sale	6,869	4,817
Loans, Net of Unearned Income	1,774,225	1,653,492
Allowance for Loan Losses	(14,210)	(13,307)
Loans, Net	1,760,015	1,640,185
Premises and Equipment, Net	87,190	91,698
Goodwill	84,811	84,811
Other Real Estate Owned	2,229	3,941
Other Assets	78,592	90,310
Total Assets	$ 2,959,183	$ 2,898,794
LIABILITIES		
Deposits:		
Noninterest Bearing Deposits	$ 947,858	$ 874,583
Interest Bearing Deposits	1,583,998	1,595,294
Total Deposits	2,531,856	2,469,877
Short-Term Borrowings	13,541	7,480
Subordinated Notes Payable	52,887	52,887
Other Long-Term Borrowings	8,568	13,967
Other Liabilities	49,744	70,373
Total Liabilities	2,656,596	2,614,584
SHAREOWNERS' EQUITY		
Preferred Stock, $.01 par value; 3,000,000 shares authorized; no shares issued and outstanding	-	-
Common Stock, $.01 par value; 90,000,000 shares authorized; 16,747,571 and 16,988,951		
shares issued and outstanding at December 31, 2018 and December 31, 2017, respectively	167	170
Additional Paid-In Capital	31,058	36,674

Retained Earnings		300,177		279,410
Accumulated Other Comprehensive Loss, Net of Tax		(28,815)		(32,044)
Total Shareowners’ Equity		302,587		284,210
Total Liabilities and Shareowners’ Equity	$	2,959,183	$	2,898,794

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 Years Ended December 31,					
(Dollars in Thousands, Except Per Share Data)		**2018**		**2017**		**2016**
INTEREST INCOME						
Loans, including Fees	$	84,117	$	75,717	$	72,867
Investment Securities:						
Taxable		12,081		8,095		6,317
Tax Exempt		787		1,052		866
Funds Sold		2,410		2,066		1,104
Total Interest Income		99,395		86,930		81,154
INTEREST EXPENSE						
Deposits		4,243		1,789		879
Short-Term Borrowings		110		82		148
Subordinated Notes Payable		2,167		1,634		1,434
Other Long-Term Borrowings		371		443		728
Total Interest Expense		6,891		3,948		3,189
NET INTEREST INCOME		92,504		82,982		77,965
Provision for Loan Losses		2,921		2,215		819
Net Interest Income After Provision for Loan Losses		89,583		80,767		77,146
NONINTEREST INCOME						
Deposit Fees		20,093		20,335		21,332
Bank Card Fees		11,378		11,191		11,221
Wealth Management Fees		8,711		8,284		7,029
Mortgage Banking Fees		4,735		5,754		5,192
Other		6,648		6,182		8,907
Total Noninterest Income		51,565		51,746		53,681
NONINTEREST EXPENSE						
Compensation		63,921		62,312		62,733
Occupancy, Net		18,503		17,837		18,296
Other Real Estate Owned, Net		(442)		1,135		3,649
Other		29,521		28,163		28,536
Total Noninterest Expense		111,503		109,447		113,214
INCOME BEFORE INCOME TAXES		29,645		23,066		17,613
Income Tax Expense		3,421		12,203		5,867
NET INCOME	**$**	**26,224**	**$**	**10,863**	**$**	**11,746**
BASIC NET INCOME PER SHARE	**$**	**1.54**	**$**	**0.64**	**$**	**0.69**
DILUTED NET INCOME PER SHARE	**$**	**1.54**	**$**	**0.64**	**$**	**0.69**

Average Basic Common Shares Outstanding	17,029	16,952	16,989
Average Diluted Common Shares Outstanding	17,072	17,013	17,061

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

CAPITAL CITY BANK GROUP, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	For the Years Ended December 31,					
(Dollars in Thousands)		**2018**		**2017**		**2016**
NET INCOME	$	26,224	$	10,863	$	11,746
Other comprehensive income (loss), before tax:						
Investment Securities:						
Change in net unrealized gain/loss on securities available for sale		(409)		(1,459)		(828)
Amortization of unrealized losses on securities transferred from						
available for sale to held to maturity		55		73		82
Total Investment Securities		(354)		(1,386)		(746)
Benefit Plans:						
Reclassification adjustment for amortization of prior service cost		199		223		278
Reclassification adjustment for amortization of net loss		5,299		4,409		3,960
Current year actuarial loss		(815)		(3,470)		(9,958)
Total Benefit Plans		4,683		1,162		(5,720)
Other comprehensive income (loss), before tax:		4,329		(224)		(6,466)
Deferred tax (expense) benefit related to other comprehensive income		(1,100)		(14)		2,498
Other comprehensive income (loss), net of tax		3,229		(238)		(3,968)
TOTAL COMPREHENSIVE INCOME	$	29,453	$	10,625	$	7,778

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

CAPITAL CITY BANK GROUP, INC.
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREOWNERS' EQUITY

(Dollars in Thousands, Except Per Share Data)	**Shares Outstanding**	**Common Stock**	**Additional Paid-In Capital**	**Retained Earnings**	**Accumulated Other Comprehensive Loss, Net of Taxes**	**Total**
Balance, January 1, 2016	17,156,919	$ 172	$ 38,256	$ 258,181	$ (22,257)	$ 274,352
Net Income		-	-	11,746	-	11,746
Other Comprehensive Loss, Net of Tax		-	-	-	(3,968)	(3,968)
Cash Dividends ($0.17 per share)		-	-	(2,890)	-	(2,890)
Stock Compensation Expense		-	1,260	-	-	1,260
Impact of Transactions Under Compensation Plans, net	123,240	-	980	-	-	980
Repurchase of Common Stock	(435,461)	(4)	(6,308)	-	-	(6,312)
Balance, December 31, 2016	16,844,698	168	34,188	267,037	(26,225)	275,168
Net Income	-	-	-	10,863	-	10,863
Other Comprehensive Loss, Net of Tax	-	-	-	-	(238)	(238)
Cash Dividends ($0.24 per share)	-	-	-	(4,071)	-	(4,071)
Stock Compensation Expense	-	-	1,502	-	-	1,502
Impact of Transactions Under Compensation Plans, net	144,253	2	984	-	-	986
Reclassification per Adoption of ASU No. 2018-02	-	-	-	5,581	(5,581)	-
Balance, December 31, 2017	16,988,951	170	36,674	279,410	(32,044)	284,210
Net Income	-	-	-	26,224	-	26,224
Other Comprehensive Loss, Net of Tax	-	-	-	-	3,229	3,229
Cash Dividends ($0.32 per share)	-	-	-	(5,457)	-	(5,457)
Stock Compensation Expense	-	-	1,421	-	-	1,421

Impact of Transactions Under Compensation Plans, net	83,061	-	990	-	-	990
Repurchase of Common Stock	(324,441)	(3)	(8,027)	-	-	(8,030)
Balance, December 31, 2018	16,747,571	$ 167	$ 31,058	$ 300,177	$ (28,815)	$ 302,587

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 Years Ended December 31,		
(Dollars in Thousands)	**2018**	**2017**	**2016**
CASH FLOWS FROM OPERATING ACTIVITIES			
Net Income	$ 26,224	$ 10,863	$ 11,746
Adjustments to Reconcile Net Income to Cash Provided by Operating Activities:			
Provision for Loan Losses	2,921	2,215	819
Depreciation	6,453	6,558	6,975
Amortization of Premiums, Discounts, and Fees, net	6,698	6,626	6,219
Gain on Retirement of Trust Preferred Securities	-	-	(2,487)
Originations of Loans Held-for-Sale	(177,742)	(191,978)	(177,022)
Proceeds From Sales of Loans Held-for-Sale	180,425	192,915	171,328
Net Gain From Sales of Loans Held-for-Sale	(4,735)	(5,754)	(5,192)
Stock Compensation	1,421	1,502	1,260
Net Tax Benefit from Stock Compensation	(41)	(223)	-
Deferred Income Taxes	4,837	7,576	3,457
Net (Gain) Loss on Sales and Write-Downs of Other Real Estate Owned	(935)	783	3,225
Impairment Loss on Premises (Hurricane Damage)	(1,213)	-	-
Loss on Disposal of Premises and Equipment	87	276	131
Net Decrease (Increase) in Other Assets	7,168	2,063	(18,374)
Net (Decrease) Increase in Other Liabilities	(16,942)	(5,531)	8,904
Net Cash Provided By Operating Activities	34,626	38,777	22,621
CASH FLOWS FROM INVESTING ACTIVITIES			
Securities Held to Maturity:			
Purchases	(102,428)	(98,861)	(50,001)
Payments, Maturities, and Calls	100,131	58,449	59,460
Securities Available for Sale:			
Purchases	(132,895)	(163,469)	(192,005)
Payments, Maturities, and Calls	161,332	198,027	114,189
Purchase of Loans Held for Investment	(26,070)	(44,083)	-
Net Increase in Loans	(98,068)	(51,625)	(73,997)
Proceeds From Insurance Claims on Premises	663	-	-
Proceeds From Sales of Other Real Estate Owned	4,774	8,031	9,443
Purchases of Premises and Equipment, net	(1,458)	(3,997)	(4,450)
Net Cash Used In Investing Activities	(94,019)	(97,528)	(137,361)
CASH FLOWS FROM FINANCING ACTIVITIES			
Net Increase in Deposits	61,979	57,591	109,437
Net Increase (Decrease) in Short-Term Borrowings	2,551	(2,489)	(52,666)
Redemption of Subordinated Notes	-	-	(7,500)
Repayment of Other Long-Term Borrowings	(1,889)	(3,694)	(9,027)
Dividends Paid	(5,457)	(4,071)	(2,890)
Payments to Repurchase Common Stock	(8,030)	-	(6,312)
Issuance of Common Stock Under Compensation Plans	797	809	840
Net Cash Provided By Financing Activities	49,951	48,146	31,882

NET DECREASE IN CASH AND CASH EQUIVALENTS		**(9,442)**		**(10,605)**		**(82,858)**
Cash and Cash Equivalents at Beginning of Year		285,442		296,047		378,905
Cash and Cash Equivalents at End of Year	$	276,000	$	285,442	$	296,047
Supplemental Cash Flow Disclosures:						
Interest Paid	$	6,879	$	3,952	$	3,195
Income Taxes Paid (Refunded)	$	157	$	6,514	$	(330)
Noncash Investing and Financing Activities:						
Loans and Premises Transferred to Other Real Estate Owned	$	2,140	$	2,384	$	4,016

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

Notes to Consolidated Financial Statements

Note 1

SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

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.

Basis of Presentation

The consolidated financial statements include the accounts of Capital City Bank Group, Inc. (“CCBG”), and its wholly owned subsidiary, Capital City Bank (“CCB” or the “Bank” and together with CCBG, the “Company”). All material inter-company transactions and accounts have been eliminated in consolidation.

The Company, which operates a single reportable business segment that is comprised of commercial banking within the states of Florida, Georgia, and Alabama, follows accounting principles generally accepted in the United States of America and reporting practices applicable to the banking industry. The principles which materially affect the financial position, results of operations and cash flows are summarized below.

The Company determines whether it has a controlling financial interest in an entity by first evaluating whether the entity is a voting interest entity or a variable interest entity under accounting principles generally accepted in the United States of America. Voting interest entities are entities in which the total equity investment at risk is sufficient to enable the entity to finance itself independently and provide the equity holders with the obligation to absorb losses, the right to receive residual returns and the right to make decisions about the entity’s activities. The Company consolidates voting interest entities in which it has all, or at least a majority of, the voting interest. As defined in applicable accounting standards, variable interest entities (“VIE’s”) are entities that lack one or more of the characteristics of a voting interest entity. A controlling financial interest in an entity is present when an enterprise has a variable interest, or a combination of variable interests, that will absorb a majority of the entity’s expected losses, receive a majority of the entity’s expected residual returns, or both. The enterprise with a controlling financial interest, known as the primary beneficiary, consolidates the VIE. CCBG's wholly owned subsidiaries, CCBG Capital Trust I

(established November 1, 2004) and CCBG Capital Trust II (established May 24, 2005) are VIEs for which the Company is not the primary beneficiary. Accordingly, the accounts of these entities are not included in the Company's consolidated financial statements.

Certain previously reported amounts have been reclassified to conform to the current year's presentation. The Company has evaluated subsequent events for potential recognition and/or disclosure through the date the consolidated financial statements included in this Annual Report on Form 10-K were filed with the United States Securities and Exchange Commission.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could vary from these estimates. Material estimates that are particularly susceptible to significant changes in the near-term relate to the determination of the allowance for loan losses, pension expense, income taxes, loss contingencies, valuation of other real estate owned, and valuation of goodwill and their respective analysis of impairment.

Cash and Cash Equivalents

Cash and cash equivalents include cash and due from banks, interest-bearing deposits in other banks, and federal funds sold. Generally, federal funds are purchased and sold for one-day periods and all other cash equivalents have a maturity of 90 days or less. The Company is required to maintain average reserve balances with the Federal Reserve Bank based upon a percentage of deposits. The average amounts of these required reserve balances for the years ended December 31, 2018 and 2017 were $23.3 million and $18.8 million, respectively.

Investment Securities

Securities are classified as held to maturity and carried at amortized cost when the Company has the positive intent and ability to hold them until maturity. Securities not classified as held to maturity or trading securities are classified as available for sale and carried at fair value, with the unrealized holding gains and losses reported as a component of other comprehensive income, net of tax. The Company determines the appropriate classification of securities at the time of purchase. Securities with limited marketability, such as stock in the Federal Reserve Bank and the Federal Home Loan Bank, are carried at cost. Securities transferred from available for sale to held to maturity are recorded at fair value at the time of transfer. The respective gain or loss is reclassified as a separate component of other comprehensive income and amortized as an adjustment to interest income over the remaining life of the security.

Interest income includes amortization of purchase premiums and discounts. Realized gains and losses are derived from the amortized cost of the security sold. Declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, the Company considers, (i) whether it has decided to sell the security, (ii) whether it is more likely than not that the Company will be required to sell the security before its market value recovers, and (iii) whether the present value of expected cash flows is sufficient to recover the entire amortized cost basis. When assessing the security's expected cash flows, the Company considers, among other things, (i) the length of time and the extent to which the fair value has been less than cost and (ii) the financial condition and near-term prospects of the issuer.

Loans Held For Sale

Certain residential mortgage loans are originated for sale in the secondary mortgage loan market. Additionally, certain other loans are periodically identified to be sold. The Company has the ability and intent to sell these loans and they are classified as loans held for sale and carried at the lower of cost or fair value. Fair value is determined on the basis of rates quoted in the respective secondary market for the type of loan held for sale. Loans are generally sold with servicing released at a premium or discount from the carrying amount of the loans. Such premium or discount is recognized as mortgage banking revenue at the date of sale. Fixed commitments are generally used at the time loans are originated or identified for sale to mitigate interest rate risk. The fair value of fixed commitments to originate and sell loans held for sale is not material.

Loans

Loans are stated at the principal amount outstanding, net of unearned income. Interest income is accrued on the effective yield method based on outstanding balances, and includes loan late fees. Fees charged to originate loans and direct loan origination costs are deferred and amortized over the life of the loan as a yield adjustment.

The Company defines loans as past due when one full payment is past due or a contractual maturity is over 30 days late. The accrual of interest is generally suspended on loans more than 90 days past due with respect to principal or interest. When a loan is placed on nonaccrual status, all previously accrued and uncollected interest is reversed against current income. Interest income on nonaccrual loans is recognized when the ultimate collectability is no longer considered 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.

Loan charge-offs on commercial and investor real estate loans are recorded when the facts and circumstances of the individual loan confirm the loan is not fully collectible and the loss is reasonably quantifiable. Factors considered in making these determinations are the borrower's and any guarantor's ability and willingness to pay, the status of the account in bankruptcy court (if applicable), and collateral value. Charge-off decisions for consumer loans are dictated by the Federal Financial Institutions Examination Council's (FFIEC) Uniform Retail Credit Classification and Account Management Policy which establishes standards for the classification and treatment of consumer loans, which generally require charge-off after 120 days of delinquency.

Allowance for Loan Losses

The allowance for loan losses is a reserve established through a provision for loan losses charged to expense, which represents management's best estimate of probable losses within the existing portfolio of loans. The allowance is that amount considered adequate to absorb losses inherent in the loan portfolio based on management's evaluation of credit risk as of the balance sheet date.

The allowance for loan losses includes allowance allocations calculated in accordance with FASB ASC Topic 310 – Receivables and ASC Topic 450 - Contingencies. The level of the allowance reflects management's continuing evaluation of specific credit risks, loan loss experience, current loan portfolio quality, present economic conditions and unidentified losses inherent in the current loan portfolio, as well as trends in the foregoing. This evaluation is inherently subjective, as it requires estimates that are susceptible to significant revision as more information becomes available.

The Company's allowance for loan losses consists of two components: (i) specific reserves established for probable losses on impaired loans; and (ii) general reserve for non-homogenous loans not deemed impaired and homogenous loan pools based on, but not limited to, historical loan loss experience, current economic conditions, levels of past due loans, and levels of problem 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 to borrowers who are experiencing financial difficulties and whose loans were modified with concessions are classified as troubled debt restructurings and measured for impairment. Loans to borrowers that have filed Chapter 7 bankruptcy, but continue to perform as agreed are classified as troubled debt restructurings and measured for impairment.

Long-Lived Assets

Premises and equipment is stated at cost less accumulated depreciation, computed on the straight-line method over the estimated useful lives for each type of asset with premises being depreciated over a range of 10 to 40 years, and equipment being depreciated over a range of 3 to 10 years. Additions, renovations and leasehold improvements to premises are capitalized and depreciated over the lesser of the useful life or the remaining lease term. Repairs and maintenance are charged to noninterest expense as incurred.

Long-lived assets are evaluated for impairment if circumstances suggest that their carrying value may not be recoverable, by comparing the carrying value to estimated undiscounted cash flows. If the asset is deemed impaired, an impairment charge is recorded equal to the carrying value less the fair value.

Bank Owned Life Insurance (BOLI)

The Company, through its subsidiary bank, has purchased life insurance policies on certain key officers. Bank owned life insurance is recorded at the amount that can be realized under the insurance contract at the balance sheet date,

which is the cash surrender value adjusted for other charges or other amounts due that are probable at settlement.

Goodwill

Goodwill represents the excess of the cost of businesses acquired over the fair value of the net assets acquired. In accordance with FASB ASC Topic 350, the Company determined it has one goodwill reporting unit. Goodwill is tested for impairment annually during the fourth quarter or on an interim basis if an event occurs or circumstances change that would more likely than not reduce the fair value of the reporting unit below its carrying value. See Note 5 – Goodwill for additional information.

Other Real Estate Owned

Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at the lower of cost or fair value less estimated selling costs, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell. The valuation of foreclosed assets is subjective in nature and may be adjusted in the future because of changes in economic conditions. Revenue and expenses from operations and changes in value are included in noninterest expense.

Loss Contingencies

Loss contingencies, including claims and legal actions arising in the ordinary course of business are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated.

Income Taxes

Income tax expense is the total of the current year income tax due or refundable and the change in deferred tax assets and liabilities (excluding deferred tax assets and liabilities related to business combinations or components of other comprehensive income). Deferred tax assets and liabilities are the expected future tax amounts for the temporary differences between carrying amounts and tax bases of assets and liabilities, computed using enacted tax rates. A valuation allowance, if needed, reduces deferred tax assets to the expected amount most likely to be realized. Realization of deferred tax assets is dependent upon the generation of a sufficient level of future taxable income and recoverable taxes paid in prior years. The income tax effects related to settlements of share-based payment awards are reported in earnings as an increase or decrease in income tax expense. Prior to 2017, income tax benefits at settlement of an award were reported as an increase or decrease to additional paid-in capital to the extent that those benefits were greater than (or less than) the income tax benefits recognized in earnings during the award’s vesting period.

On December 22, 2017, H.R.1, commonly known as the Tax Cuts and Jobs Act (the “Tax Act”), was signed into law. Among other things, the Tax Act reduced the Company's corporate federal tax rate from 35% to 21% effective January 1, 2018. As a result, the Company was required to re-measure as of December 31, 2017, through income tax expense, its deferred tax assets and liabilities using the enacted rate at which they are expected to be recovered or settled. Further discussion is provided in Note 10 – Income Taxes.

The Company files a consolidated federal income tax return and each subsidiary files a separate state income tax return.

Earnings Per Common Share

Basic earnings per common share is based on net income divided by the weighted-average number of common shares outstanding during the period excluding non-vested stock. Diluted earnings per common share include the dilutive effect of stock options and non-vested stock awards granted using the treasury stock method. A reconciliation of the weighted-average shares used in calculating basic earnings per common share and the weighted average common shares used in calculating diluted earnings per common share for the reported periods is provided in Note 13 — Earnings Per Share.

Comprehensive Income

Comprehensive income includes all changes in shareowners’ equity during a period, except those resulting from transactions with shareowners. Besides net income, other components of the Company’s comprehensive income

include the after tax effect of changes in the net unrealized gain/loss on securities available for sale and changes in the funded status of defined benefit and supplemental executive retirement plans. Comprehensive income is reported in the accompanying Consolidated Statements of Comprehensive Income and Changes in Shareowners' Equity.

In 2017, the Company adopted FASB ASU 2018-02, *Income Statement – Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income* and reclassified to retained earnings the stranded effects in accumulated other comprehensive income related to the Tax Act.

Stock Based Compensation

Compensation cost is recognized for share-based awards issued to employees, based on the fair value of these awards at the date of grant. Compensation cost is recognized over the requisite service period, generally defined as the vesting period. The market price of the Company's common stock at the date of the grant is used for restricted stock awards. For stock purchase plan awards, a Black-Scholes model is utilized to estimate the fair value of the award. The impact of forfeitures of share-based awards on compensation expense is recognized as forfeitures occur.

Revenue Recognition

Accounting Standards Codification ("ASC") 606, Revenue from Contracts with Customers ("ASC 606"), establishes principles for reporting information about the nature, amount, timing and uncertainty of revenue and cash flows arising from the entity's contracts to provide goods or services to customers. The core principle requires an entity to recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration that it expects to be entitled to receive in exchange for those goods or services recognized as performance obligations are satisfied.

The majority of the Company's revenue-generating transactions are not subject to ASC 606, including revenue generated from financial instruments, such as our loans, letters of credit, and investment securities, and revenue related to the sale of residential mortgages in the secondary market, as these activities are subject to other GAAP discussed elsewhere within our disclosures. The Company recognizes revenue from these activities as it is earned based on contractual terms, as transactions occur, or as services are provided and collectability is reasonably assured. Descriptions of the major revenue-generating activities that are within the scope of ASC 606, which are presented in the accompanying statements of income as components of non-interest income are as follows:

Deposit Fees - these represent general service fees for monthly account maintenance and activity- or transaction-based fees and consist of transaction-based revenue, time-based revenue (service period), item-based revenue or some other individual attribute-based revenue. Revenue is recognized when the Company's performance obligation is completed which is generally monthly for account maintenance services or when a transaction has been completed. Payment for such performance obligations are generally received at the time the performance obligations are satisfied.

Wealth Management - trust fees and retail brokerage fees – trust fees represent monthly fees due from wealth management clients as consideration for managing the client's assets. Trust services include custody of assets, investment management, fees for trust services and similar fiduciary activities. Revenue is recognized when the Company's performance obligation is completed each month or quarter, which is the time that payment is received. Also, retail brokerage fees are received from a third party broker-dealer, for which the Company acts as an agent, as part of a revenue-sharing agreement for fees earned from customers that are referred to the third party. These fees are for transactional and advisory services and are paid by the third party on a monthly basis and recognized ratably throughout the quarter as the Company's performance obligation is satisfied.

Bank Card Fees – bank card related fees primarily includes interchange income from client use of consumer and business debit cards. Interchange income is a fee paid by a merchant bank to the card-issuing bank through the interchange network. Interchange fees are set by the credit card associations and are based on cardholder purchase volumes. The Company records interchange income as transactions occur.

Gains and Losses from the Sale of Bank Owned Property – the performance obligation in the sale of other real estate owned typically will be the delivery of control over the property to the buyer. If the Company is not providing the financing of the sale, the transaction price is typically identified in the purchase and sale agreement. However, if the Company provides seller financing, the Company must determine a transaction price, depending on if the sale contract is at market terms and taking into account the credit risk inherent in the arrangement.

Other non-interest income primarily includes items such as mortgage banking fees (gains from the sale of residential mortgage loans held for sale), bank-owned life insurance, and safe deposit box fees none of which are subject to the requirements of ASC 606.

The Company has made no significant judgments in applying the revenue guidance prescribed in ASC 606 that affects the determination of the amount and timing of revenue from the above-described contracts with clients.

The Company has applied ASC 606 using the modified retrospective approach effective on January 1, 2018 to all existing contracts with clients covered under the scope of the standard. The Company did not have an aggregate effect of modification resulting from adoption of ASC 606, and no financial statement line items were affected by this change in accounting standard.

Accounting Changes and Reclassifications

Equity Securities

Beginning January 1, 2018, upon adoption of ASU 2016-01, equity securities with readily determinable fair values are stated at fair value with realized and unrealized gains and losses reported in income. For periods prior to January 1, 2018, equity securities were classified as available-for-sale and stated at fair value with unrealized gains and losses reported as a separate component of AOCI, net of tax. Equity securities without readily determinable fair values are recorded at cost less any impairment, if any. Upon adoption, the Company reclassified one security in the amount of $0.8 million to other assets in accordance with this accounting standard.

Employee Benefit Plans

Beginning January 1, 2018, upon adoption of ASU 2017-07, an employer must report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. The other components of net benefit cost are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations, if one is presented. If a separate line item or items are used to present the other components of net benefit cost, that line item or items must be appropriately described. If a separate line item or items are not used, the line item or items used in the income statement to present the other components of net benefit cost must be disclosed. In accordance with this accounting standard, the Company reclassified the non-service cost components of its net periodic benefit cost to other noninterest expense in the accompanying statements of income (See Note 12 – Employee Benefit Plans). Prior year amounts were retrospectively adjusted in accordance with the accounting standard. The effects on the statements of income were as follows:

Period Presented	Line Item	
(Dollars in Thousands)	Compensation	Other Expense
Year Ended December 31, 2018	($1,828)	$1,828
Year Ended December 31, 2017	($2,565)	$2,565
Year Ended December 31, 2016	($2,251)	$2,251

NEW AUTHORITATIVE ACCOUNTING GUIDANCE – NOT YET ADOPTED

ASU 2016-02, "Leases (Topic 842)." ASU 2016-02 requires that lessees and lessors recognize assets and liabilities on the balance sheet and disclose key information about leasing arrangements. ASU 2016-02 was effective for the Company on January 1, 2019. ASU 2016-02 provides for a modified retrospective transition approach requiring lessees to recognize leases on the balance sheet at the beginning of either the earliest period presented or as of the beginning of the period of adoption with the option to elect certain practical expedients. The Company will elect to apply ASU 2016-02 as of the beginning of the period of adoption (January 1, 2019) and will not restate comparative periods. The Company is also expected to elect certain practical expedients provided under ASU 2016-02 and will not reassess: (i) whether any expired or existing contracts are or contain leases, (ii) the lease classification for any expired or existing leases, and (iii) initial and direct costs of any existing leases. The Company does not expect to apply the recognition requirements of ASU 2016-02 to any short-term leases (as defined by the accounting guidance). The Company has completed the evaluation of lease obligations as defined by ASU 2016-02 and due to the small number of lease agreements, the effect of adopting ASU 2016-02 was not significant, an approximate $2 million increase in assets and liabilities with no material impact to the statement of income compared to the current lease accounting model.

ASU 2016-13, "Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Statements." ASU 2016-13 requires the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts and

requires enhanced disclosures related to the significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of an organization's portfolio. In addition, ASU 2016-13 amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. ASU 2016-13 will be effective for the Company on January 1, 2020. The Company is currently evaluating the potential impact of ASU 2016-13 on its financial statements and related disclosures. As part of its implementation efforts to date, management has formed a cross-functional implementation team and developed a project plan. The Company has also engaged a vendor to assist in model development. The data set-up process is near completion and the overall project plan remains on schedule. In conjunction with the implementation, the Company is reviewing business process and evaluating potential changes to the control environment. The Company expects the new guidance will result in an increase in the allowance for credit losses given the change from accounting for losses inherent in the loan portfolio to accounting for losses over the remaining expected life of the portfolio. However, since the magnitude of the anticipated increase in the allowance for credit losses will be impacted by economic conditions and trends in the Company's portfolio at the time of adoption, the quantitative impact cannot yet be reasonably estimated.

ASU 2017-12, "Derivatives and Hedging (Topic 815) - Targeted Improvements to Accounting for Hedging Activities." ASU 2017-12 amends the hedge accounting recognition and presentation requirements in ASC 815 to improve the transparency and understandability of information conveyed to financial statement users about an entity's risk management activities to better align the entity's financial reporting for hedging relationships with those risk management activities and to reduce the complexity of and simplify the application of hedge accounting.
ASU 2017-12 is effective for Company on January 1, 2019 and is not expected to have a significant impact on its financial statements.

ASU 2018-03, "Technical Corrections and Improvements to Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. ASU 2018-03 clarifies certain aspects of the guidance issued in ASU 2016-01. This includes the ability to irrevocably elect to change the measurement approach for equity securities measured using the practical expedient (at cost plus or minus observable transactions less impairment) to a fair value method in accordance with Topic 820, Fair Value Measurement; clarification that if an observable transaction occurs for such securities, the adjustment is as of the observable transaction date; clarification that the prospective transition approach for equity securities without a readily determinable fair values is meant only for instances in which the practical expedient is elected; and various other clarifications. ASU 2018-03 was effective for the Company on July 1, 2018 and did not have a significant impact on its financial statements.

ASU 2018-13, "Fair Value Measurement (Topic 820): Disclosure Framework – Changes to the Disclosure Requirements for Fair Value Measurement. ASU 2018-13 removes the requirement to disclose the amount of and reasons for transfers between Level 1 and Level 2 fair value measurements, the policy for timing of transfers between levels and the valuation processes for Level 3 fair value measurements. It also adds a requirement to disclose the changes in unrealized gains and losses for the period included in other comprehensive income for recurring Level 3 fair value held at the end of the reporting period. For certain unobservable inputs, an entity may disclose other quantitative information (such as the median or arithmetic average) in lieu of the weighted average if the entity determines that other quantitative information would be a more reasonable and rational method to reflect the distribution of unobservable inputs used to develop Level 3 fair value measurements. ASU 2018-13 is effective for the Company January 1, 2020 and is not expected to have a significant impact on its financial statements.

ASU 2018-14, "Compensation – Retirement Benefits – Defined Benefit Plans – General (Subtopic 715-20: Disclosure Framework – Changes to the Disclosure Requirements for Defined Benefit Plans. ASU 2018-14 removes the disclosure requirements to include amounts in accumulated other comprehensive income expected to be recognized as components of net periodic benefit cost over the next fiscal year and the amount and timing of plan assets expected to be returned to the employer. It also adds the requirement to disclose the weighted-average interest crediting rates for cash balance plans and other plans with promised interest crediting rates and an explanation of the reasons for significant gains and losses related to changes in the benefit obligation for the period. ASU 2018-14 is effective for the company January 1, 2021. The Company is currently evaluating the potential impact of ASU 2018-15 on its financial statements and related disclosures.

ASU 2018-15, "Intangibles – Goodwill and Other – Internal – Use Software (Subtopic 350-40): Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract. ASU 2018-15 aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal-use software license). ASU 2018-15 is effective for the company January 1, 2020. The Company is currently evaluating the potential impact of ASU 2018-15 on its financial statements and related disclosures.

Note 2
INVESTMENT SECURITIES

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

	2018				2017			
(Dollars in Thousands)	**Amortized Cost**	**Unrealized Gains**	**Unrealized Losses**	**Market Value**	**Amortized Cost**	**Unrealized Gain**	**Unrealized Losses**	**Market Value**
Available for Sale								
U.S. Government Treasury	$264,298	$ 167	$ 2,616	$261,849	$237,505	$ -	$ 2,164	$235,341
U.S. Government Agency	133,201	520	515	133,206	144,324	727	407	144,644
States and Political Subdivisions	42,509	-	144	42,365	91,533	2	378	91,157
Mortgage-Backed Securities	903	40	-	943	1,102	83	-	1,185
Equity Securities(1)	7,794	-	-	7,794	8,584	-	-	8,584
Total	$448,705	$ 727	$ 3,275	$446,157	$483,048	$ 812	$ 2,949	$480,911
Held to Maturity								
U.S. Government Treasury	$ 35,088	$ -	$ 477	$ 34,611	$ 98,256	$ -	$ 441	$ 97,815
States and Political Subdivisions	6,512	-	26	6,486	6,996	-	41	6,955
Mortgage-Backed Securities	175,720	220	2,624	173,316	111,427	22	1,212	110,237
Total	$217,320	$ 220	$ 3,127	$214,413	$216,679	$ 22	$ 1,694	$215,007
Total Investment Securities	$666,025	$ 947	$ 6,402	$660,570	$699,727	$ 834	$ 4,643	$695,918

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(1) *Includes Federal Home Loan Bank and Federal Reserve Bank recorded at cost of $3.0 million and $4.8 million, respectively, at December 31, 2018 and Federal Home Loan Bank, Federal Reserve Bank and FNBB, Inc. stock at $3.1 million, $4.8 million and $0.8 million , respectively, at December 31, 2017. The FNBB Inc. equity investment was reclassified to other assets in accordance with ASU 2016-01, which was adopted prospectively as allowed by the standard.*

Securities with an amortized cost of $319.6 million and $328.1 million at December 31, 2018 and December 31, 2017, respectively, were pledged to secure public deposits and for other purposes.

The Bank, as a member of the Federal Home Loan Bank of Atlanta (“FHLB”), is required to own capital stock in the FHLB based generally upon the balances of residential and commercial real estate loans, and FHLB advances. FHLB stock 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.

As a member of the Federal Reserve Bank of Atlanta, the Bank is required to maintain stock in the Federal Reserve Bank of Atlanta based on a specified ratio relative to the Bank’s capital. Federal Reserve Bank stock is carried at cost and may be sold back to the Federal Reserve Bank at its carrying value.

Investment Sales. There were no sales of investment securities for each of the last three years.

Maturity Distribution. At December 31, 2018, the Company's investment securities had the following maturity distribution based on contractual maturity. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations. Mortgage-backed securities and certain amortizing U.S. government agency securities are shown separately since they are not due at a certain maturity date.

	Available for Sale		**Held to Maturity**	
(Dollars in Thousands)	**Amortized Cost**	**Market Value**	**Amortized Cost**	**Market Value**
Due in one year or less	$ 117,923	$ 117,163	$ 20,104	$ 19,924
Due after one through five years	208,237	206,247	21,496	21,173
Mortgage-Backed Securities	903	943	175,720	173,316
U.S. Government Agency	113,848	114,010	-	-
Equity Securities	7,794	7,794	-	-
Total	$ 448,705	$ 446,157	$ 217,320	$ 214,413

Unrealized Losses. The following table summarizes the investment securities with unrealized losses at December 31, aggregated by major security type and length of time in a continuous unrealized loss position:

	Less Than 12 Months		Greater Than 12 Months		Total	
(Dollars in Thousands)	Market Value	Unrealized Losses	Market Value	Unrealized Losses	Market Value	Unrealized Losses
December 31, 2018						
Available for Sale						
U.S. Government Treasury	$ 28,420	$ 80	$ 193,501	$ 2,536	$ 221,921	$ 2,616
U.S. Government Agency	53,237	271	28,735	244	81,972	515
States and Political Subdivisions	8,243	12	31,417	132	39,660	144
Mortgage-Backed Securities	10	-	-	-	10	-
Total	89,910	363	253,653	2,912	343,563	3,275
Held to Maturity						
U.S. Government Treasury	-	-	34,612	477	34,612	477
States and Political Subdivisions	204	-	6,281	26	6,485	26
Mortgage-Backed Securities	51,327	389	84,705	2,235	136,032	2,624
Total	$ 51,531	$ 389	$ 125,598	$ 2,738	$ 177,129	$ 3,127
December 31, 2017						
Available for Sale						
U.S. Government Treasury	$ 155,443	$ 963	$ 79,900	$ 1,201	$ 235,343	$ 2,164
U.S. Government Agency	45,737	150	25,757	257	71,494	407
States and Political Subdivisions	82,999	320	5,549	58	88,548	378
Mortgage-Backed Securities	2	-	-	-	2	