

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-K

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

For the fiscal year ended December 31, 2007

The Savannah Bancorp, Inc.

(Exact name of registrant as specified in its charter)

| | | |
|------------------------|-----------------|-------------------|
| Georgia | 0-18560 | 58-1861820 |
| State of Incorporation | SEC File Number | Tax I.D. Number |

| |
|---|
| 25 Bull Street, Savannah, GA 31401 |
| (Address of principal executive offices) (Zip Code) |

| |
|--|
| 912-629-6486 |
| (Registrant's telephone number, including area code) |

| | |
|--|-----------------------------|
| Securities registered pursuant to Section 12(b) of the Act: | |
| Common, \$1.00 Par Value | NASDAQ Global Market |
| 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 ☒

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act.

Yes ☐ No ☒

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes ☒ No ☐

Indicate by check mark 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. ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☐

Accelerated filer ☒

Non-accelerated filer ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act) Yes ☐ No ☒

The aggregate market value of the voting and non-voting common equity at June 30, 2007 held by non-affiliates, based on the price of the last trade of \$25.10 per share times 4,638,024 non-affiliated shares, was \$116,414,402.

APPLICABLE ONLY TO CORPORATE REGISTRANTS

As of February 29, 2008, the registrant had outstanding 5,929,440 shares of common stock.

Portions of the 2007 Annual Report to Shareholders of Registrant are incorporated in Parts I, II and IV of this report. Portions of the Proxy Statement of Registrant dated March 24, 2008 are incorporated in Part III of this report.

REGISTRANT'S DOCUMENTS INCORPORATED BY REFERENCE

| <u>Document Incorporated by Reference</u> | <u>Part Number and Item Number of Form 10-K Into Which Incorporated</u> |
|---|---|
| Pages F-28 and F-29 of Registrant's 2007 Annual Report to Shareholders | Part II, Item 5, Market for Registrant's Common Equity and Related Shareholder Matters |
| Pages F-26-28, F-36, F-40-42 of Registrant's 2007 Annual Report to Shareholders | Part II, Item 6, Selected Financial Data |
| Pages F-26 through F-42 of Registrant's 2007 Annual Report to Shareholders | Part II, Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations |
| Pages F-37, F-38 and F-40 of Registrant's 2007 Annual Report to Shareholders | Part II, Item 7A, Quantitative and Qualitative Disclosures about Market Risk |
| Pages F-4 through F-25 of Registrant's 2007 Annual Report to Shareholders | Part II, Item 8, Financial Statements and Supplementary Data |
| Pages 4 through 15 of Registrant's Proxy Statement in connection with its Annual Shareholders' Meeting to be held April 24, 2008 ("2008 Proxy Statement") | Part III, Item 10, Directors and Executive Officers |
| Page 12 and pages 15 through 21 of Registrant's 2008 Proxy Statement | Part III, Item 11, Executive Compensation |
| Pages 4 through 8 and page 21 of Registrant's 2008 Proxy Statement | Part III, Item 12, Security Ownership of Certain Beneficial Owners and Management and Related Shareholder Matters |
| Page 22 of Registrant's 2008 Proxy Statement | Part III, Item 13, Certain Relationships and Related Transactions |
| Pages 22 and 23 of Registrant's 2008 Proxy Statement | Part III, Item 14, Principal Accountant Fees and Services |
| Pages F-2 through F-25 of Registrant's 2007 Annual Report to Shareholders | Part IV, Item 15, Exhibits and Financial Statement Schedules |

THE SAVANNAH BANCORP, INC.
2007 ANNUAL REPORT ON FORM 10-K
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PART I

The Savannah Bancorp, Inc. (the "Company") may, from time to time, make written or oral forward-looking statements (as defined in the Private Securities Litigation Reform Act of 1995), including statements contained in the Company's filings with the United States Securities and Exchange Commission ("SEC" or "Commission") (including this Annual Report on Form 10-K and the exhibits thereto), in its reports to shareholders and in other communications by the Company. These forward-looking statements may include, among others, statements about our beliefs, plans, objectives, goals, expectations, estimates and intentions that are subject to significant risks and uncertainties and which may change based on various factors, many of which are beyond our control. The words "may," "could," "should," "would," "believe," "anticipate," "estimate," "expect," "intend," "plan" and similar expressions are intended to identify forward-looking statements. The following factors, among others, could cause our financial performance to differ materially from what is contemplated in those forward-looking statements:

- The strength of the United States economy in general and the strength of the local economies in which the Company conducts operations;
- The effects of and changes in trade, monetary and fiscal policies and laws, including interest rate policies of the Board of Governors of the Federal Reserve System;
- Inflation, interest rate, market and monetary fluctuations;
- Adverse conditions in the stock market and other capital markets and the impact of those conditions on our capital markets and capital management activities, including our investment and wealth management advisory businesses;
- Changes in the cost and availability of funding due to changes in the deposit market and credit market, or the way in which the Company is perceived in such markets;
- The effects of harsh weather conditions, including hurricanes;
- Changes in United States foreign or military policy;
- The timely development of competitive new products and services by the Company and the acceptance of those products and services by new existing customers;
- The willingness of customers to accept third-party products marketed by us;
- The willingness of customers to substitute competitors' products and services for the Company's products and services and vice versa;
- The impact of changes in financial services' laws and regulations (including laws concerning taxes, banking, securities and insurance);
- Technological changes;
- Changes in consumer spending and saving habits;
- The effect of corporate restructuring, acquisitions or dispositions, including the actual restructuring and other related charges and the failure to achieve the expected gains, revenue growth or expense savings from such corporate restructuring, acquisitions or dispositions;
- The growth and profitability of our noninterest or fee income being less than expected;
- Unanticipated regulatory or judicial proceedings;
- The impact of changes in accounting policies by the SEC or the Financial Accounting Standards Board;
- The limited trading activity of our common stock;
- The effects of our lack of a diversified loan portfolio, including the risks of geographic concentrations;
- Adverse changes in the financial performance and/or condition of our borrowers, which could impact the repayment of those borrowers' outstanding loans; and
- The success of the Company at managing the risks involved in the foregoing.

The Company cautions that the foregoing list of important factors is not exclusive. The Company does not undertake to update any forward-looking statement, whether written or oral, that may be made from time to time by or on our behalf except as may be required by our disclosure obligations in filings we make with the SEC under federal securities laws.

Item 1. Business

(a) General Development of Business

The Company was incorporated as a Georgia business corporation on October 5, 1989, for the purpose of becoming a bank holding company. The Company became a bank holding company within the meaning of the Federal Bank Holding Company Act and the Georgia Bank Holding Company Act upon the acquisition of 100 percent of the common stock of The Savannah Bank, National Association ("Savannah") on August 22, 1990.

In February 1998, the Company entered into a plan of merger to exchange shares of its stock for shares of Bryan Bancorp of Georgia, Inc. ("Bryan"), the bank holding company for Bryan Bank & Trust ("Bryan Bank"). The transaction was valued at approximately \$24 million. The merger, which was accounted for as a pooling of interests, was a tax-free reorganization for federal income tax purposes. The merger was consummated on December 15, 1998. Bryan was merged into the Company and Bryan Bank became a wholly-owned subsidiary of the Company on the merger date.

On February 6, 2006, the Company invested \$10 million cash, a portion of the net proceeds from an August 2005 private placement stock offering, in 100 percent of the common stock of Harbourside Community Bank ("Harbourside"), a newly-formed federal stock savings bank, located on Hilton Head Island, South Carolina. In addition to full-service banking, Harbourside conducts mortgage banking activities including mortgage loan origination, sales and servicing. The plans for forming Harbourside began in October 2003 when Savannah opened a mortgage loan production office on Hilton Head Island.

The Company acquired all of the net assets of Minis & Co., Inc. ("Minis") as of August 31, 2007. The net assets of Minis were incorporated into a new, wholly-owned subsidiary of the Company which will continue to operate under the name of Minis & Co., Inc. The acquisition was accounted for using the purchase method of accounting, and accordingly, the results of Minis' operations have been included in the consolidated financial statements beginning September 1, 2007. Minis is a registered investment advisor based in Savannah, Georgia, offering a full line of investment management services. Minis' assets under management at September 1, 2007 were approximately \$500 million.

Savannah, Bryan Bank, Harbourside and Minis are the four operating subsidiaries of the Company. The three bank subsidiaries, collectively, are referred to as the "Subsidiary Banks" or "Banks". Savannah received its charter from the Office of the Comptroller of the Currency ("OCC") to commence business and opened for business on August 22, 1990. Bryan Bank received its charter from the Georgia Department of Banking and Finance ("GDBF") in December 1989. Harbourside received its charter from the Office of Thrift Supervision ("OTS") on February 6, 2006 and commenced public business on March 1, 2006. The deposits at the Subsidiary Banks are insured by the Federal Deposit Insurance Corporation ("FDIC").

As of December 31, 2007, Savannah had six full service offices, total assets of \$624 million, total loans of \$543 million, total deposits of \$517 million, total shareholders' equity of \$51.3 million and \$6.6 million in 2007 net income. As of December 31, 2007, Bryan Bank had one full service office, total assets of \$211 million, total loans of \$187 million, total deposits of \$172 million, total shareholders' equity of \$18.7 million and net income of \$3.8 million for the year then ended. Harbourside had two full service offices, total assets of \$89.5 million, total loans of \$78.6 million, total deposits of \$76.4 million, total shareholders' equity of \$8.7 million and a net loss of \$2.0 million for 2007.

In September 2005, the Company formed SAVB Properties, LLC for the primary purpose of owning a 50 percent interest in two real estate partnerships. Johnson Square Associates, a Georgia general partnership, owns a seven-story, 35,000 square foot building at 25 Bull Street on Johnson Square in downtown Savannah. The Company currently leases approximately 25 percent of this space for its corporate headquarters and the main office of Savannah. Whitaker Street Associates, a Georgia Limited Partnership, owned the 80' x 200' parking lot directly across Whitaker Street from 25 Bull Street. Under an agreement with the City of Savannah, the parking lot is currently being re-developed as part of a 3 acre, 1100 space underground parking garage. Upon completion of the garage construction, the partnership's surface parking lot will be restored and will include the structural foundation adequate to support a 6-story building, the maximum height allowed on this property by city ordinances. This lot will adjoin Ellis Square, one of Savannah's original squares, which is being restored by the City of Savannah.

(b) Information about Industry Segments

In June 1997, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards ("SFAS") No. 131, "Disclosures about Segments of an Enterprise and Related Information" ("SFAS 131"). SFAS 131 requires disclosure of financial and descriptive information about an enterprise's operating segments in annual and interim financial reports issued to shareholders. It defines an operating segment as a component of an enterprise which engages in business activities that generate revenues and incur expenses, whose operating results are reviewed by the chief operating decision makers in the determination of resource allocation and performance, and for which discrete financial information is available. The Company has no segments or any subsidiaries that meet the criteria for segment reporting.

(c) Narrative Description of Business

General

The Company is authorized to engage in any corporate activity permitted by law, subject to applicable federal regulatory restrictions on the activities of bank holding companies. The Company was formed for the primary purpose of becoming a holding company to own 100 percent of the stock of the Subsidiary Banks. The holding company structure provides the Company with greater flexibility than a bank would otherwise have to expand and diversify its business activities through newly formed subsidiaries or through acquisitions.

Banking Services

The Company has approximately 208 full time equivalent employees as of December 31, 2007. The Subsidiary Banks offer a full range of deposit services, including checking accounts, savings accounts and various time deposits ranging from daily money market accounts to long-term certificates of deposit. The transaction accounts and time deposits are tailored to the principal market areas at rates competitive with those offered in the area. In addition, retirement accounts such as Individual Retirement Accounts and Simplified Employee Pension accounts are offered. The FDIC insures all deposit accounts up to the maximum amount (currently \$100,000 per non-retirement account or \$250,000 for certain retirement accounts). The Subsidiary Banks solicit these accounts from individuals, businesses, foundations, organizations, and governmental authorities.

The Subsidiary Banks offer a full range of short-term and medium-term commercial, real estate, residential mortgage and personal loans. The Subsidiary Banks' primary lending focus is business, real estate and consumer lending. Commercial loans include both secured loans and a limited volume of unsecured loans. Consumer loans include secured loans for financing automobiles, home improvements, real estate and other personal investments. Unsecured consumer loans are limited and generally made to the most creditworthy borrowers. The Subsidiary Banks originate fixed and variable rate mortgage loans and offer real estate construction and acquisition loans.

The Subsidiary Banks' lending policies provide each lending officer with written guidance for lending activities as approved by the Banks' Board of Directors ("Board"). Real estate loan-to-value guidelines generally conform to regulatory loan-to-value limits. Additionally, the existence of reliable sources of repayment/cash flow are usually required before making any loan, regardless of the collateral. Appraisals are obtained as required. Lending officers or contract inspectors make on-site inspections on construction loans. Lending authority is delegated to each lending officer by the Credit Committee of each Subsidiary Banks' Board. Loans in excess of the individual officer limits must be approved by a senior officer with sufficient approval authority delegated by these committees. Loans to borrowers whose aggregate combined companywide exposure exceeds \$2,500,000 at Savannah, \$1,300,000 at Harbourside and \$1,000,000 at Bryan Bank require the approval of the Subsidiary Bank's Credit Committee.

Management and the directors are aware that environmental liabilities may negatively impact the financial condition of borrowers, the value of real property and the contingent environmental clean-up liabilities the Subsidiary Banks could incur by having a lien on environmentally deficient property. The Subsidiary Banks generally decline to make loans secured by property with environmental deficiencies. Environmental surveys are required when there is reason for concern about potential environmental liabilities.

Savannah and Bryan Bank operate residential mortgage loan origination departments. The departments take mortgage loan applications, obtain rate commitments and complete various origination documentation and follow-up for an origination and service release fee from third-party mortgage bankers. In addition to generating fee income, the departments also generate banking relationships from its customers and real estate-related contacts. These loans are funded by other mortgage investors and have not been warehoused on Savannah or Bryan Bank's books.

Harbourside's activities in the mortgage banking area include originating, processing, underwriting, closing, warehousing and selling mortgage loans. Since 2006, they have largely discontinued the sale of loans on a servicing retained basis, although they continue to service the loans originated prior to the change. Variations in mortgage origination volume, the value of loans held for sale, the initial valuation of servicing assets and the ongoing valuation of servicing assets for impairment result in the potential for both positive and negative earnings volatility.

Credit Risk Management and Allowance for Loan Losses

The Subsidiary Banks have a comprehensive program designed to control and continually monitor the credit risks inherent in the loan portfolios. This program includes a structured loan approval process in which the Board delegates authority for various types and amounts of loans to loan officers on a basis commensurate with seniority and lending experience. There are four risk grades of "criticized" assets: Special Mention, Substandard, Doubtful and Loss. Assets designated as substandard, doubtful or loss are considered "classified". The classification of assets is subject to regulatory review and reclassification. The Subsidiary Banks include aggregate totals of criticized assets, and general and specific valuation reserves in quarterly reports to the Board, which approves the overall allowance for loan losses evaluation.

The Subsidiary Banks use a risk rating system which is consistent with the regulatory risk rating system. This system applies to all assets of an insured institution and requires each institution to periodically evaluate the risk rating assigned to its assets. The Subsidiary Banks' loan risk rating systems utilize both the account officer and an independent loan review function to monitor the risk rating of loans. Each loan officer is charged with the responsibility of monitoring changes in loan quality within his or her loan portfolio and reporting changes directly to loan review and senior management. The internal credit administration function monitors loans on a continuing basis for both documentation and credit related exceptions. Additionally, the Subsidiary Banks have contracted with an external loan review service which performs a review of the Subsidiary Banks' loans to determine that the appropriate risk grade has been assigned to each borrowing relationship and to evaluate other credit quality, documentation and compliance factors. Delinquencies are monitored on all loans as a basis for potential credit quality deterioration. Commercial and mortgage loans that are delinquent 90 days (four payments) or longer generally are placed on nonaccrual status unless the credit is well-secured and in process of collection. Revolving credit loans and other personal loans are typically charged-off when payments are 120 days past due. Loans are placed on nonaccrual status or charged-off at an earlier date if collection of principal or interest in full becomes doubtful. Real estate acquired through foreclosure is classified as substandard unless there is sufficient evidence to indicate such classification is not warranted.

The allowance for loan losses is evaluated as described in the Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") section of the 2007 Annual Report to Shareholders ("2007 Annual Report") on pages F-31 through F-33.

Other Banking Services

Savannah was granted trust powers by the OCC in 1996. The Trust Department of Savannah contracts with Marshall & Ilsley Trust Company for trust data processing, securities safekeeping and certain other operational functions. This system provides clients and their advisors access to trust account information via the Internet. Employee benefit administration and certain money management functions are outsourced to third parties. Using these resources, the Trust Department offers a full array of trust services, including investment management, personal trusts, custodial accounts, estate administration and retirement plan asset management.

Originally founded in 1932, Minis is a registered investment advisory firm based in Savannah, Georgia. Minis provides fee-only investment services to individuals, families, employee benefit plans, non-profit organizations and other entities.

The Subsidiary Banks offer cash management services, Internet banking, electronic bill payment, non-cash deposit courier service, safe deposit boxes, travelers checks, direct deposit of payroll, U.S. Savings bonds, official bank checks, money orders and automatic drafts for various accounts. The Subsidiary Banks have ten automated teller machines and are members of the *STAR* network of automated teller machines. The Subsidiary Banks issue ATM and debit cards. They also offer VISA and MasterCard credit cards as an agent for a correspondent bank.

Location and Service Area

The Subsidiary Banks' primary service areas include the city of Savannah and surrounding Chatham County, the city of Richmond Hill (which is 20 miles southwest of downtown Savannah) and surrounding Bryan County and Hilton Head Island, Bluffton and southern Beaufort County in South Carolina. Their secondary service areas include Effingham and Liberty Counties, Georgia and Jasper County, South Carolina. The Subsidiary Banks' target customers are individuals and small to medium-sized businesses, including wholesale, retail and professional service businesses in the community. The Subsidiary Banks also target individuals who meet certain net worth and income requirements as potential customers for private banking services.

Savannah's main office, known as the Johnson Square Office, opened in August 1990 and is located in the primary financial district in downtown Savannah, where most of the commercial banks in the primary service area have their main Savannah offices. In recent years, regional banks with headquarters outside of the state of Georgia have acquired several of the banks in the primary service area. Savannah emphasizes that it is based in Savannah and that its directors and officers are committed to the economic development of the Savannah area.

Bryan Bank's main office opened in December 1989 and is located in the primary commercial area of the city of Richmond Hill. Several other community bank branch offices and one grocery store branch office are located in Richmond Hill.

In October 1992, Savannah opened its second office at 400 Mall Boulevard. The Mall Boulevard Office is located in the primary commercial and retail district in Savannah which includes a high concentration of professional and service-related businesses.

In November 1995, Savannah opened its third office, the West Chatham Office, at 100 Chatham Parkway. West Chatham is a full service office located six miles west of the main office in a commercial and industrial growth area of Chatham County.

In October 1997, the fourth office at 4741 Highway 80 East on Whitmarsh Island, six miles east of the main office, opened for business. Deposits, mortgage loans and consumer loans are the primary opportunities for this location which serves a large concentration of higher net worth individuals.

In October 1998, Savannah opened its fifth location in the Medical Arts Shopping Center. This office is strategically located near two major hospitals and numerous medical, dental and professional practices. This location is approximately four miles southeast of the main office.

In May 2002, the Company opened an operations center in 5,000 square feet of office space at 450 Mall Boulevard, adjacent to Savannah's existing branch office at 400 Mall Boulevard. The imaged item processing, statement rendering, information technology, deposit operations and branch operations support functions are located at this center. These functions work closely together and their relocation from different offices to one location provides an opportunity for significant service enhancements, efficiencies and synergies.

In October 2003, Savannah opened a mortgage loan production office on Hilton Head Island, South Carolina which operated as Harbourside Mortgage Company, a division of Savannah, through February 28, 2006. On March 1, 2006, the separately chartered Harbourside opened for business in its new main office building at 852 William Hilton Parkway, the primary traffic artery on Hilton Head Island.

In September 2006, Savannah opened its sixth office in The Village on Skidaway Island adjacent to the Landings community in Savannah. This office location services the higher income individuals and higher net worth retiree island communities nearby.

In December 2007, Harbourside opened its second office in Bluffton, South Carolina on Bluffton Parkway. This is a rapidly growing area with a concentration of residential homes and small businesses.

The Subsidiary Banks' business plans rely principally upon local advertising and promotional activity and upon personal contacts by their directors and officers to attract business and to acquaint potential customers with their personalized services. The Subsidiary Banks emphasize a high degree of personalized customer service. Advertising and marketing emphasize the advantages of dealing with an independent, locally-owned, relationship-oriented bank to meet the particular needs of individuals, professionals and small to medium-size businesses in the community.

Liquidity and Interest Rate Sensitivity Management

Quantitative disclosures regarding the Company's liquidity management are included on pages F-36 to F-38 in the 2007 Annual Report.

Interest Rate Risk

Quantitative discussion of the Company's interest rate risk is included on pages F-37 and F-38 in the 2007 Annual Report.

Federal and State Laws and Regulation of Banks and Bank Holding Companies

Bank holding companies and commercial and federal savings banks are extensively regulated under both federal and state law. These laws and regulations delineate the nature and extent of the activities in which commercial and federal savings banks may engage. In particular, federal savings banks are limited in the amount of commercial, non-residential real property loans and consumer loans they can hold in their portfolio. To the extent that the following information describes statutory and regulatory provisions, it is qualified in its entirety by reference to the particular statutory and regulatory provisions. Change in applicable laws or regulations may have a material effect on the business of the Company and its subsidiaries.

Savannah is subject to extensive supervision and regulation by the OCC, Bryan Bank is subject to extensive supervision by the GBDF and the FDIC and Harbourside is subject to extensive supervision by the OTS. The regulators are responsible for overseeing the affairs of the Subsidiary Banks and periodically examining the Banks to determine their compliance with laws and regulations. The Subsidiary Banks must make quarterly reports of financial condition and results of operations to the regulators. This quarterly financial information is made available to the public approximately 45 days after each quarter-end. Regulators use this data for quarterly offsite monitoring of the financial condition of the Banks. Quarterly holding company reports are filed with the Federal Reserve Bank of Atlanta ("FRB") within 40 days of each quarter-end. This financial information is reviewed by the FRB for accuracy, consistency and reasonableness and is also made available to holding company database providers within 75 days of the end of each quarter. Bank analysts, regulators and consultants regularly use this information in analyzing historical and expected performance of banks and bank holding companies.

The regulators have authority to issue cease and desist orders against banks and bank holding companies which are about to engage, are engaging or have engaged in unsafe or unsound practices in the conduct of their business. The regulators can order affirmative action to correct any harm resulting from a violation or practice, including, but not limited to, making restitution and providing reimbursement or guarantees against loss in certain cases. Regulators also administer several federal statutes, such as the Community Reinvestment Act of 1977 ("CRA") and the Depository Institution Management Interlocks Act, which apply to banks. The Subsidiary Banks are subject to special examination by the FDIC and to certain FDIC regulations.

Regulators have adopted risk-based capital requirements that specify the minimum level for which no prompt corrective action is required. In addition, the FDIC adopts FDIC insurance assessment rates based on certain risk-based and equity capital ratios. The regulators have authority to establish higher capital requirements if they determine that the circumstances of a particular institution require it and to take certain supervisory actions against undercapitalized institutions, the severity of which depends upon the institution's degree of undercapitalization. The table in Note 13 to the Consolidated Financial Statements in the 2007 Annual Report shows the capital ratios for the Company and Subsidiary Banks and the regulatory minimum capital ratios at December 31, 2007. The capital ratios

of the Company and each Subsidiary Bank exceeded the ratios required to be considered "well-capitalized" by the FDIC.

OTS regulations require institutions to meet a qualified thrift lender test. Under the test, such an institution is required to either qualify as a "domestic building and loan association" under the Internal Revenue Code or maintain at least 65% of its "portfolio assets" (total assets less: (i) specified liquid assets up to 20% of total assets; (ii) intangibles, including goodwill; and (iii) the value of property used to conduct business) in certain "qualified thrift investments" (primarily residential mortgages and related investments, including certain mortgage-backed securities) in at least 9 months out of each 12 month period. An institution that fails the qualified thrift lender test is subject to certain operating restrictions and may be required to convert to a bank charter. Harbourside passed the test in each of the four quarters of 2007 and will continue to calculate the ratio at least quarterly.

The Subsidiary Banks are subject to applicable provisions of the Federal Reserve Act ("Act") which restrict the ability of any bank to extend credit to its parent holding company. Additionally, a national banking association cannot extend credit to any affiliate (including its parent and non-bank subsidiaries of its parent); issue a guarantee, acceptance or letter of credit (including an endorsement or standby letter of credit) on behalf of its affiliates; invest in the stock or securities of affiliates or, under certain circumstances, take such stock or securities as collateral for loans to any borrower.

Shareholders of banks (including bank holding companies which own stock in banks, such as the Company) may be compelled by bank regulatory authorities to invest additional capital in the event their bank's capital becomes impaired by losses or otherwise. Failure to pay such an assessment could cause a forced sale of the holder's bank stock. In addition, the Company may also be required to provide additional capital to any banks that it acquires as a condition to obtaining the approvals and consents of regulatory authorities in connection with such acquisitions.

The earnings of the Subsidiary Banks and, consequently, of the Company, are affected significantly by the policies of the Board of Governors of the Federal Reserve System (the "Fed"), which regulates the money supply in order to mitigate recessionary and inflationary pressures. Among the techniques used to implement these objectives are open market operations in United States Government securities, changes in the rate paid by banks on bank borrowings, and changes in reserve requirements against bank deposits. These techniques are used in varying combinations to influence overall growth and distribution of bank loans, investments and deposits, and their use may also affect interest rates charged on loans or paid for deposits. The monetary policies of the Fed have had a significant effect on the operating results of banks in the past and are expected to continue to do so in the future.

The Company, as a bank holding company, is required to register as such with the Fed and the GDBF. It is required to file with both of these agencies quarterly and annual reports and other information regarding its business operations and those of its subsidiaries. It is also subject to examination by these two agencies and will be required to obtain their approval before acquiring, directly or indirectly, ownership or control of any voting shares of a bank or bank subsidiary of a bank holding company if, after such acquisition, it would own or control, directly or indirectly, more than five percent of the voting stock of such bank or banking subsidiary of a bank holding company. Furthermore, a bank holding company is prohibited from acquiring direct or indirect ownership or control of any voting stock of any company which is not a bank or bank holding company, with limited exceptions. It must engage only in the business of banking, managing or controlling banks or furnishing services to or performing services for its subsidiary banks. During 1996, the Fed enacted regulations that are slightly less restrictive regarding the types of businesses which bank holding companies may own.

Banking organizations are prohibited under the Act from participating in new financial affiliations unless their depository institution subsidiaries are well-capitalized and well-managed. Regulators are required to address any failure to maintain safety and soundness standards in a prompt manner. In addition, regulators must prohibit holding companies from participating in new financial affiliations if, at the time of certification, any insured depository affiliate had received a less than "satisfactory" CRA rating at its most recent examination.

Affiliation Authority - The Gramm-Leach-Bliley Act of 1999 ("GLB") amended section 4 of the Act to provide a framework for engaging in new financial activities. Those bank holding companies ("BHCs") that qualify to engage in the new financial activities are designated as Financial Holding Companies ("FHCs"). Provisions of GLB permit BHCs that qualify as FHCs to engage in activities, and acquire companies engaged in activities, that are financial in nature or incidental to such financial activities. FHCs are also permitted to engage in activities that are

"complementary" to financial activities if the Fed determines that the activity does not pose a substantial risk to the safety or soundness of the institution or the financial system in general.

The Fed may act by either regulation or order in determining what activities are financial in nature, incidental to financial in nature, or complementary. In doing so, the Fed must notify the Treasury Department ("Treasury") of requests to engage in new financial activities and may not determine that an activity is financial or incidental to a financial activity if Treasury objects. Furthermore, Treasury may propose that the Fed find a particular activity financial in nature or incidental to a financial activity. GLB establishes a similar procedure with regard to the Treasury's (acting through the OCC) determination of financial activities and activities that are incidental to financial activities for subsidiaries of national banks. Congress intended for the Fed and Treasury to establish a consultative process that would negate the need for either agency to veto a proposal of the other agency.

Federal Home Loan Bank Reform - GLB reformed the Federal Home Loan Bank ("FHLB") System, including expanding the collateral that a community bank can pledge against FHLB advances, thus giving smaller banks access to a substantial new liquidity source.

Privacy - GLB imposed a number of new restrictions on the ability of financial institutions to share nonpublic personal information with nonaffiliated third parties. Specifically, the GLB:

- requires financial institutions to establish privacy policies and disclose them annually to all customers, setting forth how the institutions share nonpublic personal financial information with affiliates and third parties;
- directs regulators to establish regulatory standards that ensure the security and confidentiality of customer information;
- permits customers to prohibit ("opt out" of permitting) such institutions from disclosing personal financial information to nonaffiliated third parties;
- prohibits transfer of credit card or other account numbers to third-party marketers;
- prohibits pretext calling (that is, makes it illegal for information brokers to call banks to obtain customer information with the intent to defraud the bank or customer);
- protects stronger state privacy laws, as well as those not "inconsistent" with the federal rules;
- requires the Treasury and other federal regulators to study the appropriateness of sharing information with affiliates, including considering both negative and positive aspects of such sharing for consumers.

GLB also imposes an affirmative obligation on banks to respect their customers' privacy interests. Language protects a community bank's ability to share information with third parties selling financial products (for example, insurance or securities) to bank customers. Community banks can thus continue such sales practices without being subject to the opt-out provisions contained elsewhere in the legislation.

The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 (the "Riegle-Neal Act") has introduced a process that enables nationwide interstate banking through bank subsidiaries and interstate bank mergers. Separately, the Riegle-Neal Act also permits bank subsidiaries to act as agents for each other across state lines. Since September 29, 1995, adequately capitalized and managed bank holding companies have been permitted to acquire control of a bank in any state. Acquisitions are subject to concentration limits. Beginning June 1, 1997, banks were permitted to merge with one another across state lines. The Interstate Banking Act also permits de novo branching to the extent that a particular state "opts into" the de novo branching provisions. The legislation preserves the state laws which require that a bank must be in existence for a minimum period of time before being acquired as long as the requirement is five years or less. This legislation has relevance for the banking industry due to increased competitive forces from institutions which may consolidate through mergers and those which may move into new markets through enhanced opportunities to branch across state lines. Georgia and South Carolina do not have reciprocal provisions for de novo branches or charters. Holding companies domiciled in Georgia may not branch or charter banks in South Carolina and vice versa. Alternatives for expansion between these states include acquiring an existing financial institution, chartering a federal savings bank or moving the charter of a national bank within 35 miles of its headquarters into the new state.

A bank holding company and its subsidiaries are prohibited from engaging in certain tie-in arrangements in connection with the extension of credit or provision of any property or service. Thus, a bank may not extend credit, lease or sell property or furnish any service or fix or vary the consideration for such on the condition that (i) the

customer should obtain or provide some additional credit, property or service from or to such bank (other than a loan, discount, deposit or trust service related to and usually provided in connection with a loan, discount, deposit or trust service), its bank holding company or any other subsidiary of its bank holding company or (ii) the customer may not obtain some other credit, property or service from a competitor, except to the extent reasonable conditions are imposed in a credit transaction to assure the soundness of the credit extended.

The Fed has cease and desist powers over bank holding companies and non-banking subsidiaries should their actions constitute a serious threat to the safety, soundness or stability of a subsidiary bank. The Company is also subject to certain restrictions with respect to engaging in the business of issuing, underwriting and distributing securities.

Although the Company is not presently subject to any direct regulatory restrictions on dividends (other than those of Georgia corporate law), the Company's long-term ability to pay cash dividends will depend on the amount of dividends paid by the Subsidiary Banks and any other subsequently acquired entities. OCC regulations restrict the amount of dividends which Savannah may pay without obtaining prior approval. Based on such regulatory restrictions without prior approval, Savannah is restricted from paying dividends in a calendar year which exceeds the current year's net income combined with the retained net profits of the preceding two years. Bryan Bank may pay dividends equal to no more than 50 percent of prior year net income without prior approval from the GDBF. Harbourside does not anticipate paying dividends for the foreseeable future. The dividend payout plans of the Subsidiary Banks consider the objective of maintaining their "well-capitalized" status.

The Subsidiary Banks are members of the FHLB System, which consists of 12 regional FHLBs subject to supervision and regulation by the Federal Housing Finance Board. The FHLBs maintain central credit facilities primarily for member institutions. The Subsidiary Banks, as members of the FHLB of Atlanta, are required to hold shares of capital stock in the FHLB of Atlanta in an amount at least equal to the greater of: (i) 1 percent of the aggregate outstanding principal amount of its unpaid residential mortgage loans, home purchase contracts and similar obligations as of the beginning of each year, (ii) 4.5 percent of its advances (borrowings) from the FHLB of Atlanta, or (iii) \$500,000. Additionally, the FHLB of Atlanta imposed a maximum investment in its capital stock equal to \$100,000 over the required minimum. The Subsidiary Banks are in compliance with this requirement at December 31, 2007.

Each FHLB serves as a reserve or central bank for its member institutions within its assigned regions. It is funded primarily from proceeds derived from the sale of obligations of the FHLB System. The FHLB makes advances (i.e., loans) to members in accordance with policies and procedures established by its Board. The Subsidiary Banks are authorized to borrow funds from the FHLB of Atlanta to meet demands for withdrawals of deposits, to meet seasonal requirements and for the expansion of its loan portfolio. Advances may be made on a secured or unsecured basis depending upon a number of factors, including the purpose for which the funds are being borrowed and the amount of previously existing advances. Interest rates charged for advances vary depending upon maturity, the cost of funds to the FHLB of Atlanta and the purpose of the borrowing.

Community Reinvestment Act

CRA requires the federal bank regulatory agencies to encourage financial institutions to meet the credit needs of low- and moderate-income borrowers in their local communities. In May 1995, the federal bank regulatory agencies published final amended regulations promulgated pursuant to the CRA. The final regulations eliminate the 12 assessment factors under the former regulation and replace them with performance tests. Institutions are no longer required to prepare CRA statements or extensively document director participation, marketing efforts or the ascertainment of community credit needs. Under the final rule, an institution's size and business strategy determines the type of examination that it will receive. Large, retail-oriented institutions are examined using a performance-based lending, investment and service test. Small institutions are examined using a streamlined approach. All institutions have the option of being evaluated under a strategic plan formulated with community input and pre-approved by the applicable bank regulatory agency.

CRA regulations provide for certain disclosure obligations. In accordance with the CRA, each institution must post a CRA notice advising the public of the right to comment to the institution and its regulator on the institution's CRA performance and to review the CRA public file. Each lending institution must maintain for public inspection a public file that includes a listing of branch locations and services, a summary of lending activity, a map of its communities, and any written comments from the public on its performance in meeting community credit needs.

Large institutions also are required to collect certain data, including the amount and location of originated and purchased small business, small farm, community development, and home mortgage loans, and to report this data to their regulatory agencies.

Public disclosure of written CRA evaluations of financial institutions made by regulatory agencies is required under the CRA. This promotes enforcement of CRA requirements by providing the public with the status of a particular institution's community reinvestment record. Savannah and Bryan Bank received a "satisfactory" rating on the most recent performance evaluations of their CRA efforts by their respective banking regulatory agencies. Harbourside has not yet been evaluated.

Fair Lending

Congress and various federal agencies responsible for implementing fair lending laws have been increasingly concerned with discriminatory lending practices. In 1994, those federal agencies announced a Joint Policy Statement detailing specific discriminatory practices prohibited under the Equal Opportunity Act and the Fair Housing Act. In the Policy Statement, three methods of proving lending discrimination were identified: (i) overt evidence of discrimination, where a lender blatantly discriminates on a prohibited basis; (ii) evidence of disparate treatment, when a lender treats applicants differently based upon a prohibited factor, even where there is no evidence showing that the treatment was motivated by intention to discriminate; and (iii) evidence of disparate impact, when a lender applies a practice uniformly to all applicants, but the practice has a discriminatory effect, even where such practices are neutral in appearance and applied equally.

Anti-Money Laundering

The Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 ("Patriot Act") significantly expands the responsibilities of financial institutions in preventing the use of the United States financial system to fund terrorist activities.

Title III of the Patriot Act provides for a significant overhaul of the United States anti-money laundering regime. Among other provisions, it requires financial institutions operating in the United States to develop new anti-money laundering compliance programs, due diligence policies and controls to ensure the detection and reporting of money laundering. Such required compliance programs are intended to supplement existing compliance requirements, also applicable to financial institutions, under the Bank Secrecy Act and the Office of Foreign Assets Control Regulations. This federal legislation and the resultant bank regulations require a financial institution to expeditiously search its records to determine whether it maintains or has maintained accounts, or engaged in transactions with individuals or entities listed in a database maintained by the Financial Crimes Enforcement Network ("FinCEN"). The records search must cover current accounts, accounts opened in the prior twelve months, and transactions conducted in the prior six months. Its purpose is to identify funds or transactions with individuals associated with terrorist activities. Substantial penalties and/or criminal prosecution may result from non-compliance. Management has established policies and procedures to ensure compliance with the Patriot Act.

Rules Adopted by the SEC

The Sarbanes-Oxley Act of 2002 ("Sarbox") was enacted to enhance penalties for accounting and auditing improprieties at publicly traded companies and to protect investors by improving the accuracy and reliability of corporate disclosures under the federal securities laws. Sarbox typically applies to all companies, including the Company, which file or are required to file periodic reports with the SEC. Generally, Sarbox (i) requires chief executive officers and chief financial officers to certify to the accuracy of periodic reports filed with the SEC; (ii) imposes specific and enhanced corporate disclosure requirements; (iii) accelerates the time frame for reporting of insider transactions and periodic disclosures by public companies; (iv) requires companies to adopt and disclose information about corporate governance practices, including whether or not they have adopted a code of ethics for senior financial officers and whether the audit committee includes at least one "audit committee financial expert;" and (v) requires the SEC, based on certain enumerated factors, to regularly and systematically review corporate filings.

Recent Banking Legislation

Bills are presently pending before the United States Congress and certain state legislatures, and additional bills may be introduced in the future in the Congress and the state legislatures, which, if enacted, may alter the structure, regulation and competitive relationships of the nation's financial institutions. It cannot be predicted whether or in what form any of these proposals will be adopted or the extent to which the business of the Company or the Subsidiary Banks may be affected thereby.

Competition

The banking business is very competitive. Banks generally compete with other financial institutions using the mix of banking products and services offered, the pricing of services, the convenience and availability of services, and the degree of expertise and the personal manner in which services are offered. The Subsidiary Banks compete with other commercial and savings banks in their primary service areas. The Subsidiary Banks also compete with credit unions, consumer finance companies, insurance companies, money market mutual funds, brokerage firms and other financial institutions, some of which are not subject to the degree of regulation and restriction imposed upon the Subsidiary Banks. Many of these competitors have substantially greater resources and lending limits than the Subsidiary Banks and offer certain services that the Subsidiary Banks do not provide currently.

Many of these competitors have more branch offices in the Subsidiary Bank's primary service area. However, the Company's plan is to expand into the markets which will best serve its targeted customers. Management believes that competitive pricing, local ownership, local decisions, local control and personalized, relationship-oriented service provide the Subsidiary Banks with a method to compete effectively for prospective customers.

The Subsidiary Banks experience the most competition from new local community bank entrants into the market area. Numerous banking offices of community banks and de novo banks have opened in the Savannah market since January 1, 2002. Other banks have indicated interest in the coastal Georgia and South Carolina markets. These new entrants have increased and will continue to increase the competition for existing and new business.

Deposit growth is a substantial challenge facing the banking industry and the Subsidiary Banks. It is likely that deposit growth in competitive markets will require higher deposit interest rates. Higher costs of funds without corresponding higher rates on earning assets will have a long-term negative impact on net interest income. Higher growth in lower cost core deposits, higher revenue growth from fee based services and lower overhead growth rates are the key items required to accomplish the Company's earnings growth objectives.

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SELECTED STATISTICAL INFORMATION FOR THE COMPANY

Investments

Table 1 - Weighted Average Yields by Maturity

The following table sets forth the amortized cost, fair value and tax-equivalent yields by investment type and maturity category at December 31, 2007:

| | Amortized Cost (Thousands) | Fair Value | Taxable Equivalent Yield (a) (%) |
|---|----------------------------------|---------------|---|
| Securities available for sale: | | | |
| U.S. Treasury, other U.S. Government Agencies and mortgage-backed: | | | |
| Within one year | \$ 11,346 | \$ 11,500 | 4.67 |
| One year to five years | 27,442 | 27,814 | 4.95 |
| Five years to ten years | 12,142 | 12,306 | 5.21 |
| Over ten years | 1,921 | 1,947 | 5.23 |
| Total | 52,851 | 53,567 | 4.96 |
| Other interest-earning investments: | | | |
| Within one year | 4,115 | 4,171 | 6.07 |
| One year to five years | 1,706 | 1,729 | 7.18 |
| Five years to ten years | 1,014 | 1,027 | 8.53 |
| Over ten years | 555 | 563 | 6.00 |
| Total | 7,390 | 7,490 | 6.66 |
| Total securities available for sale | \$ 60,241 | \$ 61,057 | 5.17 |

(a) The yield is calculated on the amortized cost of the securities.

Loans

Following is certain information regarding the loan portfolio as of December 31, 2007 on a consolidated basis.

Table 2 - Loan Repricing Opportunities

The following table sets forth certain loan maturity and repricing information as of December 31, 2007. Loan renewals generally reprice relative to the prime rate in effect at the time of the renewal. Management expects that certain real estate mortgage loans which have maturities of one to three years with longer amortization periods will renew at maturity.

| (\$ in thousands) | | | | |
|--|------------------------|--|-----------------------|------------|
| Loan Category | One Year or Less | After One Year Through Five years | Over Five Years | Total |
| Real estate-construction and development | \$ 117,477 | \$ 13,584 | \$ 3,049 | \$ 134,110 |
| Commercial | 49,597 | 18,506 | 3,267 | 71,370 |
| Total | \$ 167,074 | \$ 32,090 | \$ 6,316 | \$ 205,480 |
| Loans with fixed rates | \$ 34,907 | \$ 28,449 | \$ 6,202 | \$ 69,558 |
| Loans with floating and adjustable rates | 135,922 | - | - | 135,922 |
| Total | \$ 170,829 | \$ 28,449 | \$ 6,202 | \$ 205,480 |

Nonaccrual, Past Due and Restructured Loans

At December 31, 2007 and 2006, nonperforming loans were \$17,424,000 and \$2,231,000, respectively. At December 31, 2007, the Subsidiary Banks had nonaccruing loans of \$14,663,000 and \$2,761,000 in loans past due 90 days or more. Interest income of \$731,000 was recognized on nonaccrual loans in 2007.

Except for consumer loans, the Company's policy is to place loans on nonaccrual status when, in management's judgment, the collection of principal and interest in full becomes doubtful. Interest receivable accrued in prior years and subsequently determined to have doubtful collectibility is charged to the allowance for loan losses. Interest on loans that are placed on nonaccrual is recognized after principal is collected in full. In some cases where borrowers are experiencing financial difficulties, loans may be restructured to provide terms significantly different from the original contractual terms.

Loan Concentrations

Most of the Company's business activity is with customers located within Chatham and Bryan County, Georgia and southern Beaufort County, South Carolina. Table 6 on page F-36 of the 2007 Annual Report provides details of the various real estate loan concentrations. The Company has no loans that are considered to be highly leveraged transactions or foreign credits.

Allowance for Loan Losses

See pages F-31 through F-33 of the 2007 Annual Report for details about the activity and breakdown of the allowance for loan losses and additional information regarding accounting estimates in the allowance.

Deposits

Deposit Average Balances and Rates Paid

Tables 8 and 9 on pages F-41 and F-42 of the 2007 Annual Report summarize the average balances of the Company's deposits and the average rates paid on such deposits during 2007, 2006 and 2005.

Table 3 - Long-term Obligations

The following table includes a breakdown of payment obligations due under long-term contracts:

| (\$ in thousands) | Payments Due by Period | | | | |
|------------------------------|------------------------|---------------------|----------------|----------------|----------------------|
| | Total | Less than 1 Year | 1 - 3 Years | 4 - 5 Years | More than 5 Years |
| Contractual Obligations | | | | | |
| FHLB advances - long-term | \$ 2,973 | \$ 1,750 | \$ 1,050 | \$ - | \$ 173 |
| Subordinated debt | 10,310 | - | - | - | 10,310 |
| Operating leases - buildings | 12,087 | 1,092 | 1,558 | 1,335 | 8,102 |
| Long-term contracts | 5,036 | 1,152 | 2,409 | 1,475 | - |
| Total | \$ 30,406 | \$ 3,994 | \$ 5,017 | \$ 2,810 | \$ 18,585 |

Item 1A. Risk Factors

Like other financial companies, the Company is subject to a number of risks, many of which are outside of our direct control. Efforts are made to manage those risks while optimizing returns. Among the risks assumed are: (1) credit risk, which is the risk that loan customers or other counterparties will be unable to perform their contractual obligations, (2) market risk, which is the risk that changes in market rates and prices will adversely affect our financial condition or results of operation, (3) liquidity risk, which is the risk that the Company and/or Banks will have insufficient cash or access to cash to meet its operating needs, (4) operational risk, which is the risk of loss resulting from inadequate or failed internal processes, people and systems, or external events and (5) common stock marketability risk, which is risk specifically related to the marketability of the Company's common stock.

In addition to the other information included or incorporated by reference into this report, readers should carefully consider that the following important factors, among others, could materially impact our business, future results of operations, and future cash flows.

Credit Risk

Our business is affected by the strength of the local economies where we operate.

Our success significantly depends upon the growth in population, income levels, deposits and real estate development in our primary markets in coastal Georgia and South Carolina. If these communities do not grow or if prevailing economic conditions locally or nationally are unfavorable, our business may be adversely impacted. We are less able than larger institutions to spread the risks of unfavorable local economic conditions across a large number of diversified economies. Moreover, we cannot give any assurance that we will benefit from any market growth or favorable economic conditions in our primary market areas.

Any adverse market or economic conditions in coastal Georgia and South Carolina may disproportionately increase the risk that our borrowers will be unable to make their loan payments. In addition, the market value of the real estate securing loans could be adversely affected by unfavorable changes in market and economic conditions. The Hilton Head Island/Bluffton ("HHI/Bluffton") market experienced a pronounced slowdown in the fourth quarter of 2007 which adversely affected our speculative and non-owner occupied residential real estate loans that were originated in 2004-2006 in a stronger real estate market. As of December 31, 2007, approximately 89% of our loans held for investment were secured by real estate. Of the commercial real estate loans in our portfolio, approximately 38% represent properties owned and occupied by businesses to which we have extended loans. Any sustained period of increased payment delinquencies, foreclosures or losses caused by adverse market or economic conditions in coastal Georgia and South Carolina could further adversely affect the value of our assets, our revenues, results of operations and overall financial condition.

Our business is concentrated in the areas of Chatham and Bryan County, Georgia and southern Beaufort County, South Carolina.

Currently, our lending and other business is concentrated in Chatham and Bryan Counties in Georgia and southern Beaufort County in South Carolina. A downturn in market conditions in any of the respective areas may adversely affect the performance of our loans and the results of our operations and financial condition. In particular, Hilton Head Island in southern Beaufort County is a vacation and resort area with high concentrations of second home and investment properties. Changes in interest rates, local or general economic conditions, real estate values or the income tax deductibility of mortgage interest may subject this market to greater volatility which could adversely impact our performance. Additionally, our market area is susceptible to the risk of hurricane disasters and many areas are located in flood zones. While most such losses are insurable, hurricanes and flooding could adversely affect operations and our financial condition.

If our allowance for loan losses is not sufficient to cover actual charge-offs, our earnings could decrease.

Our loan customers may not repay their loans according to the terms of these loans and the collateral securing the payment of these loans may be insufficient to assure repayment. We may experience significant charge-offs which could have a material adverse effect on our operating results. Our management makes various assumptions and judgments about the collectibility of our loans, including the creditworthiness of our borrowers and the value of the

real estate and other assets serving as collateral for the repayment of our loans. We maintain an allowance for loan losses in an attempt to cover any charge-offs which may occur. In determining the size of the allowance, we rely on an analysis of our loan portfolio based on historical loss experience, volume and types of loans, trends in classification, volume and trends in delinquencies and nonaccruals, national and local economic conditions and other pertinent information. As we expand into new markets, such as the coastal South Carolina market in which Harbourside operates, our determination of the size of the allowance could be understated due to our lack of familiarity with market-specific factors. As noted above, the HHI/Bluffton market experienced a slowdown in the fourth quarter of 2007 which necessitated additional provisions for loan losses at Savannah and Harbourside.

If our assumptions are wrong, our current allowance may not be sufficient to cover future charge-offs, and adjustments may be necessary to allow for different economic conditions or adverse developments in our loan portfolio. Material additional provisions to our allowance would materially decrease our net income.

In addition, federal and state regulators periodically review our allowance for loan losses and may require us to increase our provision for loan losses or recognize further loan charge-offs, based on judgments different than those of our management. Any increase in our allowance for loan losses or loan charge-offs as required by these regulatory agencies could have a negative effect on our operating results.

Market Risk

Changes in interest rates could negatively impact our financial condition and results of operations.

Our earnings are significantly dependent on our net interest income. We expect to realize income primarily from the difference between interest earned on loans and investments and the interest paid on deposits and borrowings. We expect that we will periodically experience "gaps" in the interest rate sensitivities of our assets and liabilities, meaning that either our interest-bearing liabilities will be more sensitive to changes in market interest rates than our interest-earning assets, or vice versa. In either event, if market interest rates should move contrary to our position, this "gap" would work against us, and our earnings may be negatively affected.

For example, in the event of a decrease in interest rates, our net interest income will be negatively affected because our interest-bearing assets currently reprice faster than our interest-bearing liabilities. Although our asset-liability management strategy is designed to control our risk from changes in market interest rates, we may not be able to prevent changes in interest rates from having a material adverse effect on our results of operations and financial condition.

Changes in the level of interest rates also may negatively affect our ability to originate loans, the value of our assets and our ability to realize gains from the sale of our assets, all of which ultimately affect our earnings. A decline in the market value of our assets may limit our ability to borrow additional funds or result in our lenders requiring additional collateral from us under our loan agreements. As a result, we could be required to sell some of our loans and investments under adverse market conditions, upon terms that are less favorable to us, in order to maintain our liquidity. If those sales are made at prices lower than the amortized costs of the investments, we will incur losses. While rising interest rates are favorable to us, declining rates, like those experienced in 2007, generally have a negative impact on earnings. There can be no assurance or guarantee that declining rates will not continue to negatively impact earnings or that we will be able to take measures to hedge, on favorable terms or at all, against unfavorable events, which could adversely affect our results of operations and financial condition.

Monetary policies may adversely affect our business and earnings.

Our results of operations are affected by the policies of monetary authorities, particularly the Fed. Changes in interest rates can affect the number of loans we originate, as well as the value of our loans and other interest-bearing assets and liabilities and the ability to realize gains on the sale of those assets and liabilities. Prevailing interest rates also affect the extent to which borrowers prepay loans owned by us. When interest rates decrease, borrowers are more likely to prepay their loans, and vice versa. We may be required to invest funds generated by prepayments at less favorable interest rates. Increases in interest rates could hurt the ability of borrowers who have loans with floating interest rates to meet their increased payment obligations. If those borrowers were not able to make their payments, then we could suffer losses, and our level of nonperforming assets could increase.

The loss of significant revenues in Minis could result in lower operating earnings as well as significant non-cash charges to earnings related to the impairment of goodwill and accelerated amortization of the client list intangible asset.

Asset management fee revenues are directly impacted by the total investments under management. The assets under management are impacted by stock values, bond values, interest rates and the gain or loss of accounts due primarily to investment performance. Minis' selling shareholders have significant earn-out incentives to maintain and increase revenues through June 2010. However, events and decisions beyond their control can negatively impact assets under management and the related revenues from such assets.

Liquidity Risk

Our use of brokered deposits, uninsured local deposits and other borrowings may impair our liquidity and constitute an unstable and/or higher cost funding source.

We use wholesale, institutional and brokered deposits, uninsured local deposits and other borrowings, including repurchase agreements, federal funds purchased and FHLB borrowings, to fund a portion of our operations. Federal law requires a bank to be well-capitalized if it accepts new brokered deposits. Thus, the Company and the Banks must maintain a "well-capitalized" status to meet our funding plans. Failure to maintain "well-capitalized" status would limit our access to wholesale and brokered deposits and federal funds purchased (but not necessarily repurchase agreements or FHLB borrowings), which could impair our liquidity. We will be considered "well-capitalized" if we (i) have a total risk-based capital ratio of 10.0 percent or greater; (ii) have a Tier 1 risk-based capital ratio of 6.0 percent or greater; (iii) have a leverage ratio of 5.0 percent or greater; and (iv) are not subject to any written agreement, order, capital directive, or prompt corrective action directive issued by the FDIC to meet and maintain a specific capital level for any capital measure.

Depositors that invest in brokered deposits are generally interest rate sensitive and well informed about alternative markets and investments. Consequently, funding with brokered deposits may not provide the same stability to our deposit base as traditional local retail deposit relationships. Our liquidity may be negatively affected if brokered deposit supply declines due to a loss of investor confidence or a flight to higher quality investments such as U.S. Treasury securities. In addition, brokered deposits typically have a higher rate of interest than core local deposits.

Deposit balances in excess of the FDIC's \$100,000 insurance limit (\$250,000 for certain retirement accounts) per depositor are uninsured deposits. Customers with uninsured deposits are more sensitive to financial or reputation risk than insured depositors. Consequently, uninsured deposits do not provide the same stability to our deposit base as insured deposits. Our liquidity may be negatively affected by a decline in uninsured deposits due to a loss of investor confidence and a flight to insured deposits at other financial institutions.

Operational Risk

Future departures of our key personnel may impair our operations.

We are, and for the foreseeable future will be, dependent on the services of John C. Helmken II, President and Chief Executive Officer of the Company and of Savannah; E. James Burnsed, Vice Chairman of the Company and Chairman and Chief Executive Officer of Bryan Bank; R. Stephen Stramm, Executive Vice President – Lending of the Company and of Savannah; Robert B. Briscoe, Executive Vice President and Chief Financial Officer of the Company and of Savannah; and Jerry O'Dell Keith, a Vice President of the Company and President of Bryan Bank. Should the services of any of Messrs. Helmken, Burnsed, Stramm, Briscoe or Keith become unavailable, there can be no assurance that a suitable successor could be found who will be willing to be employed upon terms and conditions acceptable to us. A failure to replace any of these individuals promptly, should his services become unavailable, could have a material adverse effect on our results of operations and financial performance. These risks are heightened by the fact that none of these officers have entered into employment agreements with the Company or Banks. G. Mike Odom, Jr., CEO, resigned on November 17, 2006 effective February 28, 2007 to pursue other professional interests. An orderly management transition was made in the CEO position, and in 2007 several key hires were made for senior management positions.

Our continued pace of growth may require us to raise additional capital in the future, but that capital may not be available when it is needed.

We are required by federal and state regulatory authorities to maintain adequate levels of capital to support our operations. We anticipate that our current capital resources will satisfy our capital requirements for the foreseeable future. We may, at some point, however, need to raise additional capital to support our continued growth.

Our ability to raise additional capital, if needed, will depend on conditions in the capital markets at that time, which are outside our control, and on our financial performance. Accordingly, we cannot give any assurances of our ability to raise additional capital if needed on terms acceptable to us, or at all. If we cannot raise additional capital when needed, our ability to further expand our operations through internal growth and acquisitions could be materially impaired.

We have limited operating history for Harbourside upon which to base an estimate of our future financial performance.

Harbourside opened for business on March 1, 2006 and has a relatively short operating history as a bank. There was also turnover in the initial senior management, but Thomas W. Lennox has served as President and CEO since October 2006. Our operations at Harbourside are subject to the risks inherent in the establishment of any new business and, specifically, those of a new bank. Harbourside has experienced significant losses and may not be profitable for several quarters, if ever.

Our industry operates in a highly regulated environment. New laws or regulations or changes in existing laws or regulations affecting the banking industry could have a material adverse effect on our results of operations.

The Company and the Banks are subject to extensive government regulation and supervision under various state and federal laws, rules and regulations, primarily the rules and regulations of the OCC, OTS, FDIC, GDBF, SEC and the Fed. These laws and regulations are designed primarily to protect depositors, borrowers, and the deposit insurance funds of the FDIC. These regulators maintain significant authority to impose requirements on our overall operations, such as limiting certain activities or mandating the increase of capital levels. The financial services industry also is subject to frequent legislative and regulatory changes and proposed changes, the effects of which cannot be predicted.

We face substantial competition in our industry sector from banking and financial institutions that have larger and greater financial and marketing capabilities, which may hinder our ability to compete successfully.

The banking and financial services industry is highly competitive. This competitiveness may negatively impact our ability to retain qualified management and loan officers, raise sufficient deposits at an acceptable price, and attract customers. The increasingly competitive environment is a result of changes in regulation, changes in technology and product delivery systems, and the accelerating pace of consolidation among financial providers.

We compete with many different banking and financial institutions, including banks and savings and loan associations, credit unions, brokerage and investment banking firms, and mortgage companies and brokers. These entities may be branches or subsidiaries of much larger organizations affiliated with statewide, regional or national banking companies and, as a result, may have greater resources and lower costs of funds. These entities may also be start-up organizations. Any of these entities may attempt to duplicate our business plan and strategy. There can be no assurance that we will be able to compete effectively in the future.

Failure to implement our business strategies may adversely affect our financial performance.

Our management has developed a business plan that details the strategies we intend to implement in our efforts to continue profitable operations. If we cannot implement our business strategies, we may be hampered in our ability to develop business and serve our customers, which could, in turn, have an adverse effect on our financial performance. Even if our business strategies are successfully implemented, they may not have the favorable impact on operations that we anticipate.

An extended disruption of vital infrastructure could negatively impact our business, results of operations, and financial condition.

Our operations depend upon, among other things, our infrastructure, including equipment and facilities. Extended disruption of vital infrastructure by fire, power loss, natural disaster, telecommunications failure, computer hacking or viruses, terrorist activity or the domestic and foreign response to such activity, or other events outside of our control could have a material adverse impact on the financial services industry as a whole and on our business, results of operations, cash flows, and financial condition in particular. Our disaster recovery and business resumption contingency plans may not work as intended or may not prevent significant interruptions of our operations.

Non-compliance with the Patriot Act, Bank Secrecy Act, or other laws and regulations could result in fines or sanctions.

The Patriot and Bank Secrecy Acts require financial institutions to develop programs to prevent financial institutions from being used for money laundering and terrorist activities. If such activities are detected, financial institutions are obligated to file suspicious activity reports with the Treasury's FinCEN. These rules require financial institutions to establish procedures for identifying and verifying the identity of customers seeking to open new financial accounts. Failure to comply with these regulations could result in fines or sanctions. We have developed policies and procedures designed to assist in compliance with these laws and regulations.

The Fed may require the Company to commit capital resources to support the Subsidiary Banks.

The Fed, which examines the Company and our non-bank subsidiaries, has a policy stating that a bank holding company is expected to act as a source of financial and managerial strength to a subsidiary bank and to commit resources to support such subsidiary bank. Under the source of strength doctrine, the Fed may require a bank holding company to make capital injections into a troubled subsidiary bank, and may charge the bank holding company with engaging in unsafe and unsound practices for failure to commit resources to such a subsidiary bank. Capital injections may be required at times when the holding company may not have the resources to provide it, and, therefore, may be required to borrow the funds. Loans from a holding company to its subsidiary banks are subordinate in right of payment to deposits and to certain other indebtedness of such subsidiary bank. In the event of a bank holding company's bankruptcy, the bankruptcy trustee will assume any commitment by the holding company to a federal bank regulatory agency to maintain the capital of a subsidiary bank. Moreover, the bankruptcy law provides that claims based on any such commitment will be entitled to a priority of payment over the claims of the institution's general unsecured creditors, including the holders of its note obligations. Thus, any borrowing that must be done by the holding company in order to make the required capital injection becomes more difficult and expensive and may adversely impact the holding company's results of operations and cash flows.

Common Stock Marketability Risk

Our authorized preferred stock exposes holders of our common stock to certain risks.

Our Articles of Incorporation authorize the issuance of up to 10,000,000 shares of preferred stock, par value \$1.00 per share. The authorized but unissued preferred stock constitutes what is commonly referred to as "blank check" preferred stock. This type of preferred stock may be issued by us, at the direction of our Board, from time to time on any number of occasions, without shareholder approval, as one or more separate series of shares comprised of any number of the authorized but unissued shares of preferred stock, designated by resolution of the Board stating (i) the dividend rate or the amount of dividends to be paid thereon, whether dividends shall be cumulative and, if so, from which date(s), the payment date(s) for dividends, and the participating or other special rights, if any, with respect to dividends; (ii) the voting powers, full or limited, if any, of shares of such series; (iii) whether the shares of such series shall be redeemable and, if so, the price(s) at which, and the terms and conditions on which, such shares may be redeemed; (iv) the amount(s) payable upon the shares of such series in the event of voluntary or involuntary liquidation, dissolution or winding up of the Company; (v) whether the shares of such series shall be entitled to the benefit of a sinking or retirement fund to be applied to the purchase or redemption of such shares, and if so entitled, the amount of such fund and the manner of its application, including the price or prices at which such shares may be redeemed or purchased through the application of such funds; (vi) whether the shares of such series shall be convertible into, or exchangeable for, shares of any other class or classes of stock of the Company, and, if so, the

conversion price(s), or the rate(s) of exchange, and the adjustments thereof, if any, at which such conversion or exchange may be made, and any other terms and conditions of such conversion and exchange; (vii) the price or other consideration for which the shares of such series shall be issued; (viii) whether the shares of such series which are redeemed or converted shall have the status of authorized but unissued shares of serial preferred stock and whether such shares may be reissued as shares of the same or any other series of serial preferred stock; and (ix) whether the shares of such series shall be entitled to other rights, preferences and privileges. Such preferred stock may provide our Board the ability to hinder or discourage any attempt to gain control of us by a merger, tender offer at a control premium price, proxy contest or otherwise. Consequently, the preferred stock could entrench our management. The market price of our common stock could be depressed to some extent by the existence of the preferred stock. Moreover, any preferred stock that is issued will rank ahead, in terms of dividends, priority and liquidation preferences and may have greater voting rights than our Company's common stock. No shares of preferred stock have been issued as of December 31, 2007.

Our directors and executive officers own a significant portion of our common stock.

As of December 31, 2007, our directors and executive officers, collectively, beneficially owned approximately 20% of our outstanding common stock. As a result of their ownership, the directors and executive officers, as a group, have the ability to significantly influence the outcome of all matters submitted to our shareholders for approval, including the election of directors and the approval of mergers and other significant corporate transactions, even if their interests conflict with those of other shareholders, which could adversely affect the market price of our common stock.

The OCC, OTS or the GDBF may impose dividend payment and other restrictions on the Subsidiary Banks which would impact our ability to pay dividends to shareholders. Dividends from Harbourside are not anticipated for the foreseeable future.

The OCC, OTS and the GDBF are the primary regulatory agencies that examine the Subsidiary Banks. Under certain circumstances, including any determination that the activities of a bank or their subsidiaries constitute unsafe and unsound banking practices, the regulators have the authority by statute to restrict the Subsidiary Banks' ability to transfer assets, make shareholder distributions, and redeem preferred securities or pay dividends to the parent company.

Certain provisions in our Articles of Incorporation and Bylaws may deter potential acquirers and may depress our stock price.

Our Articles of Incorporation and Bylaws divide our Board into three classes, as nearly equal as possible, with staggered three-year terms. Business combinations, such as sales or mergers involving us, require the approval of a majority of shareholders as well as the recommendation for such business combination by at least two-thirds of the continuing directors, or in the alternative, unanimously recommended by the continuing directors, provided that the continuing directors constitute at least three members of the Board at the time of such approval. Shareholders may remove directors with or without cause upon the affirmative vote of the holders of at least 75% of the outstanding voting shares of the Company and the affirmative vote of the holders of at least 75% of the outstanding voting shares of the Company other than those of which an interested shareholder is the beneficial owner. These provisions could make it more difficult for a third party to acquire control of the Company. In addition, the above provisions may be altered only pursuant to specified shareholder action. With several specific exceptions, our Articles of Incorporation and Bylaws are silent with respect to the amendment of our Articles of Incorporation, and thus, the Georgia Business Corporations Code ("GBCC") dictates the requirements for making such an amendment. The GBCC generally provides that, other than in the case of certain routine amendments (such as changing the corporate name) and other amendments which the GBCC specifically allows without shareholder action, the corporation's board of directors must recommend any amendment of the Articles of Incorporation to the shareholders (unless the board elects to make no such recommendation because of a conflict of interest or other special circumstances and the board communicates the reasons for its election to the shareholders) and the affirmative vote of a majority of the votes entitled to be cast on the amendment by each voting group entitled to vote on the amendment (unless the GBCC, the articles of incorporation, or the board of directors require a greater percentage of votes) is required to amend our Articles of Incorporation.

Our Articles of Incorporation provide that the provisions regarding the approval required for certain business combinations may only be changed by the affirmative vote of at least 75% of the outstanding voting shares of the Company and the affirmative vote of the holders of at least 75% of the outstanding shares of the Company other than those of which an interested shareholder is the beneficial owner. Our Articles of Incorporation also provide that the provisions regarding the applicability of Article 11, Parts 2 and 3 of the GBCC (regarding mergers and share exchanges) to the Company may only be repealed by both the affirmative vote of at least two-thirds of the continuing directors and a majority of the votes entitled to be cast by voting shares of the Company, in addition to any other vote required by our Articles of Incorporation.

Our Bylaws generally provide that the Bylaws may be altered or amended by our shareholders at any annual meeting or special meeting of the shareholders or by our Board at any regular or special meeting of the Company's Board.

The existence of the above provisions could result in our being less attractive to a potential acquirer, or result in our shareholders receiving less for their shares of common voting stock than otherwise might be available if there were a takeover attempt.

We have certain obligations and the general ability to issue additional shares of our common stock in the future, and such future issuances may depress the price of our common stock.

We have various obligations to issue additional shares of common stock in the future. These obligations include non-qualified and incentive stock options as detailed in Note 12 on page F-20 to the Consolidated Financial Statements in the 2007 Annual Report.

The options permit the holders to purchase shares of our common stock at specified prices. These purchase prices may be less than the then current market price of our common stock. Any shares of our common stock issued pursuant to these options would dilute the percentage ownership of existing shareholders. The terms on which we could obtain additional capital during the life of these options may be adversely affected because of such potential dilution. Finally, we may issue additional shares in the future. There are no preemptive rights in connection with our common stock. Thus, the percentage ownership of existing shareholders may be diluted if we issue additional shares in the future. For issuances of shares and grants of options, our Board will determine the timing and size of the issuances and grants and the consideration or services required thereof. Our Board intends to use its reasonable business judgment to fulfill its fiduciary obligations to our then existing shareholders in connection with any such issuance or grant. Nonetheless, future issuances of additional shares could cause immediate and substantial dilution to the net tangible book value of shares of our common stock issued and outstanding immediately before such transaction. Any future decrease in the net tangible book value of such issued and outstanding shares could materially and adversely affect the market value of the shares.

Sales of large quantities of our common stock could reduce the market price of our common stock.

Any sales of large quantities of shares of our common stock, or the perception that any such sales are likely to occur, could reduce the market price of our common stock. In 2005, we issued 397,273 restricted shares to investors in a private placement of our shares which were registered with the SEC on October 21, 2005. When the registration statement covering the resale of those restricted shares became effective, the holders of those shares are able to offer to sell those shares from time to time at the current market price or at negotiated prices. In 2007, we issued 71,000 shares related to the acquisition of Minis. If holders sell large quantities of shares of our common stock, the market price of our common stock may decrease and the public market for our common stock may otherwise be adversely affected because of the additional shares available in the market.

Our common stock has experienced only limited trading.

Our common stock is quoted and traded on the NASDAQ Global Market in the United States under the symbol "SAVB". The trading volume in our common stock has been relatively low when compared with larger companies quoted on the NASDAQ Global Market or listed on the other stock exchanges. We cannot say with any certainty that a more active and liquid trading market for our common stock will develop. Because of this, it may be more difficult for you to sell a substantial number of shares for the same price at which you could sell a smaller number of shares.

We cannot predict the effect, if any, that future sales of our common stock in the market, or the availability of shares of common stock for sale in the market, will have on the market price of our common stock. We, therefore, can give no assurance that sales of substantial amounts of our common stock in the market, or the potential for large amounts of sales in the market, would not cause the market price of our common stock to decline or impair our future ability to raise capital through sales of our common stock. As of December 31, 2007, there were 5,923,797 shares of common stock outstanding. The price of our common stock will be determined in the marketplace and may be influenced by many factors, including the following:

- The depth and liquidity of the markets for our common stock;
- Investor perception of us and the industry in which we participate;
- General economic and market conditions;
- Responses to quarter-to-quarter variations in operating results;
- Earnings relative to securities analysts' estimates;
- Changes in financial estimates by securities analysts;
- Conditions, trends or announcements in the banking industry;
- Announcements of significant acquisitions, strategic alliances, joint ventures or capital commitments by us or our competitors;
- Additions or departures of key personnel;
- Accounting pronouncements or changes in accounting rules that affect our financial statements; and,
- Other factors and events beyond our control.

The market price of our common stock could experience significant fluctuations unrelated to our operating performance. As a result, an investor (due to personal circumstances) may be required to sell their shares of our common stock at a time when our stock price is depressed due to random fluctuations, possibly based on factors beyond our control.

Item 1B. Unresolved Staff Comments

None

Item 2. Properties

See Note 6 and Note 14 of Notes to Consolidated Financial Statements on page F-16 and page F-21 of the Registrant's 2007 Annual Report, which is specifically incorporated herein by reference.

Savannah's main office is located at 25 Bull Street, Savannah, Georgia, on the ground floor and lower level of a seven story office building located on Johnson Square in downtown Savannah. Savannah has leased approximately 4,700 square feet on the main floor and 2,000 square feet on the lower level of the building. In November 1998, an additional 1,475 square feet of space on the sixth floor was added to the lease. An additional 600 square feet was added to the sixth floor lease in 2003 and approximately 2,500 additional square feet in December 2005. The leases expire in June 2009. The rental costs increase by two percent of the gross rental amount each year during the current five-year term. The Company is also responsible for its pro rata share of operating cost increases in utilities, janitorial services, property taxes and insurance. In September 2005, SAVB Properties LLC, a nonconsolidated subsidiary of the Company, acquired a 50 percent interest in Johnson Square Associates, LLP ("JSA"), which owns the 25 Bull Street property. SAVB Properties LLC also acquired a 50 percent interest in Whitaker Street Associates, which owns the adjacent parking lot on which an underground parking deck is being constructed.

In 1989, Bryan Bank constructed its 8,500 square foot, two-story main office in Richmond Hill, Georgia, on land owned by Bryan Bank. The building has a walk-up ATM, a drive-up ATM and 4 drive-through lanes. All Bryan Bank personnel are housed in this location.

Savannah leases approximately 6,500 square feet on the first floor of a two-story building located at 400 Mall Boulevard, Savannah, Georgia. This space is used for a branch location and the mortgage and construction lending departments. The building is near the intersection of Mall Boulevard and Hodgson Memorial Drive, a location that is convenient to a significant concentration of commercial, service, and retail entities. The lease rate increases with

the Consumer Price Index. The initial lease term was for five years and ended March 31, 1997. Savannah committed to exercise the third five-year lease option in February 2007. There is one additional five-year renewal option included in the terms. Savannah is also responsible for its prorata share of increases in the cost of ad valorem taxes, insurance and maintenance of common areas. Savannah renovated the space, constructed a vault, and added a five lane drive-through teller facility adjacent to the building.

During 1995, Savannah entered into a five-year ground lease with seven five-year renewal options on land located at 100 Chatham Parkway. Savannah also has a right of first refusal to buy the property at appraised value should the owner ever decide to sell the property. The location is at the intersection of Chatham Parkway and U.S. Highway 80, a major commercial and industrial intersection in west Chatham County. Savannah made land improvements and constructed a 2,200 square-foot banking facility including four drive-through lanes and an ATM drive-through lane. The West Chatham Office opened for business on November 20, 1995.

In 1997, Savannah constructed a 2,300 square foot office on an out lot owned in the Island Towne Centre Shopping Plaza on Whitmarsh Island, six miles east of downtown Savannah. This office includes a four lane drive-through facility.

In November 1997, Savannah entered into a ten-year lease beginning June 1, 1998 with four five-year renewal options in the Medical Arts Shopping Center at 4809 Waters Avenue. The property consists of 3,055 square feet of banking office space and a separate drive-through facility behind the shopping center.

In March 2002, Savannah entered into a lease agreement, effective May 1, 2002, for approximately 5,000 square feet of office space at 450 Mall Boulevard, adjacent to the existing branch office at 400 Mall Boulevard. The Company is currently operating under a month to month lease while a new operations center and Bryan Bank banking office are constructed in Richmond Hill. The new building is expected to be complete in 2008.

On February 24, 2006, Harbourside entered into a lease agreement, effective March 1, 2006, for approximately 17,400 square feet of office space at 852 William Hilton Parkway on Hilton Head Island. The lease is on a new building for a 20-year initial lease term with three five-year renewal options. Harbourside's main banking office is located on the ground floor. The mortgage banking and other offices are located on the second floor. The lease is accounted for as an operating lease. The tenant is responsible for all taxes, insurance and maintenance. After five years, the rent will adjust annually by an amount that approximates the increase in the Consumer Price Index.

On August 1, 2006, Savannah entered into a lease agreement for approximately 1,200 square feet of banking office space in The Village, a shopping center on Skidaway Island. The initial term of the lease is for five years and includes two five-year renewal options. The rent will adjust annually by an amount that approximates the increase in the Consumer Price Index. Savannah is also responsible for its prorata share of increases in the cost of ad valorem taxes, insurance and maintenance of common areas.

On January 31, 2007, Harbourside entered into a lease agreement, effective October 1, 2007, for approximately 4,500 square feet of office space on Bluffton Parkway in Bluffton, South Carolina. The lease is on a new building for a 10-year initial lease term with three five-year renewal options. The tenant is responsible for all taxes, insurance and maintenance. After three years the rent will adjust three percent.

Bryan Bank entered into a contract in 2007 to acquire a lot for a future branch site in a commercial development on Highway 144 in Richmond Hill.

Item 3. Legal Proceedings

The Company is not a party to, nor is any of its property the subject of, any material pending legal proceedings incidental to the business of the Company or the Subsidiary Banks.

Item 4. Submission of Matters to a Vote of Security Holders

None

PART II

Item 5. Market for Registrant's Common Equity and Related Shareholder Matters

Incorporated herein by reference to sections entitled "Table 4 - Market for Registrant's Common Equity and Related Shareholder Matters" on page F-28 of the Financial Statement Section of the 2007 Annual Report.

Item 6. Selected Financial Data

Incorporated herein by reference to sections entitled "Table 1– Selected Financial Condition Highlights – Five-Year Comparison," "Table 2 – Selected Operating Highlights – Five-Year Comparison," "Table 3 – Selected Quarterly Data," "Table 6 – Loan Concentrations," "Table 8 – Average Balance Sheet and Rate/Volume Analysis-2007 and 2006" and "Table 9 – Average Balance Sheet and Rate/Volume Analysis-2006 and 2005" in the Registrant's MD&A on pages F-26 through F-42 of the Financial Statement Section of the 2007 Annual Report. Additional selected financial data is included on pages 15 and 16 of this Annual Report on Form 10-K.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The MD&A on pages F-26 through F-42 of the Financial Statement Section of the 2007 Annual Report are incorporated herein by reference.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk

Incorporated herein by reference to the sections entitled "Liquidity and Interest Rate Sensitivity Management" and "Table 7 – Cash Flow/Maturity Gap and Repricing Data" in the Registrant's MD&A on pages F-37, F-38 and F-40 of the Financial Statement Section of the 2007 Annual Report.

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Item 8. Financial Statements and Supplementary Data

(a)

1. Financial Statements -- See listing in Item 15
2. Financial Statement Schedules -- See Item 15

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None

Item 9A. Controls and Procedures

Evaluation of Disclosure Controls and Procedures - We have evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this Annual Report on Form 10-K as required by Rule 13a-15 of the Securities Exchange Act of 1934, as amended. This evaluation was carried out under the supervision and with the participation of our management, including our chief executive officer and chief financial officer. Based on this evaluation, the chief executive officer and chief financial officer have concluded that our disclosure controls and procedures are effective in timely alerting them to material information relating to the Company required to be included in our periodic SEC filings.

Management's Report on Internal Control over Financial Reporting and Report of Independent Registered Public Accounting Firm. - Our management is responsible for establishing and maintaining adequate internal control over financial reporting for the Company. Internal control over financial reporting is a process to provide reasonable assurance regarding the reliability of our financial reporting for external purposes in accordance with accounting principles generally accepted in the United States of America. Internal control over financial reporting includes maintaining records that in reasonable detail accurately and fairly reflect our transactions; providing reasonable assurance that transactions are recorded as necessary for preparation of our financial statements; providing reasonable assurance that receipts and expenditures of Company assets are made in accordance with management authorization; and providing reasonable assurance that unauthorized acquisition, use or disposition of Company assets that could have a material effect on our financial statements would be prevented or detected in a timely manner. Because of its inherent limitations, internal control over financial reporting is not intended to provide absolute assurance that a misstatement of our financial statements would be prevented or detected.

Management conducted an evaluation of the effectiveness of our internal control over financial reporting based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, management concluded that the Company's internal control over financial reporting was effective as of December 31, 2007. Mauldin & Jenkins, LLC has audited the effectiveness of our internal control over financial reporting and their report is included below.

Changes in Internal Control over Financial Reporting - No change in our internal control over financial reporting occurred during the fourth fiscal quarter covered by this Annual Report on Form 10-K that materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

SAVB 2007 Form 10-K

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders
The Savannah Bancorp, Inc.:

We have audited The Savannah Bancorp Inc. and Subsidiaries' (the "Company") internal control over financial reporting as of December 31, 2007, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying "Management's Report on Internal Control over Financial Reporting" included in item 9A. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, The Savannah Bancorp, Inc. and Subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2007, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of The Savannah Bancorp, Inc. and Subsidiaries as of December 31, 2007 and the related consolidated statements of income, comprehensive income, stockholders' equity and cash flows for the period ended December 31, 2007 and our report dated March 10, 2008 expressed an unqualified opinion.

/s/ Mauldin & Jenkins, LLC

Albany, Georgia
March 10, 2008

Item 9B. Other Information

None

PART III**Item 10. Directors, Executive Officers and Corporate Governance**

Incorporated herein by reference to the sections entitled "Election of Directors," "Information about the Board of Directors and Certain Committees" and "Executive Compensation and Benefits" in the Registrant's Proxy Statement dated March 24, 2008 and filed on March 17, 2008. All transactions required pursuant to the insider trading regulations were filed on either Form 4 or Form 5 of the SEC. The required Code of Ethics disclosures are also incorporated by reference to the section entitled "Code of Business Conduct and Ethics" in the Registrant's Proxy Statement dated March 24, 2008.

Item 11. Executive Compensation

Incorporated herein by reference to the sections entitled "Information about the Board of Directors and Certain Committees" under the caption "Compensation Committee" and "Executive Compensation and Benefits" in the Registrant's Proxy Statement dated March 24, 2008 and filed on March 17, 2008.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Shareholder Matters

Incorporated herein by reference to the sections entitled "Election of Directors" and "Ownership of Equity Securities" in the Registrant's Proxy Statement dated March 24, 2008 and filed on March 17, 2008.

Item 13. Certain Relationships and Related Transactions

Incorporated by reference, the information contained in Note 5 to the Consolidated Financial Statements and under the caption "Certain Transactions" in the Registrant's Proxy Statement dated March 24, 2008 and filed on March 17, 2008.

Item 14. Principal Accountant Fees and Services

Incorporated herein by reference to the information under the caption entitled "Principal Accountant Fees and Services" in the Registrant's Proxy Statement dated March 24, 2008 and filed on March 17, 2008.

PART IV

Item 15. Exhibits and Financial Statement Schedules

(a) The following documents are filed as part of this report:

1. Financial statements

Incorporated herein by reference to the financial statements, together with the applicable report of independent accountants, are included on pages F-2 through F-25 of the Financial Statement Section of the 2007 Annual Report. The index for the financial statements is as follows:

| <u>Financial Statement</u> | <u>Page</u> |
|--|-------------|
| (i) Report of Independent Registered Public Accounting Firm | F-2 |
| (ii) Report of Independent Registered Public Accounting Firm | F-3 |
| (iii) Consolidated Balance Sheets December 31, 2007 and 2006 | F-4 |
| (iv) Consolidated Statements of Income for the Years Ended December 31, 2007, 2006 and 2005 | F-5 |
| (v) Consolidated Statements of Changes in Shareholders' Equity for the Years Ended December 31, 2007, 2006 and 2005 | F-6 |
| (vi) Consolidated Statements of Cash Flows for the Years Ended December 31, 2007, 2006 and 2005 | F-7 |
| (vii) Notes to Consolidated Financial Statements | F-8 to F-25 |

2. Required financial statement schedules

Other schedules and exhibits are not required information or are inapplicable and, therefore, have been omitted.

3. The exhibits listed in the accompanying index to exhibits are filed or incorporated by reference as part of this Annual Report on Form 10-K.

Index to Exhibits

Exhibit

| <u>Number</u> | <u>Description</u> |
|---------------|--|
| 3.1 * | Articles of Incorporation |
| 3.2 * | By-laws as amended |
| 10.1 * | Lease for Bank Site at 25 Bull Street and Assumption of Lease |
| 10.5 * | Form of Organizers' Stock Option Agreement |
| 10.6 * | Lease for Mall Boulevard Office dated February 14, 1992 |
| 10.7 | The Savannah Bancorp, Inc. Incentive Stock Option Plan approved by shareholders on April 18, 1995 |
| 10.8 | Amendment to The Savannah Bancorp, Inc. Incentive Stock Option Plan approved by shareholders on April 16, 1996. |
| 10.9 * | The Savannah Bancorp, Inc. 2005 Omnibus Stock Ownership and Long Term Incentive Plan approved by shareholders on April 21, 2005. |
| 10.10 * | Lease for Harbourside Community Bank main office dated February 24, 2006. |
| 11 | Computation of Earnings Per Share ** ** Data required by Statement of Financial Accounting Standards No. 128, "Earnings per Share," is provided in Note 1 to the consolidated financial statements in the 2007 Annual Report. |
| 13 | 2007 Annual Report to Shareholders |
| 21 | Subsidiaries of Registrant |
| 22 | Proxy Statement for Annual Meeting - filed in DEF 14A on March 17, 2008 |
| 23.1 | Consent of Mauldin & Jenkins, LLC, Independent Registered Public Accounting Firm |
| 23.2 | Consent of BDO Seidman, LLP, Independent Registered Public Accounting Firm |
| 31.1 | Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 31.2 | Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 32 | Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |

*Items 3.1, 3.2, 10.1 and 10.5 were previously filed by the Company as Exhibits (with the same respective Exhibit Numbers as indicated herein) to the Company's Registration Statement (Registration No. 33-33405) filed in February 1990 and such documents are incorporated herein by reference.

Item 10.6 was filed as an exhibit with the 1992 Annual Report on Form 10-K in March 1993.

Item 10.9 was filed as an exhibit with the DEF 14A on March 25, 2005.

Item 10.10 was filed as an exhibit with the Form 8-K filed on March 3, 2006.

Signature Page

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on March 11-13, 2008 by the undersigned, thereunto duly authorized.

THE SAVANNAH BANCORP, INC.

/s/ JOHN C. HELMKEN II

John C. Helmken II
President and Chief Executive Officer
(Principal Executive Officer)

/s/ ROBERT B. BRISCOE

Robert B. Briscoe
Chief Financial Officer
(Principal Financial and Accounting Officer)

Directors:

/s/ J. WILEY ELLIS

J. Wiley Ellis
Chairman of the Board

/s/ JOHN C. HELMKEN II

John C. Helmken II

/s/ JAMES W. ROYAL, SR.

James W. Royal, Sr.

/s/ E. JAMES BURNSED

E. James Burnsed
Vice Chairman

/s/ CHARLES E. IZLAR

Charles E. Izlar

/s/ ROBERT T. THOMPSON, JR.

Robert T. Thompson, Jr.

/s/ RUSSELL W. CARPENTER

Russell W. Carpenter

/s/ AARON M. LEVY

Aaron M. Levy

/s/ ROBERT H. DEMERE, JR.

Robert H. Demere, Jr.

/s/ J. CURTIS LEWIS III

J. Curtis Lewis III

/s/ BERRYMAN W. EDWARDS

Berryman W. Edwards

/s/ M. LANE MORRISON

M. Lane Morrison

/s/ L. CARLTON GILL

L. Carlton Gill

/s/ J. TOBY ROBERTS, SR.

J. Toby Roberts, Sr.

THE SAVANNAH BANCORP, INC. AND SUBSIDIARIES
FINANCIAL STATEMENT SECTION
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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders
of The Savannah Bancorp, Inc.:

We have audited the accompanying consolidated balance sheet of The Savannah Bancorp, Inc. and its subsidiaries as of December 31, 2007, and the related consolidated statements of income, changes in shareholders' equity and cash flows for the year ended December 31, 2007. These consolidated financial statements are the responsibility of The Savannah Bancorp, Inc.'s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. Our audit of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of The Savannah Bancorp, Inc. and its subsidiaries as of December 31, 2007, and the results of its operations and its cash flows for the year ended December 31, 2007 in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of The Savannah Bancorp, Inc. and its subsidiaries' internal control over financial reporting as of December 31, 2007, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 10, 2008 expressed an unqualified opinion.

/s/ Mauldin & Jenkins, LLC

Albany, Georgia
March 10, 2008

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders
of The Savannah Bancorp, Inc.:

We have audited the accompanying consolidated balance sheet of The Savannah Bancorp, Inc. and its subsidiaries as of December 31, 2006 and the related consolidated statements of income, changes in shareholders' equity and cash flows for each of the two years in the period ended December 31, 2006. These consolidated financial statements are the responsibility of The Savannah Bancorp, Inc.'s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of The Savannah Bancorp, Inc. and its subsidiaries as of December 31, 2006, and the results of its operations and its cash flows for each of the two years in the period ended December 31, 2006 in conformity with accounting principles generally accepted in the United States of America.

/s/ BDO Seidman, LLP

Atlanta, Georgia
March 8, 2007

THE SAVANNAH BANCORP, INC. AND SUBSIDIARIES
Consolidated Balance Sheets
(\$ in thousands, except share data)

| | December 31, | |
|---|---------------------|-------------------|
| | 2007 | 2006 |
| Assets | | |
| Cash and due from banks | \$ 12,721 | \$ 18,540 |
| Federal funds sold | 4,435 | 18,363 |
| Interest-bearing deposits in banks | 20,148 | 10,394 |
| Cash and cash equivalents | 37,304 | 47,297 |
| Securities available for sale, at fair value (amortized cost of \$60,241 and \$54,163 in 2007 and 2006) | 61,057 | 53,917 |
| Loans held for sale | 180 | 914 |
| Loans, net of allowance for loan losses of \$12,864 and \$8,954 in 2007 and 2006 | 795,787 | 711,964 |
| Premises and equipment, net | 6,830 | 6,365 |
| Other real estate owned | 2,112 | 545 |
| Bank-owned life insurance | 5,985 | 5,760 |
| Goodwill and other intangibles, net | 2,806 | - |
| Other assets | 20,398 | 16,752 |
| Total assets | \$ 932,459 | \$ 843,514 |
| Liabilities | | |
| Deposits: | | |
| Noninterest-bearing | \$ 88,503 | \$ 101,156 |
| Interest-bearing demand | 127,902 | 116,493 |
| Savings | 16,168 | 18,615 |
| Money market | 176,615 | 147,279 |
| Time deposits | 355,030 | 323,281 |
| Total deposits | 764,218 | 706,824 |
| Short-term borrowings | 70,599 | 40,687 |
| Federal Home Loan Bank advances – long-term | 2,973 | 13,309 |
| Subordinated debt to nonconsolidated subsidiaries | 10,310 | 10,310 |
| Other liabilities | 8,087 | 5,810 |
| Total liabilities | 856,187 | 776,940 |
| Commitments and contingencies (Notes 14 and 17) | | |
| Shareholders' equity | | |
| Preferred stock, par value \$1 per share: | | |
| authorized 10,000,000 shares, none issued | - | - |
| Common stock, par value \$1 per share: authorized 20,000,000 shares; issued 5,923,797 and 5,781,381 shares in 2007 and 2006 | 5,924 | 5,781 |
| Additional paid-in capital | 38,279 | 35,747 |
| Retained earnings | 30,512 | 25,681 |
| Treasury stock, 318 shares in 2007 and 2006 | (4) | (4) |
| Accumulated other comprehensive income (loss), net | 1,561 | (631) |
| Total shareholders' equity | 76,272 | 66,574 |
| Total liabilities and shareholders' equity | \$ 932,459 | \$ 843,514 |

The accompanying notes are an integral part of these consolidated financial statements.

THE SAVANNAH BANCORP, INC. AND SUBSIDIARIES
Consolidated Statements of Income
(\$ in thousands, except per share data)

| | For the Years Ended December 31, | | |
|---|---|------------------|-----------------|
| | 2007 | 2006 | 2005 |
| Interest and dividend income | | | |
| Loans, including fees | \$ 59,435 | \$ 51,541 | \$ 38,503 |
| Loans held for sale | 98 | 558 | 1,335 |
| Investment securities: | | | |
| Taxable | 2,594 | 1,912 | 1,325 |
| Tax-exempt | 95 | 123 | 218 |
| Dividends | 218 | 205 | 128 |
| Deposits with banks | 346 | 293 | 473 |
| Federal funds sold | 472 | 557 | 376 |
| Total interest and dividend income | 63,258 | 55,189 | 42,358 |
| Interest expense | | | |
| Deposits | 26,415 | 19,342 | 12,373 |
| Short-term borrowings | 2,612 | 1,802 | 675 |
| Federal Home Loan Bank advances | 413 | 778 | 1,009 |
| Subordinated debt | 842 | 815 | 622 |
| Total interest expense | 30,282 | 22,737 | 14,679 |
| Net interest income | 32,976 | 32,452 | 27,679 |
| Provision for loan losses | 4,675 | 1,585 | 1,500 |
| Net interest income after provision for loan losses | 28,301 | 30,867 | 26,179 |
| Noninterest income | | | |
| Service charges on deposit accounts | 1,383 | 1,526 | 1,622 |
| Mortgage related income, net | 615 | 886 | 1,292 |
| Trust and asset management fees | 1,513 | 658 | 501 |
| Other operating income | 1,242 | 1,233 | 979 |
| Losses on sales of other real estate owned | (44) | - | (7) |
| Total noninterest income | 4,709 | 4,303 | 4,387 |
| Noninterest expense | | | |
| Salaries and employee benefits | 11,846 | 10,852 | 9,530 |
| Occupancy and equipment | 3,294 | 2,920 | 2,199 |
| Information technology | 1,616 | 1,525 | 1,244 |
| Other operating expense | 4,383 | 4,656 | 3,673 |
| Total noninterest expense | 21,139 | 19,953 | 16,646 |
| Income before income taxes | 11,871 | 15,217 | 13,920 |
| Income tax expense | 4,235 | 5,215 | 4,880 |
| Net income | \$ 7,636 | \$ 10,002 | \$ 9,040 |
| Net income per share: (a) | | | |
| Basic | \$ 1.31 | \$ 1.73 | \$ 1.68 |
| Diluted | \$ 1.29 | \$ 1.70 | \$ 1.63 |
| Dividends per share | \$ 0.48 | \$ 0.45 | \$ 0.43 |
| Average basic shares (000s) | 5,850 | 5,765 | 5,396 |
| Average diluted shares (000s) | 5,922 | 5,876 | 5,531 |

(a) Share and per share amounts have been restated to reflect the effect of a 5-for-4 stock split in December 2006.

The accompanying notes are an integral part of these consolidated financial statements.

THE SAVANNAH BANCORP, INC. AND SUBSIDIARIES
Consolidated Statements of Changes in Shareholders' Equity
(\$ in thousands, except share data)

| | For the Years Ended December 31, | | |
|--|---|------------------|------------------|
| | 2007 | 2006 | 2005 |
| Common shares issued | | | |
| Shares, beginning of year | 5,781,381 | 4,591,339 | 4,112,448 |
| Common stock issued | 78,000 | - | 397,273 |
| Stock split / dividend | - | 1,155,564 | - |
| Exercise of options | 64,416 | 34,478 | 81,618 |
| Shares, end of year | 5,923,797 | 5,781,381 | 4,591,339 |
| Treasury shares owned | | | |
| Shares, beginning of year | 318 | 267 | 282 |
| Stock split / dividend or issuance | - | 63 | (15) |
| Stock options exercised | - | (12) | - |
| Shares, end of year | 318 | 318 | 267 |
| Common stock | | | |
| Balance, beginning of year | \$ 5,781 | \$ 4,591 | \$ 4,112 |
| Common stock issued | 78 | - | 397 |
| Stock split / dividend | - | 1,156 | - |
| Stock options exercised | 65 | 34 | 82 |
| Balance, end of year | 5,924 | 5,781 | 4,591 |
| Additional paid-in capital | | | |
| Balance, beginning of year | 35,747 | 36,257 | 24,232 |
| Common stock issued, net of issuance costs | 1,702 | - | 11,191 |
| Stock split / dividend | - | (1,156) | - |
| Stock-based compensation expense, net | 147 | 191 | - |
| Stock options exercised | 683 | 272 | 494 |
| Tax benefit of option exercises and expense | - | 183 | 340 |
| Balance, end of year | 38,279 | 35,747 | 36,257 |
| Retained earnings | | | |
| Balance, beginning of year | 25,681 | 18,272 | 11,539 |
| Net income | 7,636 | 10,002 | 9,040 |
| Dividends paid | (2,805) | (2,593) | (2,307) |
| Balance, end of year | 30,512 | 25,681 | 18,272 |
| Treasury stock | | | |
| Balance, beginning of year | (4) | (4) | (4) |
| Stock options exercised | - | - | - |
| Balance, end of year | (4) | (4) | (4) |
| Accumulated other comprehensive income (loss), net | | | |
| Balance, beginning of year | (631) | (573) | 192 |
| Change in unrealized gains (losses) on securities available for sale, net of tax | 662 | 178 | (522) |
| Change in fair value of derivative instruments, net of tax | 1,530 | (236) | (243) |
| Balance, end of year | 1,561 | (631) | (573) |
| Total shareholders' equity | \$ 76,272 | \$ 66,574 | \$ 58,543 |

The accompanying notes are an integral part of these consolidated financial statements.

See Note 1 for other comprehensive income disclosures.

THE SAVANNAH BANCORP, INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows

| | For the Years Ended December 31, | | |
|--|---|---------------|----------------|
| (\$ in thousands) | 2007 | 2006 | 2005 |
| Operating activities | | | |
| Net income | \$ 7,636 | \$ 10,002 | \$ 9,040 |
| Adjustments to reconcile net income to cash | | | |
| provided by operating activities: | | | |
| Provision for loan losses | 4,675 | 1,585 | 1,500 |
| Loans originated for sale | (24,834) | (34,195) | (104,888) |
| Proceeds from sale of loans originated for sale | 25,715 | 44,067 | 111,824 |
| Net (accretion) amortization of securities | (122) | 29 | 102 |
| Depreciation and amortization | 1,070 | 976 | 809 |
| Net amortization of client list | 48 | - | - |
| Non cash stock-based compensation expense | 184 | 299 | - |
| Decrease in deferred income taxes, net | (677) | (728) | (860) |
| Gain on sale of loans, net | (147) | (313) | (760) |
| Losses on sales of foreclosed assets | 44 | - | 7 |
| Equity in net income of nonconsolidated subsidiary | (89) | (109) | - |
| Increase in CSV of bank-owned life insurance policies | (225) | (209) | (202) |
| Change in other assets and other liabilities, net | 3,232 | (5,281) | 1,995 |
| Net cash provided by operating activities | 16,510 | 16,123 | 18,567 |
| Investing activities | | | |
| Activity in available for sale securities | | | |
| Purchases | (29,356) | (20,380) | (19,396) |
| Maturities and calls | 23,400 | 11,161 | 15,518 |
| Loan originations and principal collections, net | (90,451) | (110,040) | (104,053) |
| Proceeds from sale of foreclosed assets | | 1,800 | 453 |
| | 342 | | |
| Investment in low income housing tax credits | (2,000) | - | (339) |
| Distribution from (investment in) nonconsolidated subsidiary | - | 1,300 | (2,709) |
| Purchase of consolidated subsidiary | (1,901) | - | - |
| Additions to premises and equipment | (1,450) | (2,376) | (1,044) |
| Net cash used in investing activities | (101,416) | (118,535) | (111,570) |
| Financing activities | | | |
| Net (decrease) increase in noninterest-bearing deposits | (12,653) | 8,074 | 9,292 |
| Net increase in interest-bearing deposits | 70,047 | 98,240 | 85,098 |
| Net increase (decrease) in short-term borrowings | | | |
| to repurchase and federal funds purchased | 29,912 | 20,785 | (15,167) |
| Net decrease in FHLB advances – long-term | (10,336) | (7,167) | (361) |
| Payment on note payable | - | (479) | (484) |
| Dividends paid | (2,805) | (2,593) | (2,307) |
| Issuance of common stock | - | - | 11,588 |
| Exercise of options | 748 | 381 | 916 |
| Net cash provided by financing activities | 74,913 | 117,241 | 88,575 |
| (Decrease) increase in cash and cash equivalents | (9,993) | 14,829 | (4,428) |
| Cash and cash equivalents, beginning of year | 47,297 | 32,468 | 36,896 |
| Cash and cash equivalents, end of year | \$ 37,304 | \$ 47,297 | \$ 32,468 |

Supplemental disclosures of cash flow information

Cash paid during the year for:

| | | | |
|--|-----------|-----------|-----------|
| Interest on deposits and other borrowings | \$ 29,865 | \$ 22,115 | \$ 14,199 |
| Income taxes | 5,560 | 6,038 | 4,559 |
| Non cash investing activity: | | | |
| Transfer to other real estate owned from loans | (1,953) | (2,735) | - |
| Increase (decrease) in unrealized gains/losses on investment securities available for sale, net of tax | 662 | 178 | (522) |
| Increase (decrease) in unrealized gains/losses on derivatives, net of tax | 1,530 | (236) | (243) |

The accompanying notes are an integral part of these consolidated financial statements.

Notes to Consolidated Financial Statements

Note 1 - Organization and Summary of Significant Accounting Policies

Principles of Consolidation - The consolidated financial statements include the accounts of The Savannah Bancorp, Inc. ("the Company") and its wholly-owned subsidiaries, The Savannah Bank, N.A. ("Savannah"), Bryan Bank & Trust ("Bryan"), Harbourside Community Bank ("Harbourside") and Minis & Co., Inc. ("Minis"), a registered investment advisory firm acquired on August 31, 2007. The three bank subsidiaries, together, are referred to as the "Subsidiary Banks". All significant intercompany balances and transactions have been eliminated in consolidation. Certain prior year balances have been reclassified to conform to the current year presentation.

Nature of Operations - The Company is a holding company that owns three banks and a registered investment advisory firm. Through the subsidiaries, the Company offers a full range of lending, deposit, residential mortgage origination, fiduciary, trust and investment advisory products. In the fourth quarter 2003, Savannah opened Harbourside Mortgage Company, a mortgage loan production office on Hilton Head Island, South Carolina. In March 2006, Harbourside assumed the operations of Harbourside Mortgage Company and commenced operations in its new leased headquarters facility. The primary service area of the Company is the city of Savannah, Georgia, surrounding Chatham County, Richmond Hill, Georgia (20 miles south of downtown Savannah) and Bryan County and Hilton Head Island, South Carolina and southern Beaufort County. In 2005, the Company formed a nonconsolidated subsidiary, SAVB Properties, LLC, which purchased a 50 percent interest in two real estate partnerships that own the Company's headquarters building and the adjacent parking lot. This investment is accounted for using the equity method of accounting. Minis was acquired on August 31, 2007 and additional information regarding the acquisition is included in Note 2.

Use of Estimates - In preparing consolidated financial statements in conformity with generally accepted accounting principles, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses and the evaluation of the realization of deferred tax assets.

Cash and Cash Equivalents - For purposes of the consolidated statements of cash flows, cash and cash equivalents include cash and balances due from banks, federal funds sold and interest-bearing deposits in banks, all of which mature within ninety days.

Investment Securities Available for Sale - Management has classified the entire investment securities portfolio as available for sale. Securities available for sale are carried at estimated fair value with unrealized gains and losses, net of deferred income taxes, recorded as a separate component of shareholders' equity. Purchase premiums and discounts are recognized in interest income using the interest method over the life of the securities. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

Loans Held For Sale - Loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated fair value in the aggregate. Net unrealized losses, if any, are recognized through a valuation allowance by charges to income. In estimating fair value, consideration is given to commitments from investors and prevailing market prices. Loan origination fees applicable to mortgage loans held for sale, net of certain direct origination costs, are deferred and recognized as an adjustment to the related gain or loss on subsequent sale of the loan.

Loans and Loan Fees - The Subsidiary Banks underwrite mortgage, commercial and consumer loans to customers. A substantial portion of the loan portfolio consists of real estate secured loans throughout the coastal Georgia and South Carolina areas. Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off are generally reported at their outstanding unpaid principal balances adjusted for charge-offs, the allowance for loan losses, and any deferred fees or origination costs. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the related loan yield on a straight-line basis, which approximates the interest method.

Notes to Consolidated Financial Statements

Note 1 - Organization and Summary of Significant Accounting Policies (continued)

The accrual of interest on mortgage and commercial loans is discontinued at the time the loan is 90 days past due unless the credit is well-secured and in process of collection. Revolving credit loans and other personal loans are typically charged-off when payments are 120 days past due. Past due status is based on the contractual terms of the loan. Loans are placed on nonaccrual status or charged-off at an earlier date if collection of principal or interest in full becomes doubtful.

All interest accrued in the current year but not collected for loans that are placed on nonaccrual status or charged-off is reversed against interest income. The interest on these loans is accounted for on the cash-basis or cost-recovery method until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Allowance for Loan Losses - The allowance for loan losses is based on estimates and maintained at a level considered adequate to provide for potential losses inherent in the portfolio based on the current environment. The adequacy of the allowance is based on management's continuing evaluation of the loan portfolio considering current economic conditions, underlying collateral value securing loans and other relevant qualitative and quantitative factors that deserve recognition in estimating loan losses. Actual future losses may be different from estimates due to unforeseen events. Loans that are determined to be uncollectible are charged-off against the allowance.

The adequacy of the allowance for loan losses is evaluated on a regular basis by management and reported quarterly to the Audit Committee of the Board of Directors ("Board"). The evaluation is based upon management's periodic review of the collectability of specific loans, adverse situations that may affect specific borrowers' ability to repay, the estimated value of any underlying collateral, the composition and size of the loan portfolio and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance consists of specific and general reserve components. The specific component relates to loans that are classified as doubtful or substandard. For such loans that are also classified as impaired, an allowance is established when the discounted cash flows (or value of related collateral or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers non-classified loans and is based on historical loss experience adjusted for qualitative factors.

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan by loan basis by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Premises and Equipment - Buildings, furniture, banking equipment and leasehold improvements are stated at cost less accumulated depreciation and amortization. Depreciation and amortization of these assets are computed using the straight-line method over the estimated useful lives or estimated lease terms including expected lease renewals, ranging from three to fifty years, of the respective assets for financial reporting purposes and accelerated methods for income tax purposes. Additions and major improvements are capitalized, while routine maintenance and repairs and gain or loss on dispositions are recognized currently.

Other Real Estate Owned - Assets acquired through loan foreclosure are held for sale and are initially recorded at fair value less estimated disposal costs at the date of foreclosure, 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 estimated disposal costs. Valuation allowances are established when subsequent valuations are less than

Notes to Consolidated Financial Statements

Note 1 - Organization and Summary of Significant Accounting Policies (continued)

current carrying amounts. Expenses from operations and changes in the valuation allowance and net expenses from holding these assets are included in noninterest expense.

Bank-Owned Life Insurance - Bank-owned life insurance policies are recorded at the net realizable value of the underlying insurance contracts. The change in contract value during the year represents the contract earnings during the period less the mortality costs and administrative costs of the underlying life insurance contracts. The increase in cash surrender value from bank-owned life insurance contracts is included as a component of other operating income and the mortality costs and administrative fees are recorded as noninterest expense.

Intangible Assets - Intangible assets include goodwill and other identifiable assets, such as customer lists, resulting from our acquisition of Minis. Customer list intangibles are amortized on a straight-line basis over an estimated useful life of seven to ten years and evaluated for impairment whenever events or changes in circumstances indicate the carrying amount of the assets may not be recoverable. Goodwill is not amortized but tested annually for impairment or at any time an event occurs or circumstances change that may trigger a decline in the value of the reporting unit. Examples of such events or circumstances include adverse change in operations, legal factors, business climate, unanticipated competition, change in regulatory environment, or loss of key personnel.

We will test for impairment in accordance with Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangible Assets" within twelve months of the September 1, 2007 acquisition date of Minis. Potential impairment of goodwill exists when the carrying amount of a reporting unit exceeds its fair value. The fair value for each reporting unit is computed using one or a combination of the following three methods: income, market value, or cost method. The income method uses a discounted cash flow analysis to determine fair value by considering a reporting unit's capital structure and applying a risk-adjusted discount rate to forecast earnings based on a capital asset pricing model. The market value method uses recent transaction analysis or publicly traded comparable analysis for similar assets and liabilities to determine fair value. The cost method assumes the net assets of a recent business combination accounted for under the purchase method of accounting will be recorded at fair value if no event or circumstance has occurred triggering a decline in the value. To the extent a reporting unit's carrying amount exceeds its fair value, an indication exists that the reporting unit's goodwill may be impaired, and a second step of impairment test will be performed. In the second step, the implied fair value of the reporting unit's goodwill, determined by allocating the reporting unit's fair value to all of its assets (recognized and unrecognized) and liabilities as if the reporting unit had been acquired in a business combination at the date of the impairment test. If the implied fair value of reporting unit goodwill is lower than its carrying amount, goodwill is impaired and is written down to the implied fair value. The loss recognized is limited to the carrying amount of goodwill. Once an impairment loss is recognized, future increases in fair value will not result in the reversal of previously recognized losses.

Income Taxes - Deferred income tax assets and liabilities are determined using the liability (or balance sheet) method. Deferred tax assets and liabilities arise from temporary differences between the carrying amounts of assets and liabilities for financial reporting and income tax purposes. They are reflected at currently enacted income tax rates applicable to the period in which the deferred tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through income tax expense.

Earnings Per Share - Basic earnings per share represent net income divided by the weighted average number of common shares outstanding during the period. Diluted earnings per share reflect additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to income that would result from the assumed issuance. Potential common shares that may be issued by the Company relate solely to outstanding stock options, and are determined using the treasury stock method. Earnings per common share have been computed based on the following:

| (amounts in thousands) | | | |
|---|-------|-------|-------|
| Years Ended December 31, | 2007 | 2006 | 2005 |
| Average number of common shares outstanding - basic | 5,850 | 5,765 | 5,396 |
| Effect of dilutive options | 72 | 111 | 135 |
| Average number of common shares outstanding - diluted | 5,922 | 5,876 | 5,531 |

Notes to Consolidated Financial Statements

Note 1 - Organization and Summary of Significant Accounting Policies (continued)

Stock option shares in the amount of 102,602 and 10,716 for the years ended 2007 and 2006 were excluded from the diluted earnings per share calculation due to their anti-dilutive effect. None were excluded in 2005. All share amounts have been restated to reflect the effect of a 5-for-4 stock split in December 2006.

Derivative Instruments and Hedging Activities - SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133"), as amended and interpreted, establishes accounting and reporting standards for derivatives and hedging activities. As required by SFAS 133, the Company records all derivatives at fair value on the balance sheet as either other assets or other liabilities. The Company uses derivative instruments including interest rate swaps, floors and collars as part of its overall asset and liability duration and interest rate risk management strategy. These instruments enable the Company to manage desired asset and liability duration and to reduce exposure to interest rate movements.

Other Comprehensive Income (Loss) - Comprehensive income (loss) is the change in the Company's equity during the period from transactions and other events and circumstances from non-owner sources.

| (\$ in thousands) | 2007 | 2006 | 2005 |
|--|----------|-----------|----------|
| Net income | \$ 7,636 | \$ 10,002 | \$ 9,040 |
| Change in unrealized gains (losses) on securities available for sale, net of tax | 662 | 178 | (522) |
| Change in fair value of derivative instruments, net of tax | 1,530 | (236) | (243) |
| Other comprehensive income | \$ 9,828 | \$ 9,944 | \$ 8,275 |

Accounting for Stock-Based Compensation - On January 1, 2006, the Company adopted the revised SFAS No. 123, "Share-Based Payment," ("SFAS 123R") using the modified prospective method. In accordance with SFAS 123R, the Company measures the cost of employee services received in exchange for an award of equity instruments based on the fair value of the award on the grant date. That cost is recognized over the period during which an employee is required to provide service in exchange for the award – the requisite service period. No compensation cost is recognized for equity instruments for which employees do not render the requisite service. The Company determines the fair value of employee stock options using the Black-Scholes option pricing model.

The 1995 Incentive Stock Option Plan ("1995 Plan") authorized the Company to issue both incentive and non-qualified stock options to certain key officers for the purchase of shares at the fair market value of the stock at the date of grant. In 2000, the shareholders authorized additional option shares under the 1995 Plan. All authorized shares have been awarded from the 1995 Plan.

In 2005, shareholders approved the 2005 Omnibus Stock Ownership and Long-Term Incentive Plan ("2005 Omnibus Plan") and authorized 250,000 option or restricted shares to be available for issuance. The total number of remaining options or awards available for issuance at December 31, 2007 under the 2005 Omnibus Plan was 158,121 shares of common stock. Options granted under both plans have a term of ten years and generally become fully vested over periods ranging from three to ten years. Performance based options granted to directors vest over three quarters from the date of grant.

In accordance with the modified prospective method, the Company's consolidated financial statements for periods prior to 2006 have not been restated to reflect, and do not include, the impact of SFAS 123R.

Notes to Consolidated Financial Statements

Note 1 - Organization and Summary of Significant Accounting Policies (continued)

The following table summarizes compensation costs related to the Company's stock-based compensation plans for the years ended December 31, 2007 and 2006:

| (\$ in thousands) | 2007 | 2006 |
|--|--------|--------|
| Salaries and employee benefits | \$ 143 | \$ 200 |
| Directors' stock-based compensation | 41 | 99 |
| Pre-tax stock-based compensation expense | 184 | 299 |
| Income tax benefit | (37) | (108) |
| Total stock-based compensation expense, net of tax | \$ 147 | \$ 191 |

In 2007 and 2006, the Company realized \$15,000 and \$48,000, respectively in income tax benefit associated with certain stock option exercises. Stock-based compensation expense, net of tax, for 2005 was \$151,000. Net income per diluted share would have been approximately \$0.03 less for 2005.

The Company recognizes stock-based compensation expense using the graded vesting attribution method. The remaining unrecognized compensation cost related to unvested incentive stock option and restricted share awards at December 31, 2007 is approximately \$285,000. The weighted-average period of time over which this cost will be recognized is approximately 2.9 years. This amount does not include the cost of any additional options that may be granted in future periods nor any reduction in cost for potential forfeitures.

The Company implemented an improved Black-Scholes methodology for calculating stock-based compensation in 2006. Certain assumptions in years prior to 2006 and amounts have been restated to conform to the current year methodology. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions. The values have been restated to reflect the effect of a 5-for-4 stock split in December 2006.

| | 2007 | 2006 | 2005 |
|--|-----------|-----------|-----------|
| Weighted average fair value of options granted | \$ 7.71 | \$ 8.89 | \$ 6.06 |
| Expected volatility | 28.6% | 27.7% | 29.0% |
| Dividend yield | 1.90% | 1.53% | 1.94% |
| Risk-free interest rate | 4.92% | 4.90% | 3.82% |
| Expected life | 6.0 years | 6.0 years | 6.0 years |

Risks and Uncertainties - In the normal course of its business, we encounter two significant types of risk: economic and regulatory. There are three main components of economic risk: interest rate risk, credit risk and market risk. We are subject to interest rate risk to the degree that our interest-bearing liabilities mature or reprice at different speeds, or on different indexes, than our interest-earning assets. Credit risk is the risk of default on our loan portfolio that results from borrowers' inability or unwillingness to make contractually required payments. Market risk reflects changes in the value of collateral underlying loans receivable, the valuation of real estate we hold, and the valuation of loans held for sale, investments and mortgage-backed securities available for sale and mortgage servicing rights.

We are subject to the regulations of various government agencies. These regulations can and do change significantly from period to period. We also undergo periodic examinations by the regulatory agencies, which may subject us to further changes with respect to asset valuations, amounts of required loss allowances and operating restrictions resulting from the regulators' judgments on information available to them at the time of their examination.

Notes to Consolidated Financial Statements

Note 1 - Organization and Summary of Significant Accounting Policies (continued)

Recent Accounting Pronouncements

On January 1, 2007, the Company adopted the Securities and Exchange Commission's ("SEC") Staff Accounting Bulletin No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements" ("SAB 108"). SAB 108 provides guidance on how the effects of prior year uncorrected financial statement misstatements should be considered in quantifying a current year misstatement. SAB 108 requires public companies to quantify misstatements using both an income statement (rollover) and balance sheet (iron curtain) approach and evaluate whether either approach results in a misstatement that, when all relevant quantitative and qualitative factors are considered, is material. If prior year errors that had been previously considered immaterial but now are considered material based on either approach, no restatement is required so long as management properly applied its previous approach and all relevant facts and circumstances were considered. Adjustments considered immaterial in prior years under the method previously used, but now considered material under the dual approach required by SAB 108, are to be recorded upon initial adoption of SAB 108. No adjustments were recorded upon the initial adoption of SAB 108 or during the current year.

In June 2006, the Financial Accounting Standards Board ("FASB") issued Interpretation No. 48, "Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109" ("FIN 48"). FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company adopted FIN 48 as of January 1, 2007, and the adoption had no significant impact on the Company's consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS 157"). SFAS 157 defines fair value, establishes a framework for measuring fair value under generally accepted accounting principles, and expands disclosures about fair value measurements. This statement applies under other accounting pronouncements that require or permit fair value measurements; accordingly, this statement does not require any new fair value measurements. SFAS 157 is effective for fiscal years beginning after November 15, 2007. The Company has determined that the impact of implementing the statement will not have a material effect on its financial assets and liabilities, including its derivative financial instruments.

On February 15, 2007, the FASB issued SFAS No. 159, "The Fair Value Opinion for Financial Assets and Financial Liabilities" ("SFAS 159") which permits companies to report selected financial assets and liabilities at fair value. SFAS 159 also requires entities to display the fair value of those assets and liabilities for which the entity has chosen to use fair value on the face of the balance sheet. SFAS 159 does not eliminate disclosure requirements included in other accounting standards. SFAS 159 is effective for fiscal years beginning after November 15, 2007. Management anticipates continuing to use fair value reporting primarily for the items in which other accounting standards require fair value accounting and disclosures.

Note 2 - Acquisitions

The Company acquired all of the net assets of Minis as of August 31, 2007. The net assets of Minis were incorporated into a new, wholly-owned subsidiary of the Company which will continue to operate under the name of Minis & Co., Inc. The acquisition was accounted for using the purchase method of accounting, and accordingly, the results of Minis' operations have been included in the consolidated financial statements beginning September 1, 2007. Minis is a registered investment advisor based in Savannah, Georgia, offering a full line of investment management services. Minis' assets under management at September 1, 2007 were approximately \$500 million.

Notes to Consolidated Financial Statements

Note 2 - Acquisitions (continued)

The aggregate purchase price was \$3.80 million, consisting of 71,000 shares of the Company's common stock valued at \$1.78 million, \$1.853 million in cash, net of \$118,000 in cash received at closing, and approximately \$48,000 in direct acquisition costs, primarily consisting of external legal and accounting fees. The value of the common shares issued was determined based on the average market price of the Company's common stock on the day before and the day on which the terms of the acquisition were publicly announced.

The terms of the asset purchase agreement provide for contingent earn-out consideration to the former Minis shareholders. Such consideration will be based on actual revenue earned from existing clients at August 31, 2007 as compared to a target level of revenues through June 30, 2010. Based on the assumptions at the time the asset purchase agreement was executed, the Company expected that the aggregate contingent consideration, including interest, would be approximately \$2.2 million payable as near as practicable to the June 30, 2010 determination date. However, Minis' failure to generate revenue at the agreed upon targeted level or above will result in lower contingent consideration paid to the former Minis shareholders.

The preliminary purchase price allocation relating to the Minis acquisition was as follows:

| (\$ in thousands) | September 1, 2007 |
|----------------------------------|-------------------|
| Assets acquired | |
| Cash | \$ 118 |
| Accounts receivable | 53 |
| Premises and equipment | 85 |
| Prepaid expense | 4 |
| Deferred income tax benefits | 876 |
| Intangible assets | 1,400 |
| Goodwill, net of tax benefits | 1,435 |
| Total assets acquired | 3,971 |
| Liabilities assumed | |
| Unearned revenue | 171 |
| Total liabilities assumed | 171 |
| Net assets acquired | \$ 3,800 |

The above amounts are based on the best information currently available. Additional valuation services will be engaged to provide a fully documented basis for the valuation and other factors related to the customer contracts. Of the \$2.835 million of acquired intangible assets, \$1.435 million was allocated to goodwill and \$1.4 million to identifiable intangible assets (customer contracts). The customer contracts have an estimated weighted-average useful life of 10 years. The goodwill and the customer contracts intangible assets will be deductible for tax purposes over a 15-year period. Any additional earn-out consideration to be paid will be accounted for as additional purchase price under the terms of the agreement and will be added to goodwill when determined to be payable.

Russell W. Carpenter, a shareholder of Minis who owned 40 percent of its shares, has served as a director of the Company since 1989 and expects to continue in such role until April 2010.

Note 3 - Restrictions on Cash and Demand Balances Due from Banks and Interest-Bearing Bank Balances

The Subsidiary Banks are required by the Federal Reserve Bank to maintain minimum cash reserves based upon reserve requirements calculated on their deposit balances. Cash reserves of \$469,000 and \$1,841,000 were required as of December 31, 2007 and 2006, respectively. The Company has pledged interest-bearing cash balances at the Federal Home Loan Bank of Atlanta ("FHLB") in addition to investment securities to secure public fund deposits and securities sold under repurchase agreements. Pledged cash balances were \$18,500,000 and \$7,500,000 at December 31, 2007 and 2006, respectively.

Notes to Consolidated Financial Statements

Note 4 - Securities Available for Sale

The aggregate amortized cost and fair value of securities available for sale as of December 31, 2007 and 2006 were as follows:

| 2007 | | | | |
|-------------------------------------|------------------|------------------|-------------------|------------------|
| (\$ in thousands) | Amortized Cost | Unrealized Gains | Unrealized Losses | Fair Value |
| Investment securities: | | | | |
| U. S. government-sponsored agencies | \$ 28,227 | \$ 700 | \$ (4) | \$ 28,923 |
| Mortgage-backed securities | 24,624 | 156 | (122) | 24,658 |
| State and municipal | 2,926 | 86 | - | 3,012 |
| Restricted equity securities | 4,464 | - | - | 4,464 |
| Total investment securities | \$ 60,241 | \$ 942 | \$ (126) | \$ 61,057 |
| | | | | |
| 2006 | | | | |
| (\$ in thousands) | Amortized Cost | Unrealized Gains | Unrealized Losses | Fair Value |
| Investment securities: | | | | |
| U. S. government-sponsored agencies | \$ 33,643 | \$ 73 | \$ (193) | \$ 33,523 |
| Mortgage-backed securities | 14,681 | 10 | (188) | 14,503 |
| State and municipal | 2,104 | 52 | - | 2,156 |
| Restricted equity securities | 3,735 | - | - | 3,735 |
| Total investment securities | \$ 54,163 | \$ 135 | \$ (381) | \$ 53,917 |

The distribution of securities by maturity or expected call date at December 31, 2007 is shown below:

| (\$ in thousands) | Amortized Cost | Fair Value |
|--|------------------|------------------|
| Securities available for sale: | | |
| Due in one year or less | \$ 15,255 | \$ 15,462 |
| Due after one year through five years | 28,758 | 29,148 |
| Due after five years through ten years | 12,980 | 13,156 |
| Due after ten years | 3,248 | 3,291 |
| Total investment securities | \$ 60,241 | \$ 61,057 |

At December 31, 2007 and 2006, investment securities with a carrying value of \$48,621,000 and \$44,190,000, respectively, were pledged as collateral to secure public funds, securities sold under repurchase agreements and FHLB borrowings.

Note 5 - Loans

The composition of the loan portfolio at December 31, 2007 and 2006 is presented below:

| (\$ in thousands) | 2007 | Percent of Total | 2006 | Percent of Total |
|--|-------------------|------------------|-------------------|------------------|
| Commercial | \$ 71,370 | 8.8 % | \$ 57,737 | 8.0 % |
| Real estate - construction and development | 134,110 | 16.6 | 166,172 | 23.1 |
| Real estate - mortgage | 584,477 | 72.3 | 480,381 | 66.6 |
| Installment and other consumer | 18,694 | 2.3 | 16,628 | 2.3 |
| Gross loans | 808,651 | 100.0% | 720,918 | 100.0 % |
| Allowance for loan losses | (12,864) | | (8,954) | |
| Net loans | \$ 795,787 | | \$ 711,964 | |

Notes to Consolidated Financial Statements

Note 5 - Loans (continued)

Changes in the allowance for loan losses are summarized as follows:

| (\$ in thousands) | 2007 | 2006 | 2005 |
|----------------------------|-----------|----------|----------|
| Balance, beginning of year | \$ 8,954 | \$ 7,813 | \$ 6,389 |
| Provision for loan losses | 4,675 | 1,585 | 1,500 |
| Charge-offs | (874) | (506) | (152) |
| Recoveries | 109 | 62 | 76 |
| Balance, end of year | \$ 12,864 | \$ 8,954 | \$ 7,813 |

The following is a summary of information pertaining to impaired loans as of and for the years ended December 31, 2007 and 2006:

| (\$ in thousands) | 2007 | 2006 |
|---|-----------|----------|
| Impaired loans without a valuation allowance | \$ 193 | \$ 825 |
| Impaired loans with a valuation allowance | 14,470 | - |
| Total impaired loans | \$ 14,663 | \$ 825 |
| Valuation allowance related to impaired loans | \$ 2,241 | \$ - |
| Average investment in impaired loans | \$ 7,744 | \$ 1,069 |
| Interest income recognized on impaired loans | \$ 731 | \$ 23 |

At December 31, 2007 and 2006, loans on nonaccrual status amounted to approximately \$14,663,000 and \$825,000, respectively, and loans past due 90 days or more and still accruing interest were \$2,761,000 and \$1,406,000.

The Company has granted loans to certain directors and executive officers of the Company and to their related interests. The aggregate amounts of loans were \$32,253,000 and \$16,332,000 at December 31, 2007 and 2006, respectively. During 2007, new loans of \$36,972,000 were made and repayments of \$21,051,000 were received. Unfunded commitments of credit available to related parties aggregated \$3,385,000 and \$7,554,000 at December 31, 2007 and 2006, respectively. Related party loans are made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with unrelated persons and do not involve more than normal risk of collection.

Note 6 - Premises and Equipment

Premises and equipment at December 31, 2007 and 2006 are summarized as follows:

| (\$ in thousands) | Depreciable Lives | 2007 | 2006 |
|--|-------------------|----------|----------|
| Land | - | \$ 698 | \$ 698 |
| Buildings and improvements | 39 - 50 | 2,980 | 2,665 |
| Furniture and banking equipment | 3 - 15 | 7,404 | 6,571 |
| Leasehold improvements | 10 - 39 | 2,286 | 2,069 |
| Total cost | | 13,368 | 12,003 |
| Less accumulated depreciation and amortization | | 6,538 | 5,638 |
| Premises and equipment, net | | \$ 6,830 | \$ 6,365 |

Buildings and improvements in 2007 include approximately \$332,000 of construction in progress costs for a Bryan banking office and additional space for an operations center. The total building cost is estimated at \$2,000,000.

Notes to Consolidated Financial Statements

Note 7 - Deposits

Total time deposits mature as follows: 2008 - \$317,540,000; 2009 - \$17,927,000; 2010 - \$11,700,000; 2011 - \$4,016,000 and 2012 - \$3,605,000 and thereafter - \$242,000. Brokered time deposits mature as follows: 2008 - \$79,112,000; 2009 - \$133,000; 2010 - \$342,000; 2011 - \$76,000 and 2012 - \$75,000. Additionally, \$47,360,000 of non-maturity institutional money market accounts are considered brokered deposits because the deposits are from customers of brokerage firms up to a maximum of \$100,000 per depositor. A fee is paid for these deposits in addition to the interest.

The following table indicates the amount of the Company's time deposits of \$100,000 or more at December 31, 2007 by time remaining until maturity.

| Maturity Period (\$ in thousands) | Total |
|-----------------------------------|-------------------|
| Three months or less | \$ 62,258 |
| Over three through six months | 37,794 |
| Over six through twelve months | 53,276 |
| Over twelve months | 21,817 |
| Total | \$ 175,145 |

Note 8 - Short-Term Borrowings

Short-term borrowings at December 31, 2007 and 2006 consist of federal funds purchased, securities sold under agreements to repurchase and FHLB short-term advances:

| (\$ in thousands) | Federal Funds Purchased | Securities Sold Under Repurchase Agreements | FHLB Short-Term Advances | Notes Payable |
|--|----------------------------|--|--------------------------------|------------------|
| 2007 | | | | |
| Balance at December 31 | \$ 1,857 | \$ 18,742 | \$ 50,000 | \$ - |
| Maximum indebtedness at any month end | 2,347 | 25,402 | 50,000 | - |
| Daily average indebtedness outstanding | 1,565 | 20,434 | 30,797 | - |
| Average rate paid for the year | 5.18% | 4.58% | 5.17% | - |
| Average rate paid on period-end borrowings | 4.05% | 3.75% | 4.44% | N/A |
| 2006 | | | | |
| Balance at December 31 | \$ 1,003 | \$ 15,684 | \$ 24,000 | \$ - |
| Maximum indebtedness at any month end | 2,502 | 19,073 | 40,000 | 2,100 |
| Daily average indebtedness outstanding | 1,616 | 15,724 | 17,977 | 858 |
| Average rate paid for the year | 5.02% | 4.48% | 5.28% | 7.69% |
| Average rate paid on period-end borrowings | 5.08% | 4.75% | 5.36% | N/A |

As of December 31, 2007 and 2006, the Company had short-term borrowings totaling \$70,599,000 and \$40,687,000, respectively. The average interest rates were 4.94 percent and 4.98 percent during the years ended 2007 and 2006, respectively. The interest rates on short-term borrowings ranged from 3.75 percent to 4.44 percent at December 31, 2007 and from 4.75 percent to 5.36 percent at December 31, 2006. The maximum amount outstanding at the end of any month was \$70,599,000 and \$56,683,000 during 2007 and 2006, respectively. At December 31, 2007 federal funds borrowing arrangements aggregating \$51,800,000 were available to the Subsidiary Banks from correspondent banking institutions. There are no commitment fees and no requirements for compensating balances. These unused lines principally serve as temporary liquidity back-up lines and are subject to availability of funds and other specific limitations of the correspondent banks. Savannah is a member and shareholder of the Federal Reserve Bank of Atlanta ("FRB") and has access to borrowings at the FRB discount window. Bryan has also been approved to access the FRB discount window.

Notes to Consolidated Financial Statements

Note 8 - Short-Term Borrowings (continued)

The Company has a \$5,000,000 line of credit through a correspondent bank, of which none was advanced at December 31, 2007. The primary purpose of the line is to provide access to funds that can be used for short-term corporate needs. The borrowing facility is available through September 20, 2008 at which time any outstanding indebtedness is due and payable in full. Advances on the line are subject to the Company certifying compliance with covenants and conditions specified in the agreement. The covenants include customary performance items and a negative pledge agreement on the stock of Savannah. The Company may not pledge the stock of Savannah for any other indebtedness or other purpose without the express written consent of the lender.

Note 9 - Federal Home Loan Bank Advances – Long-Term

Convertible Advances - At December 31, 2007 and 2006, the Company had a convertible fixed rate advance of \$1,000,000 with an interest rate of 6.39 percent maturing in August 2009. The advance is convertible each quarter at the option of the FHLB to an advance with a rate equal to the current three-month LIBOR. During 2007, the Company had a \$10,000,000 convertible advance with an interest rate of 4.82 percent converted by the FHLB.

Long-term Advances - Long-term advances from the FHLB totaled \$1,973,000 and \$2,309,000 at December 31, 2007 and 2006, respectively. The weighted-average interest rates on the long-term advances were 4.76 and 4.64 percent at December 31, 2007 and 2006, respectively. Aggregate maturities are \$1,750,000 in 2008, \$50,000 in 2009 and \$173,000 in 2013 and thereafter. Interest is generally payable monthly and scheduled principal reductions are made quarterly, semi-annually or at maturity. The long-term advances include prepayment penalties for each advance.

FHLB Advance Borrowing Capacity - The Subsidiary Banks are shareholders of the FHLB and have access to secured borrowings from the FHLB under Blanket Floating Lien Agreements. Under these agreements, the Subsidiary Banks have credit lines up to 80 percent of the FHLB qualifying collateral value of their 1-4 family first mortgage loans and up to 50 percent of the FHLB qualifying collateral value of their home equity lines of credit and second mortgage residential loans. The Subsidiary Banks' individual borrowing limits range from 10 to 25 percent of assets. In aggregate, the Subsidiary Banks had secured borrowing capacity of approximately \$131.5 million of which \$53.0 million was advanced at December 31, 2007. These credit arrangements serve as a core funding source as well as liquidity backup for the Subsidiary Banks. Additional advances are subject to review and approval by the FHLB.

Note 10 - Subordinated Debt to Nonconsolidated Subsidiaries

During the third quarters 2003 and 2004, the Company formed SAVB Capital Trust I and SAVB Capital Trust II (the "Trusts"), nonconsolidated subsidiaries whose sole purpose was to issue \$6,000,000 and \$4,000,000, respectively, in Trust Preferred Securities through investment pools sponsored by two national brokerage firms. The Trust Preferred Securities have maturities of 30 years and are redeemable at the Company's option on any quarterly interest payment date after five years. There are certain events (as defined in the Trust agreements) in which the securities may be redeemed within the first five years at the Company's option. At December 31, 2007, the interest rates on the securities were 8.09 and 7.19 percent, respectively, with quarterly resets at the three-month LIBOR plus 2.85 and 2.20 percent, respectively. The Company's liabilities to the nonconsolidated Trusts are recorded as liabilities of \$6.186 million and \$4.124 million and investments of \$186,000 and \$124,000, respectively, in the consolidated balance sheet. Subject to certain limitations, the securities qualify as Tier 1 capital for regulatory capital purposes under Federal Reserve Bank regulations.

Notes to Consolidated Financial Statements

Note 11 - Income Taxes

Income tax expense is composed of the following for each of the years ended December 31:

| (\$ in thousands) | 2007 | 2006 | 2005 |
|--------------------|----------|----------|----------|
| Current federal | \$ 5,355 | \$ 5,537 | \$ 5,227 |
| Current state | 418 | 411 | 513 |
| Total current | 5,773 | 5,948 | 5,740 |
| Deferred federal | (1,364) | (629) | (755) |
| Deferred state | (174) | (104) | (105) |
| Total deferred | (1,538) | (733) | (860) |
| Income tax expense | \$ 4,235 | \$ 5,215 | \$ 4,880 |

Investments in federal and state low-income housing tax credit partnerships reduced federal and state income tax expense approximately \$265,000, \$227,000 and \$226,000 in 2007, 2006 and 2005, respectively.

A reconciliation between income tax expense and the amounts computed by applying the U.S. federal tax rate of 34 percent to income before income taxes is as follows:

| (\$ in thousands) | 2007 | 2006 | 2005 |
|---------------------------------------|----------|----------|----------|
| Tax provision at 34% | \$ 4,036 | \$ 5,173 | \$ 4,733 |
| State tax, net of federal tax benefit | 212 | 199 | 226 |
| Benefit of tax-exempt income, net | (121) | (129) | (157) |
| Other | 108 | (28) | 78 |
| Income tax expense | \$ 4,235 | \$ 5,215 | \$ 4,880 |

Deferred income tax assets and liabilities are comprised of the following at December 31, 2007 and 2006:

| (\$ in thousands) | 2007 | 2006 |
|--------------------------------------|----------|----------|
| Deferred tax assets: | | |
| Allowance for loan losses | \$ 4,748 | \$ 3,285 |
| Tax-deductible goodwill | 856 | - |
| Unrealized losses on securities | - | 93 |
| Unamortized loan fees | 269 | 361 |
| Unamortized non-compete costs | 34 | 39 |
| Unrealized losses on derivatives | - | 293 |
| Deferred compensation expense | 311 | 232 |
| Stock-compensation expense | 31 | 60 |
| Other | 378 | 165 |
| Total deferred tax assets | 6,627 | 4,528 |
| Deferred tax liabilities: | | |
| Depreciation | 408 | 395 |
| Deferred costs on loans and deposits | 93 | 101 |
| Unrealized gains on securities | 285 | - |
| Unrealized gains on derivatives | 644 | - |
| Other | 165 | 79 |
| Total deferred tax liabilities | 1,595 | 575 |
| Net deferred tax assets | \$ 5,032 | \$ 3,953 |

The net deferred tax assets are included in the consolidated balance sheets in other assets. The Company files a consolidated Federal tax return and a consolidated Georgia return for the Georgia-based parent and subsidiaries.

Notes to Consolidated Financial Statements

Note 12 - Stock Option and Employee Benefit Plans

As discussed in Note 1, the Company has two stock option plans. All authorized shares have been awarded from the 1995 Plan. There are 158,121 authorized option shares remaining under the 2005 Omnibus Plan at December 31, 2007. The options granted in the chart below generally vest 20 percent each year over five years and are exercisable over ten years except for 22,729 option shares granted to directors in 2007, 2006 and 2005 which vest within one year and 18,310 restricted share awards which vest from three to ten years. Some of the executive officer option shares also include minimum performance triggers as a condition of vesting.

Changes in stock options outstanding for the three years ended December 31, 2007, 2006 and 2005 are as follows. All share and per share amounts have been restated to reflect the effect of a 5-for-4 stock split in December 2006.

| | 2007 | | 2006 | | 2005 | |
|----------------------------------|----------|---------------------------------|----------|---------------------------------|-----------|---------------------------------|
| | Shares | Weighted Average Exercise Price | Shares | Weighted Average Exercise Price | Shares | Weighted Average Exercise Price |
| Outstanding at beginning of year | 271,230 | \$ 15.58 | 304,046 | \$ 14.49 | 369,190 | \$ 11.26 |
| Granted | 24,733 | 25.39 | 10,716 | 28.56 | 36,878 | 22.31 |
| Exercised | (64,410) | 11.63 | (35,976) | 10.28 | (102,022) | 5.64 |
| Forfeited | (21,069) | 5.52 | (7,556) | 15.99 | - | - |
| Outstanding at end of year | 210,484 | \$ 17.76 | 271,230 | \$ 15.58 | 304,046 | \$ 14.49 |
| Exercisable at end of year | 148,013 | \$ 16.30 | 182,254 | \$ 14.12 | 176,199 | \$ 12.30 |

At December 31, 2007, the aggregate intrinsic value of outstanding and exercisable stock options was \$402,000 and \$391,000, respectively.

Options outstanding at December 31, 2007 were as follows:

| Outstanding Common Options | Outstanding | | | Exercisable | |
|----------------------------|------------------------------|-----------------------|------------------------|-------------|------------------------|
| | Remaining Contractual Number | Weighted Average Life | Weighted Average Price | Number | Weighted Average Price |
| Range of exercise prices | | | | | |
| \$9.98 - \$12.00 | 24,578 | 2.84 | \$ 10.12 | 24,578 | \$ 10.12 |
| \$12.01 - \$15.00 | 45,027 | 2.77 | 13.21 | 45,027 | 13.21 |
| \$15.01 - \$20.00 | 69,525 | 6.05 | 16.70 | 44,679 | 16.42 |
| \$20.01 - \$25.00 | 35,905 | 7.14 | 22.31 | 18,280 | 22.42 |
| \$25.00 - \$28.56 | 35,449 | 9.16 | 26.31 | 15,449 | 27.60 |
| Total outstanding | 210,484 | 5.68 | \$ 17.76 | 148,013 | \$ 16.30 |

Restricted Stock - In 2007 and 2006, the Board granted 18,310 shares of restricted stock under the 2005 Omnibus Plan which awards certain officers common shares of the Company. The cost of these shares is being amortized against earnings using the vesting schedule over the three and ten year vesting periods. Unrecognized compensation cost for restricted stock awards was \$207,000 at December 31, 2007.

The Company sponsors a 401(k) employee savings and profit sharing plan in which substantially all full-time employees are eligible to participate. The plan allows eligible employees to save a portion of their salary on a pre-tax basis. Contributions by the Company to the plan are discretionary. Contributions and administrative expenses related to the plan aggregated \$354,000, \$356,000 and \$276,000 for the years ended December 31, 2007, 2006 and 2005, respectively.

Notes to Consolidated Financial Statements

Note 13 - Capital Ratios and Dividend Restrictions

The Subsidiary Banks' primary regulators have adopted capital requirements that specify the minimum capital level for which no prompt corrective action is required. In addition, the Federal Deposit Insurance Corporation ("FDIC") has adopted FDIC insurance assessment rates based on certain "well-capitalized" risk-based and equity capital ratios. Failure to meet minimum capital requirements can result in the initiation of certain actions by the regulators that, if undertaken, could have a material effect on the Company's and the Subsidiary Banks' financial statements. Management believes that the Company and the Subsidiary Banks meet all capital adequacy requirements to which they are subject as of December 31, 2007. The following tables show the capital ratios for the Company and the Subsidiary Banks at December 31, 2007 and 2006:

| (\$ in thousands) | Company | | Savannah | | Bryan | | Harbourside | |
|--|----------|----------|----------|----------|----------|---------|------------------|----------|
| | 2007 | 2006 | 2007 | 2006 | 2007 | 2006 | 2007 | 2006 |
| Qualifying Capital | | | | | | | | |
| Tier 1 capital | \$81,049 | \$77,205 | \$50,433 | \$48,718 | \$18,045 | \$16,83 | \$ 8,681 | \$ 8,687 |
| Total capital | 90,748 | 85,910 | 56,864 | 54,712 | 20,328 | 18,874 | 9,612 | 9,207 |
| Leverage Ratios | | | | | | | | |
| Tier 1 capital to average assets | 8.93% | 9.57% | 8.29% | 8.58% | 8.62% | 9.23% | 10.11% | 15.55% |
| Risk-based Ratios | | | | | | | | |
| Tier 1 capital to risk-weighted assets | 10.49% | 11.09% | 9.84% | 10.17% | 9.88% | 10.31% | 11.86% | 16.98% |
| Total capital to risk-weighted assets | 11.74% | 12.34% | 11.09% | 11.42% | 11.13% | 11.56% | 13.13% | 18.00% |
| Required Regulatory Capital Ratios: | | | | | Minimum | | Well-Capitalized | |
| Tier 1 capital to average assets | | | | | 4.00% | | 5.00% | |
| Tier 1 capital to risk-weighted assets | | | | | 4.00% | | 6.00% | |
| Total capital to risk-weighted assets | | | | | 8.00% | | 10.00% | |

As of December 31, 2007, the Subsidiary Banks were categorized as well-capitalized under the regulatory framework for prompt corrective action in the most recent notification from the FDIC. There are no conditions or events since the notification that management believes have changed the institutions' categories. Harbourside must maintain a minimum 8.0 percent tangible equity to asset ratio through March 2009 under the terms of its de novo charter which became effective in March 2006. The tangible equity to capital ratio was 9.70 percent at December 31, 2007.

Banking regulations restrict the amount of cash dividends that banks may pay without obtaining regulatory approval. At December 31, 2007, \$15,716,000 in retained earnings of the Subsidiary Banks was available for the payment of dividends, subject to maintaining adequate capital ratios in the Subsidiary Banks. The Company is not subject to any regulatory restrictions on the payment of dividends to its shareholders.

Note 14 - Leases and Commitments

Future minimum payments under non-cancelable land and office space operating leases with remaining terms in excess of one year are presented as follows: 2008 - \$1,092,000; 2009 - \$845,000; 2010 - \$713,000; 2011 - \$718,000; 2012 - \$617,000; 2013 and thereafter is \$8,102,000. The land and office space leases contain customary escalation clauses. The Company or the Subsidiary Banks are responsible for taxes, insurance and maintenance during the lease term under certain leases. During 2007, the Company renegotiated its long-term data processing contract. Future minimum payments are as follows: 2008 - \$1,152,000; 2009 - \$1,186,500; 2010 - \$1,222,000; 2011 - \$1,259,000; 2012 - \$216,000. The contract contains customary escalation and buyout clauses.

The net rental expense for all office space operating leases amounted to \$1,169,000 in 2007, \$1,006,000 in 2006 and \$653,000 in 2005. The leases on the office space have five to twenty-year renewal options and require increased rental payments under consumer price index escalation clauses.

Notes to Consolidated Financial Statements

Note 15 - Other Operating Expense

The components of other operating expense for the years ended December 31, 2007, 2006 and 2005 were as follows:

| (\$ in thousands) | 2007 | 2006 | 2005 |
|---------------------------------------|----------|----------|----------|
| Regulatory assessments and audit fees | \$ 876 | \$ 832 | \$ 694 |
| Professional and directors fees | 854 | 959 | 748 |
| Advertising and sales promotion | 433 | 463 | 294 |
| Stationery and supplies | 300 | 301 | 239 |
| Postage and courier | 277 | 265 | 243 |
| Loan costs | 209 | 185 | 170 |
| Taxes and licenses | 203 | 204 | 154 |
| Telephone | 203 | 173 | 150 |
| Correspondent bank charges | 123 | 155 | 137 |
| Dues and subscriptions | 116 | 110 | 97 |
| Insurance | 77 | 90 | 76 |
| Pre-opening expenses | - | 263 | 129 |
| Other expense | 712 | 656 | 542 |
| Total other operating expense | \$ 4,383 | \$ 4,656 | \$ 3,673 |

Note 16 - On-Balance Sheet Derivative Instruments and Hedging Activities

SFAS 133, as amended and interpreted, establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. As required by SFAS 133, the Company records all derivatives on the balance sheet at fair value. The accounting for changes in the fair value of derivatives depends on the intended use of the derivative and the resulting designation. Derivatives used to hedge the exposure to variability in expected future cash flows, or other types of forecasted transactions, are considered cash flow hedges.

For derivatives designated as cash flow hedges, the effective portion of changes in the fair value of the derivative is initially reported in other comprehensive income (outside of earnings) and subsequently reclassified to earnings when the hedged transaction affects earnings. The ineffective portion of changes in the fair value of the derivative is recognized directly in earnings. The Company assesses the effectiveness of each hedging relationship by comparing the changes in cash flows of the derivative hedging instrument with the changes in cash flows of the designated hedged item or transaction. For derivatives not designated as hedges, changes in fair value are recognized in earnings. The Company does not currently have any derivatives that are not designated as hedges.

The Company's objective in using derivatives is to add stability to interest income and to manage its exposure to interest rate movements or other identified risks. To accomplish this objective, the Company primarily uses interest rate floors, collars or swaps as part of its cash flow hedging strategy. Interest rate floors and collars designated as cash flow hedges involve the receipt of variable-rate cash flows above or below the applicable strike rates over the life of the agreements without exchange of the underlying principal amount. Interest rate swap agreements designated as cash flow hedges involve the receipt of fixed rate amounts in exchange for variable rate payments over the life of the agreements without exchange of the underlying principal amount. During 2007, such derivatives were used to hedge the variable cash flows associated with existing variable rate assets. The Company does not use derivatives for trading or speculative purposes.

Exposure to credit risk arises from the possibility of nonperformance by counterparties. These counterparties consist of financial institutions that are well established and well capitalized. The Company controls this credit risk through limits and monitoring procedures. No losses on derivative instruments have resulted as a result of counterparty nonperformance. Nevertheless, the related credit risk is considered and measured when and where appropriate.

Notes to Consolidated Financial Statements

Note 16 - On-Balance Sheet Derivative Instruments and Hedging Activities (continued)

Selected information with respect to notional amounts, recorded fair values, and maturity dates of derivative instruments is summarized as follows as of December 31.

| (\$ in thousands) | Maturity | Notional Amount | 2007 | | 2006 | |
|----------------------------|-----------|-----------------|------------|-----------|------------|-----------|
| | | | Fair Value | | Fair Value | |
| | | | Asset | Liability | Asset | Liability |
| Cash flow hedges: | | | | | | |
| Interest rate swap | Nov 2010 | \$ 50,000 | \$ 1,514 | \$ - | \$ - | \$ 332 |
| 6%/9% Interest rate collar | June 2010 | 40,000 | 284 | - | - | 29 |
| 6% Interest rate floor | June 2010 | 35,000 | 264 | - | 49 | - |
| Total | | \$ 125,000 | \$ 2,062 | \$ - | \$ 49 | \$ 361 |

The net change in fair value of derivative instruments of \$1,530,000 and (\$236,000) in 2007 and 2006, respectively, for derivatives designated as cash flow hedges is separately disclosed in the statements of changes in shareholders' equity. No hedge ineffectiveness on cash flow hedges was recognized during 2007 or 2006.

Amounts reported in accumulated other comprehensive income related to derivatives will be reclassified to interest income as interest payments are received on the Company's variable-rate assets. The change in net unrealized gains (losses) on cash flow hedges reflects a reclassification of (\$299,000) and (\$184,000) of net unrealized gains (losses) from accumulated other comprehensive income to interest income during 2007 and 2006, respectively. During 2008, the Company estimates that \$429,000 will be reclassified.

In January, 2008 the Company terminated \$25 million of their interest rate swap position for a gain of \$966,000. This amount will be amortized into interest income on a straight-line basis over the remaining life of the swap.

Note 17 - Financial Instruments with Off-Balance Sheet Risk

The Company is a party to financial instruments with off-balance sheet risk in the normal course of business in order to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. These instruments involve, to varying degrees, elements of credit and interest rate risk.

The Company's exposure to loan losses in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual amounts of those instruments. The credit risk involved is essentially the same as that involved in extending loan facilities to customers. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments. The Company evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained by the Company upon extension of credit, if deemed necessary, is based on management's credit evaluation of the borrower. Collateral may include cash, securities, accounts receivable, inventory, equipment, and real estate.

Commitments to extend credit are agreements to lend to a customer as 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. At December 31, 2007 and 2006 unfunded commitments to extend credit and unfunded lines of credit were \$136,480,000 and \$156,323,000, of which some were subject to interest rate lock commitments. Since many of these commitments are expected to expire without being drawn upon, these amounts do not necessarily represent future cash requirements.

Letters of credit are conditional commitments issued by the Company to guarantee payment or performance by a customer to a third party. At December 31, 2007 and 2006, commitments under letters of credit aggregated approximately \$7,916,000 and \$10,204,000, respectively.

Notes to Consolidated Financial Statements

Note 18 - Fair Value of Financial Instruments

As with most financial institutions, the majority of the Company's assets and liabilities are considered financial instruments. Many of the financial instruments, however, lack an available trading market as characterized by a willing buyer and willing seller engaging in an exchange transaction. Therefore, significant estimates and present value calculations are used for the purpose of this disclosure. Such estimates involve judgments as to economic conditions, risk characteristics and future expected loss experience of various financial instruments and other factors that cannot be determined with precision.

Cash and due from banks, federal funds sold, all non-maturity deposits, and other borrowings have carrying amounts which approximate fair value primarily because of the short repricing opportunities of these instruments.

Following is a description of the methods and assumptions used by the Company to estimate the fair value of its financial instruments:

Investment securities: Fair value is based upon quoted market prices, if available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

Loans: The fair value for loans is estimated for portfolios of loans with similar financial characteristics. Loans are segregated by type, such as commercial, mortgage, and consumer loans. The fair value of the loan portfolio is calculated by discounting contractual cash flows using estimated market discount rates which reflect the credit and interest rate risk inherent in the loan. The estimated fair value of the Subsidiary Banks' off-balance sheet commitments is nominal since the committed rates approximate current rates offered for commitments with similar rate and maturity characteristics and since the estimated credit risk associated with such commitments is not significant.

Derivative instruments: The fair value of derivative instruments, consisting of interest rate contracts, is equal to the estimated amount that the Company would receive or pay to terminate the derivative instruments at the reporting date, taking into account current interest rates and the credit-worthiness of the counterparties.

Deposit liabilities: The fair value of time deposits is based on the discounted value of contractual cash flows. The discount rate is based on the LIBOR swap curve.

The carrying amounts and estimated fair values of the Company's financial instruments are as follows as of December 31:

| (\$ in thousands) | 2007 | | 2006 | |
|---|----------------|----------------------|----------------|----------------------|
| | Carrying Value | Estimated Fair Value | Carrying Value | Estimated Fair Value |
| Financial assets: | | | | |
| Cash and federal funds sold | \$ 17,156 | \$ 17,156 | \$ 36,903 | \$ 36,903 |
| Interest-bearing deposits | 20,148 | 20,148 | 10,394 | 10,394 |
| Securities available for sale | 61,057 | 61,057 | 53,917 | 53,917 |
| Loans held for sale | 180 | 180 | 914 | 917 |
| Loans, net of allowance for loan losses | 795,787 | 803,012 | 711,964 | 709,133 |
| Derivative asset positions | 2,062 | 2,062 | 49 | 49 |
| Financial liabilities: | | | | |
| Deposits | 764,218 | 766,102 | 706,824 | 705,986 |
| Short-term borrowings | 70,599 | 70,503 | 40,687 | 40,687 |
| FHLB advances – long-term | 2,973 | 2,942 | 13,309 | 13,410 |
| Subordinated debt to nonconsolidated subsidiaries | 10,310 | 10,310 | 10,310 | 10,310 |
| Derivative liability positions | - | - | 361 | 361 |

Notes to Consolidated Financial Statements

Note 19 - The Savannah Bancorp, Inc. (Parent Company Only) Financial Information (\$ in thousands)

The following are condensed balance sheets of the Parent Company at December 31, 2007 and 2006:

| | 2007 | 2006 |
|---|-----------|-----------|
| Assets | | |
| Cash on deposit | \$ 40 | \$ 35 |
| Interest-bearing deposits | 1,040 | 652 |
| Investment in subsidiaries | 82,652 | 73,607 |
| Premises and equipment | 1,072 | 1,005 |
| Investment in nonconsolidated subsidiary | 1,607 | 1,518 |
| Other assets | 1,483 | 1,189 |
| Total assets | \$ 87,894 | \$ 78,006 |
| Liabilities | | |
| Subordinated debt | \$ 10,310 | \$ 10,310 |
| Other liabilities | 1,312 | 1,122 |
| Total liabilities | 11,622 | 11,432 |
| Shareholders' equity | | |
| Common stock | 5,924 | 5,781 |
| Capital surplus | 38,279 | 35,747 |
| Retained earnings | 30,512 | 25,681 |
| Treasury stock | (4) | (4) |
| Accumulated other comprehensive income (loss) | 1,561 | (631) |
| Total shareholders' equity | 76,272 | 66,574 |
| Total liabilities and equity | \$ 87,894 | \$ 78,006 |

Notes to Consolidated Financial Statements

The operating results of the Parent Company are shown below for the three years ended December 31:

| | 2007 | 2006 | 2005 |
|---|----------|-----------|----------|
| Dividends from subsidiaries | \$ 7,500 | \$ 3,700 | \$ 1,250 |
| Interest income | 27 | 59 | 146 |
| Interest expense | 842 | 881 | 652 |
| Net interest and dividend income | 6,685 | 2,878 | 744 |
| Other income | 38 | 30 | 58 |
| Processing / management fees | 5,090 | 4,352 | 3,827 |
| Total income | 11,813 | 7,260 | 4,629 |
| Corporate expenses | 618 | 721 | 663 |
| Processing / management costs | 5,165 | 4,427 | 3,891 |
| Other expenses | 5,783 | 5,148 | 4,554 |
| Income before income taxes and equity in undistributed net income of subsidiaries | 6,030 | 2,112 | 75 |
| Income tax benefits | 415 | 550 | 440 |
| Income before equity in undistributed net income of subsidiaries | 6,445 | 2,662 | 515 |
| Equity in undistributed net income of subsidiaries | 1,191 | 7,340 | 8,525 |
| Net income | \$ 7,636 | \$ 10,002 | \$ 9,040 |

Notes to Consolidated Financial Statements

The cash flows of the Parent Company are shown below for the three years ended December 31:

| | 2007 | 2006 | 2005 |
|---|------------|----------------|--------------|
| Operating activities | | | |
| Net income | \$ 7,636 | \$ 10,002 | \$ 9,040 |
| Adjustments to reconcile net income to cash provided by operating activities: | | | |
| Equity in undistributed net income of subsidiaries | (1,191) | (7,340) | (8,525) |
| Depreciation of equipment | 369 | 306 | 259 |
| Non cash stock-based compensation expense | 147 | 299 | - |
| Change in other assets and liabilities, net | (104) | 364 | (436) |
| Net cash provided by operating activities | 6,857 | 3,631 | 338 |
| Investing activities | | | |
| Distribution from (investment in) nonconsolidated subsidiary | - | 1,300 | (2,709) |
| Investment in consolidated subsidiary | (1,970) | - | - |
| Purchase of equipment and software | (437) | (353) | (626) |
| Capital contribution to consolidated subsidiaries | (2,000) | (10,000) | (2,000) |
| Net cash used in investing activities | (4,407) | (9,053) | (5,335) |
| Financing activities | | | |
| Net (decrease) increase in short-term borrowings | - | (2,000) | 2,000 |
| Dividends paid | (2,805) | (2,593) | (2,307) |
| Issuance of common stock | - | - | 11,588 |
| Exercise of options | 748 | 381 | 916 |
| Net cash (used in) provided by financing activities | (2,057) | (4,212) | 12,197 |
| Increase (decrease) in cash and cash equivalents | 393 | (9,634) | 7,200 |
| Cash, beginning of year | 687 | 10,321 | 3,121 |
| Cash, end of year | \$ 1,080 | \$ 687 | \$ 10,321 |

The Parent Company financial statements include the following intercompany items: interest-bearing deposits on the balance sheets; dividend income, interest income and processing / management fees on the statements of income. The investment in the nonconsolidated subsidiary on the balance sheet represents 50 percent ownership in two limited partnerships which own the headquarters building at 25 Bull Street, Savannah, GA and the associated parking lot.

Management's Discussion and Analysis of Financial Condition and Results of Operations

For a comprehensive presentation of the Company's financial condition and results of operations, the following selected financial data and analysis should be reviewed along with the consolidated financial statements and the accompanying notes to the consolidated financial statements.

Table 1 - Selected Financial Condition Highlights -- Five Year Comparison

| (\$ in thousands, except share data) | 2007 | 2006 | 2005 | 2004 | 2003 |
|--|------------|------------|------------|------------|------------|
| Selected Average Balances | | | | | |
| Assets | \$ 869,026 | \$ 769,917 | \$ 685,163 | \$ 557,474 | \$ 443,502 |
| Loans held for sale | 1,299 | 7,842 | 23,033 | 27,209 | 939 |
| Loans - net of unearned fees | 754,490 | 658,750 | 565,131 | 441,421 | 356,006 |
| Securities | 58,910 | 50,600 | 41,300 | 40,703 | 44,015 |
| Other interest-earning assets | 16,201 | 17,278 | 26,168 | 22,383 | 21,198 |
| Total interest-earning assets | 830,900 | 734,470 | 655,632 | 531,716 | 422,158 |
| Interest-bearing deposits | 628,310 | 542,375 | 487,493 | 371,877 | 300,045 |
| Borrowed funds | 70,939 | 62,255 | 55,255 | 67,353 | 40,158 |
| Total interest-bearing liabilities | 699,249 | 604,630 | 542,748 | 439,230 | 340,203 |
| Noninterest-bearing deposits | 91,367 | 96,113 | 89,386 | 76,593 | 65,403 |
| Total deposits | 719,677 | 638,488 | 576,879 | 448,470 | 365,448 |
| Shareholders' equity | 71,516 | 61,766 | 47,428 | 38,126 | 35,740 |
| Loan to deposit ratio – average | 105% | 103% | 98% | 98% | 97% |
| Selected Financial Data at Year-End | | | | | |
| Assets | \$ 932,459 | \$ 843,514 | \$ 717,901 | \$ 617,341 | \$ 476,865 |
| Interest-earning assets | 878,992 | 803,927 | 685,531 | 593,035 | 449,025 |
| Loans held for sale | 180 | 914 | 10,473 | 26,471 | 10,393 |
| Loans - net of unearned fees | 808,651 | 720,918 | 613,667 | 499,868 | 386,731 |
| Deposits | 764,218 | 706,824 | 600,510 | 506,120 | 389,146 |
| Interest-bearing liabilities | 759,597 | 669,974 | 558,116 | 488,546 | 360,817 |
| Shareholders' equity | 76,272 | 66,574 | 58,543 | 40,071 | 36,771 |
| Loan to deposit ratio | 106% | 102% | 102% | 99% | 99% |
| Shareholders' equity to total assets | 8.18% | 7.89% | 8.15% | 6.49% | 7.71% |
| Dividend payout ratio | 36.73% | 25.92% | 25.53% | 37.69% | 45.00% |
| Risk-based capital ratios: | | | | | |
| Tier 1 capital to risk-weighted assets | 10.49% | 11.09% | 11.52% | 9.95% | 10.60% |
| Total capital to risk-weighted assets | 11.74% | 12.34% | 12.77% | 11.20% | 11.85% |
| Loan Quality Data | | | | | |
| Nonperforming assets | \$ 19,535 | \$ 2,776 | \$ 1,357 | \$ 998 | \$ 1,525 |
| Nonperforming loans | 17,424 | 2,231 | 1,357 | 538 | 598 |
| Nonaccruing loans | 14,663 | 825 | 1,313 | 210 | 574 |
| Loans past due 90 days - accruing | 2,761 | 1,406 | 44 | 328 | 24 |
| Net charge-offs | 765 | 444 | 76 | 128 | 306 |
| Allowance for loan losses | 12,864 | 8,954 | 7,813 | 6,389 | 5,067 |
| Nonperforming loans to loans | 2.15% | 0.31% | 0.22% | 0.11% | 0.15% |
| Nonperforming assets to loans and other real estate owned | 2.41% | 0.39% | 0.22% | 0.20% | 0.39% |
| Net charge-offs to average loans | 0.10% | 0.07% | 0.01% | 0.03% | 0.09% |
| Allowance for loan losses to total loans | 1.59% | 1.24% | 1.27% | 1.28% | 1.31% |
| Per Share Data at Year-End (a) | | | | | |
| Book value | \$ 12.88 | \$ 11.52 | \$ 10.20 | \$ 7.80 | \$ 7.17 |
| Common stock closing price (NASDAQ) | \$ 17.14 | \$ 27.25 | \$ 28.38 | \$ 21.64 | \$ 18.56 |
| Common shares outstanding (000s) | 5,924 | 5,781 | 5,739 | 5,140 | 5,129 |

(a) Share and per share amounts have been restated to reflect the effect of a 5-for-4 stock split in December 2006 and December 2004.

Table 2 - Selected Operating Highlights – Five-Year Comparison

| (\$ in thousands, except share data) | 2007 | 2006 | 2005 | 2004 | 2003 |
|---|-----------|-----------|-----------|-----------|-----------|
| Summary of operations | | | | | |
| Interest income - taxable equivalent | \$ 63,414 | \$ 55,347 | \$ 42,544 | \$ 28,947 | \$ 23,221 |
| Interest expense | 30,282 | 22,737 | 14,679 | 8,427 | 6,695 |
| Net interest income - taxable equivalent | 33,132 | 32,610 | 27,865 | 20,520 | 16,526 |
| Taxable equivalent adjustment | (156) | (158) | (186) | (240) | (284) |
| Net interest income | 32,976 | 32,452 | 27,679 | 20,280 | 16,242 |
| Provision for loan losses | 4,675 | 1,585 | 1,500 | 1,450 | 1,000 |
| Net interest income after provision for loan losses | 28,301 | 30,867 | 26,179 | 18,830 | 15,242 |
| Noninterest income | | | | | |
| Service charges on deposits accounts | 1,383 | 1,526 | 1,622 | 1,598 | 1,572 |
| Mortgage related income, net | 615 | 886 | 1,292 | 1,079 | 776 |
| Trust fees | 1,513 | 658 | 501 | 442 | 398 |
| Other operating income | 1,242 | 1,233 | 979 | 981 | 635 |
| Losses on sales of other real estate | (44) | - | (7) | - | - |
| Total noninterest income | 4,709 | 4,303 | 4,387 | 4,100 | 3,381 |
| Noninterest expense | | | | | |
| Salaries and employee benefits | 11,846 | 10,852 | 9,530 | 8,362 | 6,693 |
| Occupancy and equipment | 3,294 | 2,920 | 2,199 | 1,963 | 1,767 |
| Information technology | 1,616 | 1,525 | 1,244 | 1,049 | 908 |
| Other operating expense | 4,383 | 4,656 | 3,673 | 2,880 | 2,287 |
| Total noninterest expense | 21,139 | 19,953 | 16,646 | 14,254 | 11,655 |
| Income before income taxes | 11,871 | 15,217 | 13,920 | 8,676 | 6,968 |
| Income tax expense | 4,235 | 5,215 | 4,880 | 2,940 | 2,324 |
| Net income | \$ 7,636 | \$ 10,002 | \$ 9,040 | \$ 5,736 | \$ 4,644 |
| Net income per share: (a) | | | | | |
| Basic | \$ 1.31 | \$ 1.73 | \$ 1.68 | \$ 1.12 | \$ 0.91 |
| Diluted | \$ 1.29 | \$ 1.70 | \$ 1.63 | \$ 1.09 | \$ 0.89 |
| Cash dividends paid per share | \$ 0.48 | \$ 0.45 | \$ 0.43 | \$ 0.42 | \$ 0.41 |
| Average basic shares outstanding (000s) | 5,850 | 5,765 | 5,396 | 5,136 | 5,129 |
| Average diluted shares outstanding (000s) | 5,922 | 5,876 | 5,531 | 5,261 | 5,226 |
| Performance ratios (averages) | | | | | |
| Net interest margin | 3.99% | 4.44% | 4.25% | 3.86% | 3.91% |
| Return on average assets | 0.88% | 1.30% | 1.32% | 1.03% | 1.05% |
| Return on average equity | 10.68% | 16.19% | 19.06% | 15.04% | 12.99% |
| Efficiency ratio | 56.09% | 54.29% | 51.91% | 58.47% | 59.40% |

(a) Share and per share amounts have been restated to reflect the effect of a 5-for-4 stock split in December 2006 and December 2004.

Table 3 - Selected Quarterly Data

The following is a summary of unaudited quarterly results for 2007 and 2006:

| | 2007 | | | | 2006 | | | |
|---|---------|---------|---------|---------|---------|---------|---------|---------|
| | Fourth | Third | Second | First | Fourth | Third | Second | First |
| Net interest income | \$8,080 | \$8,308 | \$8,412 | \$8,176 | \$8,260 | \$8,119 | \$8,156 | \$7,917 |
| Provision for loan losses | 3,145 | 635 | 395 | 500 | 450 | 360 | 360 | 415 |
| Net interest income after provision for loan losses | 4,935 | 7,673 | 8,017 | 7,676 | 7,810 | 7,759 | 7,796 | 7,502 |
| Noninterest income | 1,493 | 1,164 | 1,000 | 1,052 | 1,090 | 1,056 | 1,086 | 1,071 |
| Noninterest expense | 5,790 | 5,176 | 5,026 | 5,147 | 5,137 | 4,945 | 4,976 | 4,895 |
| Income before income taxes | 638 | 3,661 | 3,991 | 3,581 | 3,763 | 3,870 | 3,906 | 3,678 |
| Income tax expense | 285 | 1,280 | 1,400 | 1,270 | 1,240 | 1,280 | 1,368 | 1,327 |
| Net income | \$ 353 | \$2,381 | \$2,591 | \$2,311 | \$2,523 | \$2,590 | \$2,538 | \$2,351 |
| Per share: (a) | | | | | | | | |
| Net income – basic | \$.060 | \$.406 | \$.445 | \$.400 | \$.437 | \$.450 | \$.441 | \$.408 |
| Net income – diluted | \$.059 | \$.402 | \$.439 | \$.392 | \$.429 | \$.441 | \$.432 | \$.401 |
| Dividends | \$.120 | \$.120 | \$.120 | \$.120 | \$.112 | \$.112 | \$.112 | \$.112 |
| Average shares (000s) | | | | | | | | |
| Basic | 5,923 | 5,862 | 5,824 | 5,782 | 5,779 | 5,761 | 5,759 | 5,759 |
| Diluted | 5,968 | 5,928 | 5,899 | 5,890 | 5,884 | 5,886 | 5,894 | 5,886 |

(a) Share and per share amounts have been restated to reflect the effect of a 5-for-4 stock split in December 2006. The summation of quarterly earnings per share may not agree with annual earnings per share.

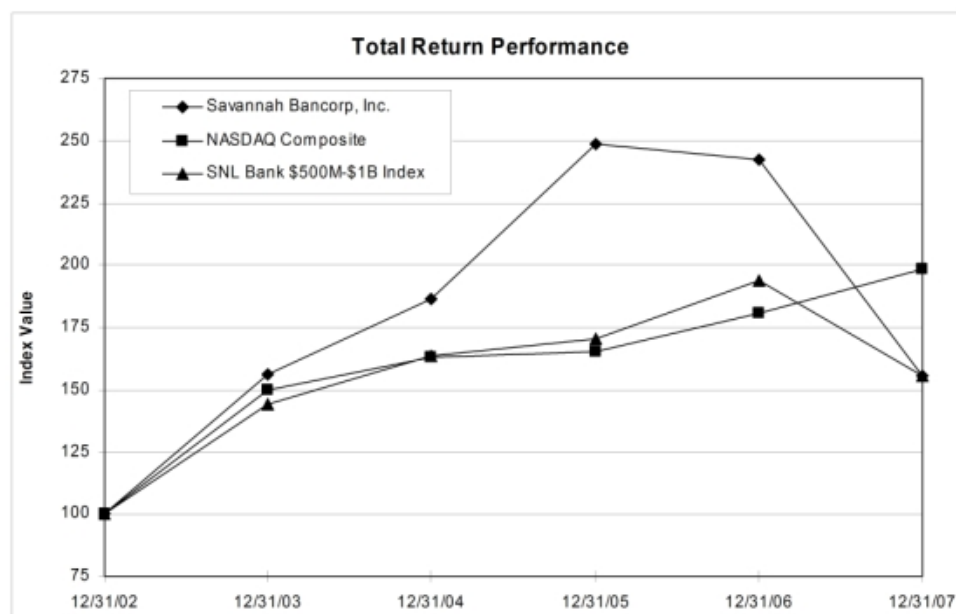
Table 4 - Market for Registrant's Common Equity and Related Shareholder Matters

The Company's common stock is traded on NASDAQ under the symbol SAVB. The quarterly high, low and closing stock trading prices for 2007 and 2006 are listed below. There were approximately 720 holders of record of Company common stock and, according to information provided to the Company, approximately 740 additional shareholders in street name through brokerage accounts at December 31, 2007. The per share amounts have been restated to reflect the effect of a 5-for-4 stock split in December 2006.

| Closing Market Prices | 2007 | | | | 2006 | | | |
|-----------------------|----------|----------|----------|----------|----------|----------|----------|----------|
| | Fourth | Third | Second | First | Fourth | Third | Second | First |
| High | \$ 24.69 | \$ 25.97 | \$ 27.20 | \$ 28.07 | \$ 28.14 | \$ 30.31 | \$ 30.40 | \$ 29.58 |
| Low | 17.10 | 23.00 | 24.71 | 27.00 | 26.60 | 26.58 | 27.26 | 27.12 |
| Close | 17.14 | 24.69 | 25.10 | 27.00 | 27.25 | 26.64 | 30.26 | 28.06 |

Table 5 - Stock Performance Graph

The following table provides a graphic comparison of the cumulative total shareholder return on the common stock of the Company for the five year period from December 31, 2002 through December 31, 2007. It includes the cumulative total return on the NASDAQ Market Index, the SNL \$500M-\$1B Bank Index and assumes the re-investment of all dividends over the same period. All cumulative returns assume an initial investment of \$100.



| For the Years Ended December 31, | | | | | | |
|----------------------------------|--------|--------|--------|--------|--------|--------|
| Index | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 |
| The Savannah Bancorp, Inc. | 100.00 | 156.28 | 186.46 | 248.79 | 242.60 | 155.59 |
| NASDAQ Composite | 100.00 | 150.01 | 162.89 | 165.13 | 180.85 | 198.60 |
| SNL \$500M-\$1B Bank Index | 100.00 | 144.19 | 163.41 | 170.41 | 193.81 | 155.31 |

Source: SNL Financial LC, Charlottesville, VA ©2008

Introduction

Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD & A") provides supplemental information which sets forth the major factors that have affected the Company's financial condition and results of operations. These discussions should be read in conjunction with the Consolidated Financial Statements and related notes. The MD & A is divided into subsections entitled:

| |
|--|
| Selected Financial Data Tables 1 - 5 (preceding pages) |
| Introduction |
| Critical Accounting Estimate |
| Results of Operations |
| Financial Condition and Capital Resources |
| Liquidity and Interest Rate Sensitivity Management |
| Off-Balance Sheet Arrangements |
| Forward Looking Statements |

These discussions should facilitate a better understanding of the major factors and trends that affect the Company's earnings performance and financial condition and how the Company's performance during 2007 compared with prior years. Throughout this section, The Savannah Bancorp, Inc. and its subsidiaries, collectively, are referred to as "SAVB" or the "Company." The Savannah Bank, N.A. is referred to as "Savannah," Bryan Bank & Trust is referred to as "Bryan" and Harbourside Community Bank is referred to as "Harbourside". Harbourside opened and began offering full service banking activities on March 1, 2006. Minis & Co., Inc. is referred to as "Minis." The operations of Minis, a registered investment advisor and wholly-owned subsidiary, are included beginning September 1, 2007. Collectively, Savannah, Bryan and Harbourside are referred to as the "Subsidiary Banks."

The averages used in this report are the averages of daily balances for each respective period. See Tables 8 and 9 for average balances and interest rates presented on an annual basis. All share and per share amounts have been restated to reflect the effect of a 5-for-4 stock split in December 2006 and December 2004. Certain prior year balances have been reclassified to conform to the current year presentation.

The Company is headquartered in Savannah, Georgia and, as of December 31, 2007, had nine banking offices and ten ATMs in Savannah and surrounding Chatham County, Richmond Hill, Georgia, Hilton Head Island and Bluffton, South Carolina. In March 2006, Harbourside opened on Hilton Head Island as a separately chartered federal savings bank. In September 2006, Savannah opened a new office adjacent to the Landings community in Savannah. In December 2007, Harbourside opened its Bluffton Parkway Office in Bluffton, South Carolina.

Savannah and Bryan are located in the relatively diverse and growing Savannah Metropolitan Statistical Area. The diversity of major employers includes manufacturing, port related transportation, construction, military, healthcare, tourism, education, warehousing and the supporting services and products for each of these major employers. The real estate market is experiencing moderate government and commercial growth and slower residential growth. Coastal Georgia and South Carolina continue to be desired retiree residential destinations.

Harbourside specifically targets real estate lending and related full service banking opportunities in the coastal South Carolina market. During 2006 and 2007, the business strategy changed resulting in a significant reduction in the sale of loans on a servicing retained basis. The change was due to the lower profit opportunity on a significantly lower volume of residential mortgage loans.

The primary risks to the Company include trends or events that would cause or result in a significant decline in local employment, real estate values, loans or core deposits. The Company operates in very competitive markets with the related challenges of competitive pricing on loans, deposits and other banking services. Competition for the best talent is also a strategic challenge faced in competitive markets.

The primary strategic objectives of the Company are growth in loans, deposits, product lines and service quality in existing markets, and quality expansion into new markets, within acceptable risk parameters, which results in enhanced shareholder

value. The Company believes that the management team and the operational and internal control infrastructure are largely in place to execute the Board of Directors' ("Board") objectives over the long term.

Critical Accounting Estimate - Allowance for Loan Losses

The Company considers its policies regarding the allowance for loan losses to be its most critical accounting estimate due to the significant degree of management judgment involved. The allowance for loan losses is established through charges to earnings in the form of a provision for loan losses based on management's continuous evaluation of the loan portfolio. Loan losses and recoveries are charged or credited directly to the allowance. The amount of the allowance reflects management's opinion of an adequate level to absorb probable losses inherent in the loan portfolio at December 31, 2007. The amount charged to the provision and the level of the allowance is based on management's judgment and is dependent upon growth in the loan portfolio, the total amount of past due loans and nonperforming loans, known loan deteriorations, and concentrations of credit. Other factors affecting the allowance include market interest rates, loan sizes, portfolio maturity and composition, collateral values and general economic conditions. Finally, management's assessment of probable losses, based upon internal credit grading of the loans and periodic reviews and assessments of credit risk associated with particular loans, is considered in establishing the allowance amount.

No assurance can be given that the Company will not sustain loan losses which would be sizable in relationship to the amount reserved or that subsequent evaluation of the loan portfolio, in light of conditions and factors then prevailing, will not require significant changes in the allowance for loan losses by future charges or credits to earnings. The allowance for loan losses is also subject to review by various regulatory agencies through their periodic examinations of the Subsidiary Banks. Such examinations could result in required changes to the allowance for loan losses. No adjustment in the allowance or significant adjustments to the Subsidiary Bank's internally classified loans were made as a result of the most recent regulatory examinations.

The allowance for loan losses totaled \$12,864,000 or 1.59 percent of total loans at December 31, 2007. This is compared to an allowance of \$8,954,000 or 1.24 percent of total loans at December 31, 2006. For 2007, the Company reported net charge-offs of \$765,000 or 0.10 percent of average loans for 2007. This is compared to net charge-offs of \$444,000 or 0.07 percent of average loans for 2006. During 2007 and 2006, provisions for loan losses of \$4,675,000 and \$1,585,000, respectively, were added to the allowance for loan losses. The fourth quarter 2007 provision for loan losses was \$3,145,000 which included approximately \$2,600,000 of additional provision due to significantly higher nonperforming loans as discussed below.

The Company's nonperforming assets consist of other real estate owned, loans on nonaccrual status and loans which are contractually past due 90 days or more on which interest is still being accrued. Nonaccrual loans of \$14,663,000 and loans past due 90 days or more of \$2,761,000 totaled \$17,424,000, or 2.15 percent of gross loans, at December 31, 2007. Nonaccrual loans of \$825,000 and loans past due 90 days or more of \$1,406,000 totaled \$2,231,000, or 0.31 percent of gross loans, at December 31, 2006. Generally, loans are placed on nonaccrual status when the collection of the principal or interest in full becomes doubtful. Nonperforming assets also included \$2,112,000 and \$545,000 of other real estate owned at December 31, 2007 and 2006, respectively.

Impaired loans under Statement of Financial Accounting Standards ("SFAS") No. 114 were all on nonaccrual status and totaled \$14,663,000 and \$825,000 at December 31, 2007 and 2006, respectively.

The \$17.4 million in nonperforming loans was primarily loans made in or related to the Bluffton/Hilton Head Island, South Carolina ("Bluffton/HHI") market and includes 49 loans. The loans consist of \$1.9 million in one nearly complete residential property, \$10.8 million in 28 completed residential properties, \$2.0 million in 10 residential lots and \$2.7 million in 10 nonresidential loans. A number of borrowers whose primary repayment sources are directly related to real estate activities have been negatively impacted by the downturn in the local real estate market, especially during the last six months of 2007.

During the fourth quarter 2007, the Company expected to successfully resolve several larger nonperforming and performing but weaker credits based on our discussions with the borrowers and other involved parties. However, the

Bluffton/HHI real estate market continued to slow during November and December and several of the larger loans moved from a current, or slightly past due status, to nonperforming status during this period. Experienced internal risk management and special asset personnel and resources were identified and given the responsibility to minimize losses during the workout and resolution of these loans.

During November and December, extensive internal loan review procedures and analyses were performed on approximately \$135 million of portfolio loans that were nearly all secured by real estate and originated in the Bluffton/HHI market. These loans include approximately \$60 million of loans in Savannah's loan portfolio. The additional fourth quarter loan loss provision of \$2.6 million was divided equally between the allowance for loan losses for Savannah and Harbourside. Fourth quarter charge-offs remained relatively low as the loans had not made it through the workout or foreclosure process.

Higher risk characteristics were identified, primarily in the speculative and non-owner occupied Bluffton/HHI residential real estate loans that were originated in 2004-2006 in a much stronger real estate market. Many of the loans are not currently delinquent or past due but are now properly graded so that the appropriate attention can be provided. Management believes that adequate provisions and allowances for loan losses have been recorded in accordance with recently expanded regulatory guidance that became effective in 2007.

If the allowance for loan losses had changed by five percent, the effect on net income would have been approximately \$396,000. If the allowance had to be increased by this amount, it would not have changed the Subsidiary Banks' status as well-capitalized financial institutions.

Changes in the allowance for loan losses from 2003 through 2007 are summarized as follows:

| (\$ in thousands) | 2007 | 2006 | 2005 | 2004 | 2003 |
|---|-----------|----------|----------|----------|----------|
| Balance at the beginning of the year | \$ 8,954 | \$ 7,813 | \$ 6,389 | \$ 5,067 | \$ 4,373 |
| Charge-offs – commercial | (150) | - | (22) | (143) | (161) |
| Charge-offs – consumer | (103) | (125) | (82) | (112) | (112) |
| Charge-offs – real estate | (621) | (381) | (41) | - | (122) |
| Charge-offs – total | (874) | (506) | (152) | (255) | (395) |
| Recoveries – commercial | 6 | 6 | 7 | 26 | 7 |
| Recoveries – consumer | 43 | 54 | 53 | 68 | 70 |
| Recoveries – real estate | 60 | 2 | 16 | 33 | 12 |
| Recoveries – total | 109 | 62 | 76 | 127 | 89 |
| Net charge-offs | (765) | (444) | (76) | (128) | (306) |
| Provision for loan losses | 4,675 | 1,585 | 1,500 | 1,450 | 1,000 |
| Balance at the end of the year | \$ 12,864 | \$ 8,954 | \$ 7,813 | \$ 6,389 | \$ 5,067 |
| Ratio of net charge-offs to average loans | 0.10% | 0.07% | 0.01% | 0.03% | 0.09% |

The allowance for loan losses is allocated by loan category based on management's assessment of risk within the various categories of loans. Loans are segregated by category and by credit risk rating within each category. The allowance for loan losses is allocated to each category by applying reserve percentages to each category. These percentages are based upon management's assessment of risk inherent within each category and the historical and anticipated loss rates within each category.

The Company's allocation of the allowance for loan losses is presented in the following table:

| (\$ in thousands) | 2007 | 2006 | 2005 | 2004 | 2003 |
|---|-----------|----------|----------|----------|----------|
| Commercial | \$ 750 | \$ 900 | \$ 700 | \$ 650 | \$ 600 |
| Real estate-construction and development | 4,150 | 4,350 | 3,750 | 2,750 | 1,650 |
| Real estate-mortgage | 6,750 | 2,350 | 1,900 | 1,750 | 1,300 |
| Consumer | 200 | 400 | 350 | 400 | 400 |
| Unallocated | 1,014 | 954 | 1,113 | 839 | 1,117 |
| Total allowance for loan losses | \$ 12,864 | \$ 8,954 | \$ 7,813 | \$ 6,389 | \$ 5,067 |

The composition of the loan portfolio as a percentage of total loans is presented below:

| Loan Categories | 2007 | 2006 | 2005 | 2004 | 2003 |
|---|--------|--------|--------|--------|--------|
| Commercial | 8.8% | 8.0% | 7.4% | 7.3% | 11.1% |
| Real estate-construction and development | 16.6 | 23.1 | 23.6 | 19.4 | 13.4 |
| Real estate-mortgage | 72.3 | 66.6 | 66.7 | 69.9 | 71.1 |
| Consumer | 2.3 | 2.3 | 2.3 | 3.4 | 4.4 |
| Total loans | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% |

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Results of Operations

2007 Compared with 2006

Net income for 2007 was \$7,636,000, a decrease of 24 percent from \$10,002,000 in 2006. Net income per diluted share was \$1.29 and \$1.70 in 2007 and 2006, respectively. Higher interest income resulting from solid growth in interest-earning assets was offset by higher interest expense on interest-bearing liabilities and a much higher provision for loan losses as discussed in the previous section. Return on average equity was 10.68 percent, return on average assets was 0.88 percent and the efficiency ratio was 56.09 percent in 2007.

Average interest-earning assets increased 13 percent to \$831 million in 2007 from \$734 million in 2006. Net interest income was \$32,976,000 in 2007 compared to \$32,452,000 in 2006, an increase of \$524,000 or 1.6 percent. Average loans were \$754 million for 2007, 14 percent higher when compared to \$659 million in 2006. The net interest margin decreased to 3.99 percent in 2007 from 4.44 percent in 2006. As shown in Table 8, the decline in net interest margin was primarily due to the rise in deposit and other borrowing costs over the prior 12 months and changes in the deposit mix. The increase in the yield on interest-earning assets was more than offset by increasing costs of interest-bearing liabilities. As shown in Table 7, the Company's balance sheet is asset-sensitive since the interest-earning assets reprice faster than interest-bearing liabilities. Rising interest rates favorably impact the net interest margin of an asset-sensitive balance sheet and falling rates adversely impact the net interest margin. However, when the prime rate stops decreasing, the interest rates on time deposits, certain non-maturity deposits and other funding sources will continue to decline due to the re-pricing lag associated with those liabilities.

The provision for loan losses was \$4,675,000 for 2007, compared to \$1,585,000 for 2006. Changes in the provision are impacted as discussed in detail under the "Allowance for Loan Losses" section above. Loan growth was \$88 million in 2007, primarily in real estate-secured loans, compared to \$107 million in 2006. The higher provision for loan losses in 2007 as compared to 2006 is attributable to significantly higher nonperforming loans resulting from a weaker overall real estate market, higher interest rates and much tighter availability of funding for larger residential real estate loans.

Noninterest income was \$4,709,000 in 2007 compared to \$4,303,000 in 2006, an increase of \$406,000, or 9.4 percent. Trust and investment management fees were \$855,000 higher, but were offset by lower mortgage related income and service charges on deposit accounts. Mortgage banking related income, net of direct origination costs, was \$615,000 in 2007 compared to \$886,000 for the same period in 2006, a decrease of \$271,000 or 31 percent. The mortgage related income was impacted negatively by lower mortgage origination volumes resulting from slowing residential real estate sales, higher credit standards in the secondary market for borrowers and higher mortgage loan rates, particularly on larger loans.

Noninterest expense was \$21,139,000 in 2007 compared to \$19,953,000 in 2006, an increase of \$1,186,000, or 5.9 percent. The increase included four months of Minis & Co., Inc. expenses of \$455,000 in 2007. Salaries and employee benefits increased \$994,000 or 9.2 percent. Occupancy, equipment and information technology expenses increased approximately \$465,000, or 11 percent. Other operating expense decreased \$273,000, or 5.9 percent, primarily due to nonrecurring pre-opening expenses related to the opening of Harbourside in 2006 and nonrecurring first year Sarbanes-Oxley costs incurred in the first quarter 2006.

Income tax expense was \$4,235,000 in 2007 and \$5,215,000 in 2006. The combined effective federal and state tax rates were 35.7 percent and 34.3 percent in 2007 and 2006, respectively. The increase was primarily due to lower tax-exempt income for state tax purposes in 2007 and tax benefits related to the exercise and sale of incentive stock options in 2006. The Company has never recorded a valuation allowance against deferred tax assets. All significant deferred tax assets are considered to be realizable due to expected future taxable income.

2006 Compared with 2005

Net income in 2006 was \$10,002,000, up 11 percent from \$9,040,000 in 2005. Net income per diluted share was \$1.70 in 2006 compared to \$1.63 per share in 2005, an increase of 4.3 percent. The earnings increase is primarily attributable to growth in interest-earning assets and a higher net interest margin partially offset by higher expenses and lower noninterest income. Net income for 2006 includes after tax stock-based compensation expense of \$191,000 or \$0.03 per diluted share in 2006 and none in 2005. Average outstanding diluted shares increased 345,000, or 6.2 percent, in 2006 compared with 2005. The increase in average shares outstanding resulted from the private placement sale of 397,000 shares in August 2005 and additional shares being issued upon exercise of stock options. Return on average equity was 16.19 percent and return on average assets was 1.30 percent. The efficiency ratio was 54.29 percent in 2006. Prior period per share amounts have been restated to reflect the effect of a 5-for-4 stock split in December 2006.

Average interest-earning assets for 2006 increased 12 percent to \$734 million in 2006 from \$656 million in 2005. Net interest income was \$32,452,000 in 2006 compared to \$27,679,000 in 2005, an increase of \$4,773,000 or 17 percent. Average loans were \$659 million in 2006, 17 percent higher when compared to \$565 million in 2005. The net interest margin increased to 4.44 percent in 2006 from 4.25 percent in 2005. As shown in Table 9, the increase in the net interest margin was primarily due to the rise in loan rates and increases in equity and noninterest-bearing deposits.

The provision for loan losses was \$1,585,000 for 2006, compared to \$1,500,000 in 2005. Loan growth was \$107 million in 2006, primarily in real estate-secured loans, compared to \$114 million in loan growth in 2005. Net charge-offs of \$444,000 in 2006 as compared to \$76,000 in 2005 are the primary reason for the higher provision for loan losses in 2006.

Noninterest income was \$4,303,000 in 2006 compared to \$4,387,000 in 2005, a decrease of \$84,000 or 1.9 percent. The decrease was a result of lower mortgage related income and service charges on deposit accounts offset by higher trust fees and other operating income. Noninterest income included mortgage banking related income, net of direct production costs, of \$886,000 in 2006 compared to \$1,292,000 in 2005, a decrease of \$406,000 or 31 percent. Net mortgage related income declined because of lower mortgage origination volume due to higher interest rates, personnel turnover at Harbourside and a decline in residential real estate market activity. No market valuation adjustments were required for loans held for sale during 2006. Service charges on deposit accounts declined 5.9 percent or \$96,000, primarily because of higher earnings credits on commercial checking accounts due to increases in the 90-day Treasury interest rate.

Noninterest expense was \$19,953,000 in 2006 compared to \$16,646,000 in 2005, an increase of \$3,307,000, or 20 percent. The increase in overall noninterest expense included normal operating cost increases, approximately \$263,000 non-recurring startup costs at Harbourside, approximately \$1,000,000 of increased operating costs for the Harbourside expansion and \$299,000 of stock-based compensation expense resulting from adopting SFAS No. 123R effective January 1, 2006. Salaries and benefits increased \$1,322,000 or 14 percent, and included \$200,000 of stock-based compensation expense. In addition to normal salary increases, the personnel cost increases included additional staff in credit administration, accounting, internal audit and at Harbourside. Occupancy, equipment and information technology expenses increased approximately \$1,002,000, or 29 percent, primarily due to the Harbourside expansion, enhancements to systems capabilities and account / transaction volume increases. Other operating expense increased \$983,000 or 27 percent and included additional costs related to the Harbourside expansion, higher audit, advertising and professional fees, \$99,000 in stock-based compensation expense for directors and various other expenses.

Income tax expense was \$5,215,000 in 2006 and \$4,880,000 in 2005. The combined effective federal and state tax rates were 34.3 percent and 35.1 percent in 2006 and 2005, respectively. The decline is primarily due to additional low income housing tax credits added in mid-2005. The Company has never recorded a valuation allowance against deferred tax assets. All deferred tax assets are considered to be realizable due to expected future taxable income.

Financial Condition and Capital Resources

Balance Sheet Activity

The major changes in the Company's assets and liabilities for the current and prior period are shown in the consolidated statements of cash flows. Average total assets increased 13 percent to \$869 million in 2007 from \$770 million in 2006. Total assets were \$932 million and \$844 million at December 31, 2007 and 2006, respectively, an increase of 10 percent. The increase in loans of \$88 million in 2007 was funded primarily by \$57 million in deposit growth and \$30 million in additional short-term borrowings.

The Company has classified all investment securities as available for sale. Lower short-term interest rates resulted in an overall net unrealized gain in the investment portfolio. The unrealized gain or loss amounts are recorded in shareholders' equity as accumulated other comprehensive income (loss), net of tax.

The Harbourside expansion impacts the funding sources, capital requirements and liquidity of the Company. Historically, deposits at the Subsidiary Banks have been obtained from local customers, but funding sources have been expanded to include non-local deposits and more frequent use of short-term advances from the FHLB. Total deposits included brokered time deposits and institutional money market accounts of \$127 million at December 31, 2007 and \$111 million at December 31, 2006.

Loans

The following table shows the composition of the loan portfolio at December 31, 2007 and 2006, including a more detailed breakdown of real estate secured loans by collateral type and purpose. Certain prior year balances have been reclassified to conform to the current year presentation.

Table 6 - Loan Concentrations

| (\$ in thousands) | 2007 | % of Total | 2006 | % of Total | % Change (\$) |
|--------------------------------------|------------|---------------|------------|---------------|---------------|
| Non-residential real estate | | | | | |
| Owner-occupied | \$ 118,714 | 15 | \$ 90,848 | 13 | 31 |
| Non owner-occupied | 118,904 | 15 | 98,032 | 14 | 21 |
| Construction | 33,923 | 4 | 22,128 | 3 | 53 |
| Commercial land and lot development | 38,127 | 5 | 35,610 | 5 | 7 |
| Total non-residential real estate | 309,668 | 39 | 246,618 | 35 | 26 |
| Residential real estate | | | | | |
| Owner-occupied – 1-4 family | 83,828 | 10 | 87,965 | 12 | 5 |
| Non owner-occupied – 1-4 family | 114,992 | 14 | 68,397 | 10 | 68 |
| Construction | 57,541 | 7 | 110,412 | 15 | (48) |
| Residential land and lot development | 109,718 | 14 | 93,060 | 12 | 18 |
| Home equity lines | 43,322 | 5 | 40,794 | 6 | 6 |
| Total residential real estate | 409,401 | 50 | 400,628 | 55 | 2 |
| Total real estate loans | 719,069 | 89 | 647,246 | 90 | 11 |
| Commercial | 71,370 | 9 | 57,737 | 8 | 24 |
| Consumer | 18,692 | 2 | 16,628 | 2 | 12 |
| Unearned fees, net | (480) | - | (693) | - | (31) |
| Total loans, net of unearned fees | \$ 808,651 | 100 | \$ 720,918 | 100 | 12 |

Capital Resources

The Office of the Comptroller of the Currency and Office of Thrift Supervision have adopted capital requirements that specify the minimum capital level for which no prompt corrective action is required. In addition, the FDIC assesses FDIC insurance premiums based on certain “well-capitalized” risk-based and equity capital ratios. As of December 31, 2007, the Subsidiary Banks and the Company exceeded the minimum requirements necessary to be classified as “well-capitalized.”

Total equity capital for the Company was \$76.3 million, or 8.18 percent of total assets, at December 31, 2007. Tier 1 capital was 10.49 percent of risk-weighted assets at the same date. Tier 1 capital at December 31, 2007 includes \$10.0 million of trust preferred debt issued by the Company’s nonconsolidated subsidiaries.

Under Federal Reserve Bank holding company capital regulations, trust preferred debt qualifies for Tier 1 capital treatment up to a limit of 25 percent of tangible equity capital plus trust preferred debt. All of the Company’s trust preferred debt qualifies as Tier 1 capital. At December 31, 2007, the Company has the capacity to issue approximately \$14 million in additional qualifying trust preferred debt which would qualify as Tier 1 capital.

The Company has a \$5,000,000 line of credit through a correspondent bank, of which none was advanced at December 31, 2007. The primary purpose of the line is to provide access to funds that can be used for short-term corporate needs. The borrowing facility is available through September 20, 2008 at which time any outstanding indebtedness is due and payable in full. Advances on the line are subject to the Company certifying compliance with covenants and conditions specified in the agreement. The covenants include customary performance items and a negative pledge agreement on the stock of Savannah. The Company may not pledge the stock of Savannah for any other indebtedness or purpose without the express written consent of the lender.

Liquidity and Interest Rate Sensitivity Management

The objectives of balance sheet management include maintaining adequate liquidity and preserving reasonable balance between the repricing of interest sensitive assets and liabilities at favorable interest rate spreads. The objective of liquidity management is to ensure the availability of adequate funds to meet the loan demands and the deposit withdrawal needs of customers. This is achieved through maintaining a combination of sufficient liquid assets, core deposit growth and unused capacity to purchase and borrow funds in the money markets.

During 2007, portfolio loans increased \$88 million to \$809 million and deposits increased \$57 million to \$764 million. The loan to deposit ratio was 106 and 102 percent at December 31, 2007 and 2006, respectively. Average loan growth in 2007 was 15 percent. Average deposit growth in 2007 was 13 percent.

In addition to local deposit growth, primary funding and liquidity sources include borrowing capacity with the FHLB, temporary federal funds purchased lines with correspondent banks and non-local institutional and brokered deposits. Contingency funding and liquidity sources include the ability to sell loans, or participations in certain loans, to investors and borrowings from the Federal Reserve Bank of Atlanta (“FRB”) discount window.

The Subsidiary Banks have Blanket Floating Lien Agreements with the FHLB. Under these agreements, the Subsidiary Banks have credit lines up to 80 percent of the FHLB qualifying collateral value of their 1-4 family first mortgage loans and up to 50 percent of the FHLB qualifying collateral value of their home equity lines of credit and second mortgage residential loans. The Subsidiary Banks individual borrowing limits range from 10 to 25 percent of assets. In aggregate, the Subsidiary Banks had secured borrowing capacity of approximately \$131.5 million of which \$53.0 million was advanced at December 31, 2007. These credit arrangements serve as a core funding source as well as liquidity backup for the Subsidiary Banks. The Subsidiary Banks also have conditional federal funds borrowing lines available from correspondent banks that management believes can provide up to \$20 million of funding needs for 30-60 days. Savannah and Bryan have been approved to access the FRB discount window to borrow on a secured basis at 100 basis points over the Federal Funds Target Rate. The amount of credit available is subject to the amounts and types of collateral available when borrowings are requested.

A continuing objective of interest rate sensitivity management is to maintain appropriate levels of variable rate assets, including variable rate loans and shorter maturity investments, relative to interest rate sensitive liabilities, in order to control potential negative impacts upon earnings due to changes in interest rates. Interest rate sensitivity management requires analyses and actions that take into consideration volumes of assets and liabilities repricing and the timing and magnitude of their price changes to determine the effect upon net interest income. The Company utilizes hedging strategies to reduce interest rate risk as noted below.

The Company's cash flow, maturity and repricing gap at December 31, 2007 was \$61 million at one year, or 6.9 percent of total interest-earning assets. At December 31, 2006 the gap at one year was \$81 million, or 10 percent of total interest-earning assets. Interest-earning assets with maturities over five years totaled approximately \$49.9 million, or 5.7 percent of total interest-earning assets. See Table 7 for cash flow, maturity and repricing gap. The gap position between one and five years is of less concern because management has time to respond to changing financial conditions and interest rates with actions that reduce the impact of the longer-term gap positions on net interest income. However, interest-earning assets with maturities and/or repricing dates over five years may include significant rate risk and market value of equity concerns in the event of significant interest rate increases.

The Company is asset-sensitive within one year. The decreases in the prime rate from 8.25 percent to 7.25 percent during the latter part of 2007 and the level of nonaccrual loans have negatively impacted net interest income and net interest margin. Increased funding costs more than offset the overall increases in interest-earning assets resulting in net interest margin compression in 2007.

Since June 2005, the Company has implemented various strategies to reduce the Company's asset-sensitive position, primarily through the use of short maturity funding sources and hedging strategies such as interest rate floors, collars and swaps. During 2005, Savannah entered into a five year prime rate-based floor transaction with a notional amount of \$35 million and a 6 percent strike rate. Also in 2005, Savannah and Bryan entered into a five year prime rate-based collar with a notional amount of \$40 million that includes a 6 percent floor and 9 percent cap rate and a \$50 million interest rate swap, fully hedged by floating rate loans, in which they receive 7.645 percent fixed rate and pay a variable rate at the prime rate. In 2008 the Company terminated \$25 million of their interest rate swap position for a gain of \$966,000 which will be amortized into interest income on a straight-line basis over the remaining life of the swap. These actions have reduced the Company's exposure to falling interest rates.

Management monitors interest rate risk quarterly using rate-sensitivity forecasting models and other balance sheet analytical reports. If and when projected interest rate risk exposures are outside of policy tolerances or desired positions, specific strategies to return interest rate risk exposures to desired levels are developed by management, approved by the Asset-Liability Committee and reported to the Board. Management upgraded its interest rate risk reporting systems by engaging outside balance sheet consultants during the second quarter of 2005. Better forecasting models are especially valuable during periods of volatile interest rates, rapid growth and changing interest rate yield curves.

Off-Balance Sheet Arrangements

In order to meet the financing needs of its customers, the Company is a party to financial instruments with off-balance sheet risks in the normal course of business. At December 31, 2007, the Company had unfunded commitments to extend credit of \$136 million and outstanding stand-by letters of credit of \$7.9 million. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company uses the same credit policies in establishing commitments and issuing letters of credit as it does for on-balance sheet instruments. Management does not anticipate that funding obligations arising from these financial instruments will adversely impact its ability to fund future loan growth or deposit withdrawals.

Forward Looking Statements

This MD & A and other Company communications and statements may contain "forward-looking statements." These forward-looking statements may include, among others, statements about our beliefs, plans, objectives, goals, expectations, estimates and intentions that are subject to significant risks and uncertainties and which may change based on various factors, many of which are beyond our control. The words "may," "could," "should," "would," "believe," "anticipate," "estimate," "expect," "intend," "plan" and similar expressions are intended to identify forward-looking statements. The following factors, among others, could cause our financial performance to differ materially from what is contemplated in those forward-looking statements:

- * The strength of the United States economy in general and the strength of the local economies in which we conduct operations may be different than expected resulting in, among other things, a deterioration in credit quality or a reduced demand for credit, including the resultant effect on our loan portfolio and allowance for loan losses;
- * The effects of and changes in trade, monetary and fiscal policies and laws, including interest rate policies of the Board of Governors of the Federal Reserve System;
- * Inflation, interest rate, market and monetary fluctuations;
- * Adverse conditions in the stock market and other capital markets and the impact of those conditions on our capital markets and capital management activities, including our investment and wealth management advisory businesses;
- * Changes in the cost and availability of funding due to changes in the deposit market and credit market, or the way in which the Company is perceived in such markets;
- * The effects of harsh weather conditions, including hurricanes;
- * Changes in U.S. foreign or military policy;
- * The timely development of competitive new products and services by us and the acceptance of those products and services by new and existing customers;
- * The willingness of customers to accept third-party products marketed by us;
- * The willingness of customers to substitute competitors' products and services for our products and services and vice versa;
- * The impact of changes in financial services laws and regulations (including laws concerning taxes, banking, securities and insurance);
- * Technological changes;
- * Changes in consumer spending and saving habits;
- * The effect of corporate restructuring, acquisitions or dispositions, including the actual restructuring and other related charges and the failure to achieve the expected gains, revenue growth or expense savings from such corporate restructuring, acquisitions or dispositions;
- * The growth and profitability of our noninterest or fee income being less than expected;
- * Unanticipated regulatory or judicial proceedings;
- * The impact of changes in accounting policies by the SEC or the Financial Accounting Standards Board;
- * The limited trading activity or our common stock;
- * The effects of our lack of a diversified loan portfolio, including the risks of geographic concentrations;
- * Adverse changes in the financial performance and/or condition of our borrowers, which could impact the repayment of those borrowers' outstanding loans; and
- * Our success at managing the risks involved in the foregoing.

We caution that the foregoing list of important factors is not exhaustive. Also, we do not undertake to update any forward-looking statements, whether written or oral, that may be made from time to time by us or on our behalf except as may be required by our disclosure obligations in filings we make with the SEC under federal securities laws.

Table 7 - Cash Flow/Maturity Gap and Repricing Data

The following is the cash flow/maturity and repricing data for the Company as of December 31, 2007:

| (\$ in thousands) | Immediate | 0 - 3 Months | 3 - 12 Months | 1 - 3 Years | 3 - 5 Years | Over 5 Years | Total |
|---|--------------------|-------------------|------------------|-------------------|-------------------|-------------------|-------------------|
| Interest-earning assets | | | | | | | |
| Investment securities | \$ - | \$ 6,957 | \$ 8,500 | \$ 20,090 | \$ 9,047 | \$ 15,647 | \$ 60,241 |
| Interest-bearing deposits | 20,148 | - | - | - | - | - | 20,148 |
| Federal funds sold | 4,435 | - | - | - | - | - | 4,435 |
| Loans held for sale | - | 180 | - | - | - | - | 180 |
| Loans - fixed rates | - | 51,274 | 134,338 | 152,902 | 35,659 | 32,525 | 406,698 |
| Loans - variable rates | - | 358,679 | 12,744 | 5,447 | 8,723 | 1,697 | 387,290 |
| Total interest-earning assets | 24,583 | 417,090 | 155,582 | 178,439 | 53,429 | 49,869 | 878,992 |
| Interest-bearing liabilities | | | | | | | |
| NOW and savings ** | - | 7,203 | 14,407 | 36,018 | 43,221 | 43,221 | 144,070 |
| Money market accounts ** | - | 66,749 | 45,240 | 25,851 | 38,775 | - | 176,615 |
| Time deposits | - | 138,894 | 180,798 | 27,642 | 7,461 | 235 | 355,030 |
| Short-term borrowings | 51,857 | 18,742 | - | - | - | - | 70,599 |
| FHLB advances - long-term | - | 1,078 | 676 | 1,062 | 11 | 146 | 2,973 |
| Subordinated debt | - | 10,310 | - | - | - | - | 10,310 |
| Total interest-bearing liabilities | 51,857 | 242,976 | 241,121 | 90,573 | 89,468 | 43,602 | 759,597 |
| GAP-Excess assets (liabilities) | (27,274) | 174,114 | (85,539) | 87,866 | (36,039) | 6,267 | 119,395 |
| GAP-Cumulative | \$ (27,274) | \$ 146,840 | \$ 61,301 | \$ 149,167 | \$ 113,128 | \$ 119,395 | \$ 119,395 |
| Cumulative sensitivity ratio * | 0.47 | 1.50 | 1.11 | 1.24 | 1.16 | 1.16 | 1.16 |

* Cumulative interest-earning assets / cumulative interest-bearing liabilities

** Repricing of NOW, savings and money market accounts based on estimated percentages of market interest rate changes.

Note – At December 31, 2007 the Company had unfunded loan commitments and unfunded lines of credit totaling \$136 million. The Company believes the likelihood of these commitments either being totally funded or funded at the same time is low. However, should a significant funding requirement occur, the Company has available borrowing capacity from the FHLB of \$78 million. Additionally, further sources of funding include brokered time deposits and certain other non-local deposits.

Table 8 - Average Balance Sheet and Rate/Volume Analysis - 2007 and 2006

The following table presents average balances of the Company and the Subsidiary Banks on a consolidated basis, the taxable-equivalent interest earned and the rate paid thereon during 2007 and 2006.

| Average Balance | | Average Rate | | | Taxable-Equivalent Interest (b) | | Variance | (a) Variance Attributable to | |
|------------------------------------|-----------|--------------|------|---------------------------------|---------------------------------|-----------|----------|------------------------------|----------|
| 2007 | 2006 | 2007 | 2006 | | 2007 | 2006 | | Rate | Volume |
| (\$ in thousands) | | (%) | | | (\$ in thousands) | | | (\$ in thousands) | |
| Assets | | | | | | | | | |
| \$ 6,958 | \$ 5,969 | 4.97 | 4.91 | Interest-bearing deposits | \$ 346 | \$ 293 | \$ 53 | \$ 4 | \$ 49 |
| 56,851 | 48,190 | 5.01 | 4.47 | Investments - taxable | 2,848 | 2,153 | 695 | 260 | 435 |
| 2,059 | 2,410 | 7.33 | 7.47 | Investments - non-taxable | 151 | 180 | (29) | (3) | (26) |
| 9,243 | 11,309 | 5.11 | 4.93 | Federal funds sold | 472 | 557 | (85) | 20 | (105) |
| 1,299 | 7,842 | 7.54 | 7.12 | Loans held for sale | 98 | 558 | (460) | 33 | (493) |
| 754,490 | 658,750 | 7.89 | 7.83 | Loans (c) | 59,499 | 51,606 | 7,893 | 395 | 7,498 |
| 830,900 | 734,470 | 7.63 | 7.54 | Total interest-earning assets | 63,414 | 55,347 | 8,067 | 661 | 7,406 |
| 38,126 | 35,447 | | | Noninterest-earning assets | | | | | |
| \$869,026 | \$769,917 | | | Total assets | | | | | |
| Liabilities and equity | | | | | | | | | |
| Deposits | | | | | | | | | |
| \$114,053 | \$ 95,138 | 2.00 | 1.32 | NOW accounts | 2,279 | 1,254 | 1,025 | 647 | 378 |
| 17,831 | 19,104 | 0.99 | 0.99 | Savings accounts | 176 | 190 | (14) | - | (14) |
| 167,887 | 135,736 | 4.27 | 3.75 | Money market accounts | 7,164 | 5,093 | 2,071 | 706 | 1,365 |
| 131,553 | 105,220 | 5.35 | 4.68 | CDs, \$100M or more | 7,020 | 4,927 | 2,093 | 694 | 1,399 |
| 74,234 | 81,084 | 4.83 | 3.98 | CDs, broker | 3,605 | 3,225 | 380 | 714 | (334) |
| 122,752 | 106,093 | 5.03 | 4.39 | Other time deposits | 6,171 | 4,653 | 1,518 | 679 | 839 |
| 628,310 | 542,375 | 4.20 | 3.57 | Total interest-bearing deposits | 26,415 | 19,342 | 7,073 | 3,417 | 3,656 |
| 7,833 | 15,770 | 5.27 | 4.93 | FHLB advances – long-term | 413 | 778 | (365) | 54 | (419) |
| 52,796 | 36,175 | 4.95 | 4.98 | Short-term borrowings | 2,612 | 1,802 | 810 | (11) | 821 |
| 10,310 | 10,310 | 8.17 | 7.90 | Subordinated debt | 842 | 815 | 27 | 28 | (1) |
| Total interest-bearing liabilities | | | | | | | | | |
| 699,249 | 604,630 | 4.33 | 3.76 | | 30,282 | 22,737 | 7,545 | 3,446 | 4,099 |
| 91,367 | 96,113 | | | Noninterest-bearing deposits | | | | | |
| 6,894 | 7,408 | | | Other liabilities | | | | | |
| 71,516 | 61,766 | | | Shareholders' equity | | | | | |
| \$869,026 | \$769,917 | | | Liabilities and equity | | | | | |
| | | 3.30 | 3.78 | Interest rate spread | | | | | |
| | | 3.99 | 4.44 | Net interest margin | | | | | |
| | | | | Net interest income | \$ 33,132 | \$ 32,611 | \$ 522 | \$(2,785) | \$ 3,300 |
| \$131,651 | \$129,840 | | | Net earning assets | | | | | |
| \$719,677 | \$638,488 | | | Average deposits | | | | | |
| | | 3.67 | 3.03 | Average cost of deposits | | | | | |
| 105% | 103% | | | Average loan to deposit ratio | | | | | |

(a) This table shows the changes in interest income and interest expense for the 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 rate changes or solely due to volume changes are attributed to volume.

(b) The taxable equivalent adjustment of \$156 in 2007 and \$158 in 2006 results from tax exempt income less non-deductible TEFRA interest expense.

(c) Average nonaccruing loans have been excluded from total average loans and included in noninterest-earning assets.

Table 9 - Average Balance Sheet and Rate/Volume Analysis - 2006 and 2005

The following table presents average balances of the Company and the Subsidiary Banks on a consolidated basis, the taxable-equivalent interest earned and the rate paid thereon during 2006 and 2005.

| Average Balance | | Average Rate | | | Taxable-Equivalent Interest (b) | | Variance | (a) Variance Attributable to | |
|------------------------------------|-----------|--------------|------|---------------------------------|---------------------------------|-----------|----------|------------------------------|----------|
| 2006 | 2005 | 2006 | 2005 | | 2006 | 2005 | | Rate | Volume |
| (\$ in thousands) | | (%) | | | (\$ in thousands) | | | (\$ in thousands) | |
| Assets | | | | | | | | | |
| \$ 5,969 | \$ 14,747 | 4.91 | 3.21 | Interest-bearing deposits | \$ 293 | \$ 473 | \$ (180) | \$ 251 | \$ (431) |
| 48,190 | 36,999 | 4.47 | 4.02 | Investments - taxable | 2,153 | 1,489 | 664 | 166 | 498 |
| 2,410 | 4,301 | 7.47 | 6.93 | Investments - non-taxable | 180 | 298 | (118) | 23 | (141) |
| 11,309 | 11,421 | 4.93 | 3.29 | Federal funds sold | 557 | 376 | 181 | 187 | (6) |
| 7,842 | 23,033 | 7.12 | 5.80 | Loans held for sale | 558 | 1,335 | (777) | 304 | (1,081) |
| 658,750 | 565,131 | 7.83 | 6.83 | Loans (c) | 51,606 | 38,573 | 13,033 | 5,651 | 7,382 |
| 734,470 | 655,632 | 7.54 | 6.49 | Total interest-earning assets | 55,347 | 42,544 | 12,803 | 6,884 | 5,919 |
| 35,447 | 29,531 | | | Noninterest-earning assets | | | | | |
| \$769,917 | \$685,163 | | | Total assets | | | | | |
| Liabilities and equity | | | | | | | | | |
| Deposits | | | | | | | | | |
| \$ 95,138 | \$ 89,963 | 1.32 | 0.77 | NOW accounts | 1,254 | 697 | 557 | 495 | 62 |
| 19,104 | 20,020 | 0.99 | 0.93 | Savings accounts | 190 | 187 | 3 | 12 | (9) |
| 135,736 | 104,023 | 3.75 | 2.35 | Money market accounts | 5,093 | 2,443 | 2,650 | 1,456 | 1,194 |
| 105,220 | 76,661 | 4.68 | 3.45 | CDs, \$100M or more | 4,927 | 2,642 | 2,285 | 943 | 1,342 |
| 81,084 | 112,347 | 3.98 | 3.24 | CDs, broker | 3,225 | 3,640 | (415) | 831 | (1,246) |
| 106,093 | 84,479 | 4.39 | 3.27 | Other time deposits | 4,653 | 2,764 | 1,889 | 946 | 943 |
| 542,375 | 487,493 | 3.57 | 2.54 | Total interest-bearing deposits | 19,342 | 12,373 | 6,969 | 5,021 | 1,948 |
| 15,770 | 20,669 | 4.93 | 4.88 | FHLB advances – long-term | 778 | 1,009 | (231) | 10 | (241) |
| 36,175 | 24,276 | 4.98 | 2.78 | Short-term borrowings | 1,802 | 675 | 1,127 | 534 | 593 |
| 10,310 | 10,310 | 7.90 | 6.03 | Subordinated debt | 815 | 622 | 193 | 193 | - |
| Total interest-bearing liabilities | | | | | 22,737 | 14,679 | 8,058 | 5,753 | 2,305 |
| 604,630 | 542,748 | 3.76 | 2.70 | Noninterest-bearing deposits | | | | | |
| 96,113 | 89,386 | | | Other liabilities | | | | | |
| 7,408 | 5,601 | | | Shareholders' equity | | | | | |
| 61,766 | 47,428 | | | Liabilities and equity | | | | | |
| \$769,917 | \$685,163 | | | Interest rate spread | | | | | |
| | | 3.78 | 3.79 | Net interest margin | | | | | |
| | | 4.44 | 4.25 | Net interest income | \$ 32,610 | \$ 27,861 | \$ 4,745 | \$ 1,131 | \$ 3,614 |
| \$129,840 | \$112,884 | | | Net earning assets | | | | | |
| \$638,488 | \$576,879 | | | Average deposits | | | | | |
| | | 3.03 | 2.14 | Average cost of deposits | | | | | |
| 103% | 98% | | | Average loan to deposit ratio | | | | | |

(a) This table shows the changes in interest income and interest expense for the 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 rate changes or solely due to volume changes are attributed to volume.

(b) The taxable equivalent adjustment of \$158 in 2006 and \$186 in 2005 results from tax exempt income less non-deductible TEFRA interest expense.

(c) Average nonaccruing loans have been excluded from total average loans and included in noninterest-earning assets.

Subsidiaries of Registrant

| <u>Name</u> | <u>State of Incorporation</u> |
|---|----------------------------------|
| The Savannah Bank, National Association | United States (National Charter) |
| Bryan Bank & Trust | Georgia |
| Harbourside Community Bank | United States (Thrift Charter) |
| Minis & Co, Inc. | Georgia |
| Nonconsolidated subsidiaries: | |
| SAVB Properties, LLC | Georgia |
| SAVB Capital Trust 1 | Delaware |
| SAVB Capital Trust 2 | Delaware |

Consent of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders
of The Savannah Bancorp, Inc.

We hereby consent to the incorporation by reference in the Registration Statements on Form S-3 (No. 333-146547) and Form S-8 (No. 333-69175) of The Savannah Bancorp, Inc. of our report dated March 10, 2008, relating to the consolidated financial statements as of December 31, 2007 and for the year then ended, which appear in the Annual Report to Shareholders, which is incorporated by reference in this Annual Report on Form 10-K.

/s/ Mauldin & Jenkins, LLC

Albany, Georgia
March 10, 2008

Consent of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders
of The Savannah Bancorp, Inc.

We hereby consent to the incorporation by reference in the Registration Statements on Form S-3 (No. 333-146547) and Form S-8 (No. 333-69175) of The Savannah Bancorp, Inc. of our report dated March 8, 2007, relating to the consolidated financial statements as of December 31, 2006 and for the two years then ended, which appear in the Annual Report to Shareholders, which is incorporated by reference in this Annual Report on Form 10-K.

/s/ BDO Seidman, LLP

Atlanta, Georgia
March 10, 2008

Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, John C. Helmken II, certify that:

1. I have reviewed this annual report on Form 10-K of The Savannah Bancorp, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal controls over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal controls over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 14, 2008 /s/ John C. Helmken II
John C. Helmken II
President and Chief Executive Officer

Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Robert B. Briscoe, certify that:

1. I have reviewed this annual report on Form 10-K of The Savannah Bancorp, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal controls over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal controls over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 14, 2008 /s/ Robert B. Briscoe

Robert B. Briscoe
Chief Financial Officer

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Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

We certify, pursuant to 18 U.S.C. Section 1350, as adopted by Section 906 of the Sarbanes-Oxley Act of 2002 that:

- (1) the Annual Report on Form 10-K of the Company for the year ended December 31, 2007 (the "Report") of The Savannah Bancorp, Inc. (the "Company") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: 3/14/08

/s/ John C. Helmken II
John C. Helmken II
President and Chief Executive Officer
(Principal Executive Officer)

Date: 3/14/08

/s/ Robert B. Briscoe
Robert B. Briscoe
Chief Financial Officer
(Principal Financial and Accounting Officer)