

Featured Products & Services

Free Checking

Regardless of your age, First South Bank offers free checking. With any free checking account you can enjoy the luxury of unlimited check writing, no monthly service charges, and free withdrawals at all FSB ATMs. Some of our free checking accounts also provide you with free personalized checks. All FSB checking customers receive a VISA debit card that can be used at ATMs and at most VISA retailers for point of sale purchases. Personal online banking and bill payment are also available to free checking customers absolutely free. Stop by and talk to a FSB representative today.

Individual Retirement Accounts

One of the most effective ways to accumulate retirement savings is through an Individual Retirement Account. Regardless of whether you are looking at a Traditional IRA or a Roth IRA, both can provide you with tax-advantaged savings. Contributing to an IRA can help you fulfill your financial plans. If you are 50 or above, there are some "catch-up provisions" available that may allow you to make increased contributions. Consider talking with a FSB representative today regarding FDIC insured CDs and money market accounts.

Equity Lines

With the onset of 2007 you may want to consider tapping into the equity in your home for debt consolidation, college tuition, for a face-lift to your kitchen or family room, or to pay for that long needed vacation. Whatever your reason, an Equity Line of Credit works just like a revolving credit line. It is there when you need it and all you have to do is write a check. An equity line of credit can be a good choice if you are looking at securing a loan because in most cases the interest expense is tax deductible.

¹All loan products are subject to credit approval. Rates are subject to change.



First South Bank

Member FDIC

Corporate Office

1311 Carolina Avenue
Washington, NC 27889
(252) 946-4178

Full-Service Branch Offices

Buxton	Kill Devil Hills
Chocowinity	Kinston
Durham	Lumberton (2)
Elizabeth City	New Bern (3)
Fayetteville (2)	Raleigh
Greenville (2)	Rocky Mount (5)
Hope Mills	Tarboro
Washington (3)	

Loan Production Office

Kill Devil Hills

First South Leasing, LLC

Greenville

Shareholder Information

Stock Listing:

NASDAQ - National Market System
Symbol - FSBK

Registrar and Transfer Agent:

Registrar and Transfer Company
10 Commerce Drive
Cranford, NJ 07016-3572
1-800-368-5948

Investor Relations:

PO Box 2047
Washington, North Carolina 27889
1-800-946-4178

www.firstsouthnc.com

Quarterly Financial Report

December 31, 2006

First South Bancorp

Dear Shareholders:

Net income for the quarter ended December 31, 2006 increased 6.1% to \$4,365,137 from \$4,115,671 earned in the quarter ended December 31, 2005. Diluted earnings per share increased 4.9% to \$0.43 per share for the quarter ended December 31, 2006 from \$0.41 per share for the quarter ended December 31, 2005. Net income for the year ended December 31, 2006 increased 21.7% to \$17,192,356 from \$14,128,704 earned in the year ended December 31, 2005. Diluted earnings per share increased 22.0% to \$1.72 per share for the year ended December 31, 2006 from \$1.41 per share for the year ended December 31, 2005.

Our earnings this quarter continue to be supported by sustaining the volume of our net interest income during a period of rising interest rates, slower loan growth, and competitive pressure on deposit flows in the market areas we serve, reflecting both our balance sheet and interest rate risk management efforts.

Total assets of the Company increased to \$910.5 million at December 30, 2006 from \$834.2 million at December 31, 2005, reflecting a 9.1% annualized growth rate. The net loan and leases receivable portfolio increased 7.4% to \$761.4 million at December 31, 2006 from \$708.9 million at December 31, 2005; while deposits increased 9.1% to \$800.2 million at December 31, 2006 from \$733.8 million at December 31, 2005.

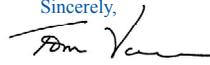
We also continued placing efforts on controlling operating expenses, resulting in a 43.5% efficiency ratio for the quarter ended December 31, 2006. Our key performance ratios, return on average assets (ROA) and return on average equity (ROE), continue to place us at the top of our peer group. Our ROA and ROE was 1.9% and 22.4%, respectively, for the quarter ended December 31, 2006.

The year ended December 31, 2006 was eventful for First South Bancorp. We increased the quarterly cash dividend payment rate by 25.0%, and combined with the appreciation in market price of our common stock, resulted in a 38.3% total return to our shareholders. We received national and statewide recognition for our operating efficiency, return on equity, net interest margin and various other operating performance ratios. First South Bancorp was listed in the new NASDAQ Global Select Market, placing us in a peer group of the top listed companies in the world. We also retained our listing in the Russell Index of funds which raises the Company's visibility with investors that rely on the Russell Indexes as part of their investment strategy.

During 2006 the First South Bank opened a new full service branch office in Buxton, North Carolina and we are currently renovating a new full service branch office in Durham, North Carolina. This expansion will allow us to better serve the banking needs in our growing market area, expand our customer base in existing markets and represents a continuation of the growth of our branch office network.

We are pleased to enclose our dividend check of \$0.17 per share payable to shareholders of record as of January 10, 2007. This dividend payment represents a payout ratio of 37.8% of basic earnings per share and is our thirty-ninth consecutive quarterly cash dividend.

The Board of Directors, officers and staff of the First South Bancorp and First South Bank thanks you for your support and trust. We pledge our continued commitment to you and we welcome your comments and suggestions.

Sincerely,

 Tom Vann
 President and Chief Executive Officer

Condensed Statements of Financial Condition*(in thousands)*

	December 31, 2006	December 31, 2005**
	<i>(unaudited)</i>	
Assets		
Cash and cash equivalents	\$ 25,804	\$ 32,943
Investment securities	56,454	41,828
Mortgage backed securities	36,729	22,702
Loans and leases receivable, net	761,437	708,929
Premises and equipment	8,898	8,831
Goodwill	4,219	4,219
Federal Home Loan Bank stock	1,933	1,689
Accrued interest receivable	5,398	4,289
Mortgage servicing rights	1,267	1,402
Income tax receivable	1,841	1,146
Other assets	6,568	6,256
	<u>\$ 910,548</u>	<u>\$ 834,234</u>
Total Assets		
Liabilities and Stockholders' Equity		
Deposits	\$ 800,188	\$ 733,753
Borrowings	11,140	11,788
Junior subordinated debentures	10,310	10,310
Other liabilities	10,113	10,192
Total liabilities	831,751	766,043
Total Stockholders' Equity	78,797	68,191
Total Liabilities and Stockholder's Equity	<u>\$ 910,548</u>	<u>\$ 834,234</u>

Condensed Statements of Income (unaudited)*(in thousands, except per share data)*

	Three Months Ended December 31		Year Ended December 31	
	2006	2005	2006	2005
Interest income	\$ 17,849	\$ 14,931	\$ 67,752	\$ 53,176
Interest expense	7,343	4,560	25,607	15,464
Net interest income	10,506	10,371	42,145	37,712
Provision for loan losses	0	266	933	1,711
Net interest income after provision for credit losses	10,506	10,105	41,212	36,001
Non-interest income	2,190	2,133	9,259	8,207
Non-interest expense	5,532	5,507	22,207	21,132
Income before taxes	7,164	6,731	28,264	23,076
Income tax expense	2,799	2,615	11,072	8,947
Net Income	<u>\$ 4,365</u>	<u>\$ 4,116</u>	<u>\$ 17,192</u>	<u>\$ 14,129</u>
Basic earnings per share	\$ 0.45	\$ 0.43*	\$ 1.77*	\$ 1.49*
Diluted earnings per share	\$ 0.43	\$ 0.41*	\$ 1.72*	\$ 1.41*
Dividends per share	\$ 0.17	\$ 0.14*	\$ 0.68*	\$ 0.53*
Weighted average shares - basic	9,780,619	9,500,829*	9,714,565*	9,488,073*
Weighted average shares - diluted	10,060,369	10,006,262*	10,002,869*	9,980,222*

* Adjusted for three-for-two stock split on May 25, 2006.

** Derived from audited consolidated financial statements.