FIRST BANCORP /NC/
Form 10-Q
August 09, 2012

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2012

Commission File Number 0-15572

FIRST BANCORP

(Exact Name of Registrant as Specified in its Charter)

North Carolina (State or Other Jurisdiction of Incorporation or Organization)	56-1421916 (I.R.S. Employer Identification Number)

341 North Main Street, Troy, North Carolina 27371-0508
(Address of Principal Executive Offices) (Zip Code)

(Registrant's telephone number, including area code) (910) 576-6171

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 twelve 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. ý YES o NO

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). ý YES o NO

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

o Large Accelerated Filer	ý Accelerated Filer	o Non-Accelerated Filer (Do not check if a smaller reporting company)	o Smaller Reporting Company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). o YES ý NO

The number of shares of the registrant's Common Stock outstanding on July 31, 2012 was 16,975,481.

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FIRST BANCORP AND SUBSIDIARIES

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FORWARD-LOOKING STATEMENTS

Part I of this report contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934 and the Private Securities Litigation Reform Act of 1995, which statements are inherently subject to risks and uncertainties. Forward-looking statements are statements that include projections, predictions, expectations or beliefs about future events or results or otherwise are not statements of historical fact. Such statements are often characterized by the use of qualifying words (and their derivatives) such as “expect,” “believe,” “estimate,” “plan,” “project,” or other statements concerning our opinions or judgment about future events. Our actual results may differ materially from those anticipated in any forward-looking statements, as they will depend on many factors about which we are unsure, including many factors which are beyond our control. Factors that could influence the accuracy of such forward-looking statements include, but are not limited to, the financial success or changing strategies of our customers, our level of success in integrating acquisitions, actions of government regulators, the level of market interest rates, and general economic conditions. For additional information about factors that could affect the matters discussed in this paragraph, see the “Risk Factors” section of our 2011 Annual Report on Form 10-K.

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Part I. Financial Information

Item 1 - Financial Statements

First Bancorp and Subsidiaries

Consolidated Balance Sheets

($ in thousands-unaudited)	June 30, 2012	December 31, 2011(audited)	June 30, 2011
ASSETS			
Cash and due from banks, noninterest-bearing	$58,872	80,341	73,676
Due from banks, interest-bearing	203,313	135,218	163,414
Federal funds sold	—	608	1,157
Total cash and cash equivalents	262,185	216,167	238,247
Securities available for sale	171,907	182,626	171,844
Securities held to maturity (fair values of $61,676, $62,754, and $59,860)	56,182	57,988	57,593
Presold mortgages in process of settlement	4,053	6,090	2,466
Loans – non-covered	2,114,906	2,069,152	2,040,714
Loans – covered by FDIC loss share agreement	322,895	361,234	401,726
Total loans	2,437,801	2,430,386	2,442,440
Allowance for loan losses – non-covered	(47,523)	(35,610)	(34,465)
Allowance for loan losses – covered	(5,931)	(5,808)	(5,540)
Total allowance for loan losses	(53,454)	(41,418)	(40,005)
Net loans	2,384,347	2,388,968	2,402,435
Premises and equipment	73,642	69,975	68,898
Accrued interest receivable	10,932	11,779	12,000
FDIC indemnification asset	116,902	121,677	142,894
Goodwill	65,835	65,835	65,835
Other intangible assets	3,452	3,897	4,349
Other real estate owned – non-covered	37,895	37,023	31,849
Other real estate owned – covered	70,850	85,272	102,883
Bank-owned life insurance	27,380	2,207	2,160
Other assets	43,193	40,970	30,296
Total assets	$3,328,755	3,290,474	3,333,749
LIABILITIES			
Deposits: Noninterest bearing checking accounts	$381,353	335,833	323,223
Interest bearing checking accounts	472,342	423,452	371,693
Money market accounts	545,356	513,832	499,286
Savings accounts	160,137	146,481	145,576

Time deposits of $100,000 or more	725,699	753,233	765,787
Other time deposits	553,411	582,206	641,853
Total deposits	2,838,298	2,755,037	2,747,418
Securities sold under agreements to repurchase	—	17,105	68,608
Borrowings	111,394	133,925	138,796
Accrued interest payable	1,549	1,872	2,208
Other liabilities	37,440	37,385	24,421
Total liabilities	2,988,681	2,945,324	2,981,451
Commitments and contingencies			
SHAREHOLDERS' EQUITY			
Preferred stock, no par value per share. Authorized: 5,000,000 shares			
Issued and outstanding: 63,500, 63,500, and 65,000 shares	63,500	63,500	65,000
Discount on preferred stock	—	—	(2,474)
Common stock, no par value per share. Authorized: 40,000,000 shares			
Issued and outstanding: 16,973,008, 16,909,820 and 16,862,536 shares	105,437	104,841	105,141
Retained earnings	179,298	185,491	188,737
Accumulated other comprehensive income (loss)	(8,161)	(8,682)	(4,106)
Total shareholders' equity	340,074	345,150	352,298
Total liabilities and shareholders' equity	$3,328,755	3,290,474	3,333,749

See notes to consolidated financial statements.

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First Bancorp and Subsidiaries

Consolidated Statements of Income

($ in thousands, except share data-unaudited)	Three Months Ended June 30, 2012	2011	Six Months Ended June 30, 2012	2011
INTEREST INCOME				
Interest and fees on loans	$35,636	38,464	70,678	75,271
Interest on investment securities:				
Taxable interest income	1,149	1,463	2,407	2,895
Tax-exempt interest income	491	499	984	999
Other, principally overnight investments	178	103	317	193
Total interest income	37,454	40,529	74,386	79,358
INTEREST EXPENSE				
Savings, checking and money market	759	1,103	1,608	2,333
Time deposits of $100,000 or more	2,085	2,661	4,260	5,265
Other time deposits	1,169	1,767	2,438	3,936
Securities sold under agreements to repurchase	—	48	4	98
Borrowings	490	470	1,034	932
Total interest expense	4,503	6,049	9,344	12,564
Net interest income	32,951	34,480	65,042	66,794
Provision for loan losses – non-covered	5,194	7,607	23,751	15,177
Provision for loan losses – covered	1,273	3,327	4,271	7,100
Total provision for loan losses	6,467	10,934	28,022	22,277
Net interest income after provision for loan losses	26,484	23,546	37,020	44,517
NONINTEREST INCOME				
Service charges on deposit accounts	2,967	3,294	5,814	5,939
Other service charges, commissions and fees	2,340	2,070	4,532	3,985
Fees from presold mortgage loans	489	346	900	641
Commissions from sales of insurance and financial products	432	409	815	764
Gain from acquisition			—	10,196
Foreclosed property losses and write-downs – non-covered	(1,318)	(271)	(2,006)	(1,624)
Foreclosed property losses and write-downs – covered	(6,554)	(2,583)	(11,101)	(7,517)
FDIC indemnification asset income, net	3,558	1,826	7,663	6,866
Securities gains (losses)	(3)	60	449	74
Other gains (losses)	(141)	(37)	53	(17)
Total noninterest income	1,770	5,114	7,119	19,307
NONINTEREST EXPENSES				
Salaries	10,173	9,694	20,347	19,405
Employee benefits	2,777	2,954	6,691	6,156
Total personnel expense	12,950	12,648	27,038	25,561

Net occupancy expense	1,615	1,598	3,296	3,270
Equipment related expenses	1,164	1,110	2,334	2,172
Intangibles amortization	223	226	446	450
Acquisition expenses	—	243	—	594
Other operating expenses	7,496	7,088	14,709	15,909
Total noninterest expenses	23,448	22,913	47,823	47,956
Income (loss) before income taxes	4,806	5,747	(3,684)	15,868
Income taxes (benefit)	1,516	2,021	(1,792)	5,767
Net income (loss)	3,290	3,726	(1,892)	10,101
Preferred stock dividends	(829)	(812)	(1,589)	(1,625)
Accretion of preferred stock discount	—	(229)	—	(458)
Net income (loss) available to common shareholders	$2,461	2,685	(3,481)	8,018
Earnings (loss) per common share:				
Basic	$0.15	0.16	(0.21)	0.48
Diluted	0.15	0.16	(0.21)	0.48
Dividends declared per common share	$0.08	0.08	0.16	0.16
Weighted average common shares outstanding:				
Basic	16,952,624	16,841,289	16,938,620	16,827,615
Diluted	16,952,624	16,868,571	16,938,620	16,855,027

See notes to consolidated financial statements.

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First Bancorp and Subsidiaries

Consolidated Statements of Comprehensive Income

($ in thousands-unaudited)	Three Months Ended June 30, 2012	2011	Six Months Ended June 30, 2012	2011
Net income (loss)	$ 3,290	3,726	(1,892)	10,101
Other comprehensive income (loss):				
Unrealized gains on securities available for sale:				
Unrealized holding gains arising during the period, pretax	186	1,198	901	1,387
Tax benefit	(72)	(467)	(350)	(541)
Reclassification to realized losses (gains)	3	(60)	(449)	(74)
Tax expense (benefit)	(1)	23	175	29
Postretirement Plans:				
Amortization of unrecognized net actuarial loss	82	140	383	280
Tax expense	(32)	(56)	(149)	(112)
Amortization of prior service cost and transition obligation	8	9	17	18
Tax expense	(3)	(4)	(7)	(8)
Other comprehensive income	171	783	521	979
Comprehensive income (loss)	$ 3,461	4,509	(1,371)	11,080

See notes to consolidated financial statements.

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First Bancorp and Subsidiaries

Consolidated Statements of Shareholders' Equity

(In thousands, except per share - unaudited)	Preferred Stock	Preferred Stock Discount	Common Stock Shares	Common Stock Amount	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
Balances, January 1, 2011	$65,000	(2,932)	16,801	$104,207	183,413	(5,085)	344,603
Net income					10,101		10,101
Common stock issued under stock option plans			2	30			30
Common stock issued into dividend reinvestment plan			30	421			421
Cash dividends declared ($0.16 per common share)					(2,694)		(2,694
Preferred dividends					(1,625)		(1,625
Accretion of preferred stock discount		458			(458)		—
Stock-based compensation			29	483			483
Other comprehensive income						979	979
Balances, June 30, 2011	$65,000	(2,474)	16,862	$105,141	188,737	(4,106)	352,298
Balances, January 1, 2012	$63,500	—	16,910	$104,841	185,491	(8,682)	345,150
Net income (loss)					(1,892)		(1,892
Common stock issued into dividend reinvestment plan			31	335			335
Repurchases of common stock			—	(2)			(2
Cash dividends declared ($0.16 per common share)					(2,712)		(2,712
Preferred dividends					(1,589)		(1,589
Stock-based compensation			32	263			263
Other comprehensive income						521	521
Balances, June 30, 2012	$63,500	—	16,973	$105,437	179,298	(8,161)	340,074

See notes to consolidated financial statements.

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First Bancorp and Subsidiaries

Consolidated Statements of Cash Flows

($ in thousands-unaudited)	Six Months Ended June 30, 2012	2011
Cash Flows From Operating Activities		
Net income (loss)	$(1,892)	10,101
Reconciliation of net income to net cash provided by operating activities:		
Provision for loan losses	28,022	22,277
Net security premium amortization	907	748
Purchase accounting accretion and amortization, net	(5,721)	(6,565)
Gain from acquisition	—	(10,196)
Foreclosed property losses and write-downs	13,107	9,141
Gain on securities available for sale	(449)	(74)
Other losses (gains)	(53)	17
Increase in net deferred loan costs	(96)	(323)
Depreciation of premises and equipment	2,278	2,182
Stock-based compensation expense	263	483
Amortization of intangible assets	446	450
Origination of presold mortgages in process of settlement	(41,858)	(35,532)
Proceeds from sales of presold mortgages in process of settlement	43,895	37,028
Decrease in accrued interest receivable	847	1,579
Increase in other assets	(13,188)	(6,866)
Increase (decrease) in accrued interest payable	(323)	126
Increase (decrease) in other liabilities	415	(5,238)
Net cash provided by operating activities	26,600	19,338
Cash Flows From Investing Activities		
Purchases of securities available for sale	(47,395)	(23,721)
Purchases of securities held to maturity	—	(3,816)
Proceeds from sales of securities available for sale	9,641	2,518
Proceeds from maturities/issuer calls of securities available for sale	48,590	34,829
Proceeds from maturities/issuer calls of securities held to maturity	1,685	1,053
Purchase of bank-owned life insurance	(25,000)	—
Net decrease (increase) in loans	(42,993)	45,905
Proceeds from FDIC loss share agreements	15,286	32,468
Proceeds from sales of foreclosed real estate	25,767	16,425
Purchases of premises and equipment	(5,945)	(3,323)
Net cash received in acquisition	—	54,037
Net cash provided (used) by investing activities	(20,364)	156,375
Cash Flows From Financing Activities		
Net increase (decrease) in deposits and repurchase agreements	66,211	(83,523)
Repayments of borrowings, net	(22,500)	(62,081)
Cash dividends paid – common stock	(2,708)	(2,690)
Cash dividends paid – preferred stock	(1,554)	(1,625)

Proceeds from issuance of common stock	335	451
Repurchase of common stock	(2)	—
Net cash provided (used) by financing activities	39,782	(149,468)
Increase in cash and cash equivalents	46,018	26,245
Cash and cash equivalents, beginning of period	216,167	212,002
Cash and cash equivalents, end of period	$262,185	238,247
Supplemental Disclosures of Cash Flow Information:		
Cash paid during the period for:		
Interest	$9,667	12,438
Income taxes	5,275	11,710
Non-cash transactions:		
Unrealized gain on securities available for sale, net of taxes	277	801
Foreclosed loans transferred to other real estate	25,324	42,984

See notes to consolidated financial statements.

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First Bancorp and Subsidiaries

Notes to Consolidated Financial Statements

(*unaudited)*
For the Periods Ended June 30, 2012 and 2011

Note 1 - Basis of Presentation

In the opinion of the Company, the accompanying unaudited consolidated financial statements contain all adjustments necessary to present fairly the consolidated financial position of the Company as of June 30, 2012 and 2011 and the consolidated results of operations and consolidated cash flows for the periods ended June 30, 2012 and 2011. All such adjustments were of a normal, recurring nature. Reference is made to the 2011 Annual Report on Form 10-K filed with the SEC for a discussion of accounting policies and other relevant information with respect to the financial statements. The results of operations for the periods ended June 30, 2012 and 2011 are not necessarily indicative of the results to be expected for the full year. The Company has evaluated all subsequent events through the date the financial statements were issued.

Note 2 – Accounting Policies

Note 1 to the 2011 Annual Report on Form 10-K filed with the SEC contains a description of the accounting policies followed by the Company and discussion of recent accounting pronouncements. During the first six months of 2012, there were no new standards or guidance issued by the regulatory authorities relevant to the Company.

Note 3 – Reclassifications

Certain amounts reported in the period ended June 30, 2011 have been reclassified to conform to the presentation for June 30, 2012. These reclassifications had no effect on net income or shareholders’ equity for the periods presented, nor did they materially impact trends in financial information.

Note 4 – Equity-Based Compensation Plans

At June 30, 2012, the Company had the following equity-based compensation plans: the First Bancorp 2007 Equity Plan, the First Bancorp 2004 Stock Option Plan, the First Bancorp 1994 Stock Option Plan, and one plan that was assumed from an acquired entity. The Company's shareholders approved all equity-based compensation plans, except for those assumed from acquired companies. The First Bancorp 2007 Equity Plan became effective upon the approval of shareholders on May 2, 2007. As of June 30, 2012, the First Bancorp 2007 Equity Plan was the only plan that had shares available for future grants.

The First Bancorp 2007 Equity Plan is intended to serve as a means to attract, retain and motivate key employees and directors and to associate the interests of the plans' participants with those of the Company and its shareholders. The First Bancorp 2007 Equity Plan allows for both grants of stock options and other types of equity-based compensation, including stock appreciation rights, restricted stock, restricted performance stock, unrestricted stock, and performance units.

Recent equity grants to employees have either had performance vesting conditions, service vesting conditions, or both. Compensation expense for these grants is recorded over the various service periods based on the estimated number of equity grants that are probable to vest. No compensation cost is recognized for grants that do not vest and any previously recognized compensation cost will be reversed. As it relates to director equity grants, the Company grants common shares, valued at approximately $226,000 in the aggregate on the date of the grant, to non-employee directors in June of each year. Compensation expense associated with these director grants is recognized on the date of grant since there are no vesting conditions.

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The Company granted long-term restricted shares of common stock to certain senior executives on February 24, 2011 and February 23, 2012 with a two year minimum vesting period. The total compensation expense associated with the February 24, 2011 grant was $105,500 and the grant will fully vest on February 24, 2013. The Company recorded $22,000 in stock option expense in the first six months of 2012 and will record $9,700 in each subsequent quarter of 2012 related to this grant. The total compensation expense associated with the February 23, 2012 grant was $89,700 and the grant will fully vest on February 23, 2014. The Company recorded $14,900 in the first six months of 2012 and will record $11,200 in each subsequent quarter of 2012 related to this grant.

Under the terms of the predecessor plans and the First Bancorp 2007 Equity Plan, options can have a term of no longer than ten years, and all options granted thus far under these plans have had a term of ten years. The Company's options provide for immediate vesting if there is a change in control (as defined in the plans).

At June 30, 2012, there were 476,624 options outstanding related to the three First Bancorp plans, with exercise prices ranging from $14.35 to $22.12. At June 30, 2012, there were 871,257 shares remaining available for grant under the First Bancorp 2007 Equity Plan. The Company also has a stock option plan as a result of a corporate acquisition. At June 30, 2012, there were 4,788 stock options outstanding in connection with the acquired plan, with option prices ranging from $10.66 to $15.22.

The Company issues new shares of common stock when options are exercised.

The Company measures the fair value of each option award on the date of grant using the Black-Scholes option-pricing model. The Company determines the assumptions used in the Black-Scholes option pricing model as follows: the risk-free interest rate is based on the U.S. Treasury yield curve in effect at the time of the grant; the dividend yield is based on the Company's dividend yield at the time of the grant (subject to adjustment if the dividend yield on the grant date is not expected to approximate the dividend yield over the expected life of the option); the volatility factor is based on the historical volatility of the Company's stock (subject to adjustment if future volatility is reasonably expected to differ from the past); and the weighted-average expected life is based on the historical behavior of employees related to exercises, forfeitures and cancellations.

The Company's equity grants for the six months ended June 30, 2012 were the issuance of 1) 9,559 shares of long-term restricted stock to certain senior executives on February 23, 2012, at a fair market value of $10.96 per share, which was the closing price of the Company's common stock on that date, and 2) 25,452 shares of common stock to non-employee directors on June 1, 2012 (1,818 shares per director), at a fair market value of $8.86 per share, which was the closing price of the Company's common stock on that date.

The Company's equity grants for the six months ended June 30, 2011 were the issuance of 1) 7,259 shares of long-term restricted stock to certain senior executives on February 24, 2011, at a fair market value of $14.54 per share, which

was the closing price of the Company's common stock on that date, and 2) 21,210 shares of common stock to non-employee directors on June 1, 2011 (1,414 shares per director), at a fair market value of $11.39 per share, which was the closing price of the Company's common stock on that date.

The Company recorded total stock-based compensation expense of $263,000 and $483,000 for the six month periods ended June 30, 2012 and 2011, respectively, which relates to the employee grants discussed above and is recorded as "salaries expense." Stock based compensation is reflected as an adjustment to cash flows from operating activities on the Company's Consolidated Statement of Cash Flows. The Company recognized $103,000 and $188,000 of income tax benefits related to stock based compensation expense in the income statement for the six months ended June 30, 2012 and 2011, respectively.

As noted above, certain of the Company's stock option grants contain terms that provide for a graded vesting schedule whereby portions of the award vest in increments over the requisite service period. The Company has elected to recognize compensation expense for awards with graded vesting schedules on a straight-line basis over the requisite service period for the entire award. Compensation expense is based on the estimated number of stock options and awards that will ultimately vest. Over the past five years, there have only been minimal amounts of forfeitures, and therefore the Company assumes that all options granted without performance conditions will become vested.

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The following table presents information regarding the activity for the first six months of 2012 related to all of the Company's stock options outstanding:

	Options Outstanding			
	Number of Shares	Weighted-Average Exercise Price	Weighted-Average Contractual Term (years)	Aggregate Intrinsic Value
Balance at December 31, 2011	493,850	$ 18.92		
Granted	—	—		
Exercised	—	—		
Forfeited	—	—		
Expired	(12,438)	18.71		
Outstanding at June 30, 2012	481,412	$ 18.92	3.2	$ —
Exercisable at June 30, 2012	480,412	$ 18.92	3.2	$ —

The Company did not have any stock option exercises during the six months ended June 30, 2012 and received $30,000 as a result of stock option exercises during the six months ended June 30, 2011. The Company recorded no tax benefits from the exercise of nonqualified stock options during the six months ended June 30, 2012 or 2011.

As discussed above, the Company granted 7,259 and 9,559 long-term restricted shares of common stock to certain senior executives on February 24, 2011 and February 23, 2012, respectively.

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The following table presents information regarding the activity during 2012 related to the Company's outstanding restricted stock:

	Long-Term Restricted Stock	
	Number of Units	Weighted-Average Grant-Date Fair Value
Nonvested at December 31, 2011	7,259	$ 14.54
Granted during the period	9,559	$ 10.96
Vested during the period	—	—
Forfeited or expired during the period	(2,474)	12.55
Nonvested at June 30, 2012	14,344	$ 12.50

Note 5 – Earnings Per Common Share

Basic earnings per common share were computed by dividing net income (loss) available to common shareholders by the weighted average number of common shares outstanding during the period. Diluted earnings per common share is computed by assuming the issuance of common shares for all potentially dilutive common shares outstanding during the reporting period. Currently, the Company's potentially dilutive common stock issuances relate to grants under the Company's equity-based compensation plans, including stock options and restricted stock. The following is a reconciliation of the numerators and denominators used in computing basic and diluted earnings per common share:

	For the Three Months Ended June 30,					
	2012			2011		
($ in thousands except per share amounts)	Income (Numer-ator)	Shares (Denom-inator)	Per Share Amount	Income (Numer-ator)	Shares (Denom-inator)	Per Share Amount
Basic EPS						
Net income available to common shareholders	$2,461	16,952,624	$ 0.15	$2,685	16,841,289	$ 0.16
Effect of Dilutive Securities	—	—		—	27,282	
Diluted EPS per common share	$2,461	16,952,624	$ 0.15	$2,685	16,868,571	$ 0.16

($ in thousands except per share amounts)	For the Six Months Ended June 30, 2012 Income (Numer-ator)	2012 Shares (Denom-inator)	2012 Per Share Amount	2011 Income (Numer-ator)	2011 Shares (Denom-inator)	2011 Per Share Amount
Basic EPS						
Net income (loss) available to common shareholders	$(3,481)	16,938,620	$(0.21)	$8,018	16,827,615	$0.48
Effect of Dilutive Securities	—	—		—	27,412	
Diluted EPS per common share	$(3,481)	16,938,620	$(0.21)	$8,018	16,855,027	$0.48

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For both the three and six months ended June 30, 2012, there were 386,662 options, respectively, that were antidilutive because the exercise price exceeded the average market price for the period. For both the three and six month periods ended June 30, 2011, there were 542,916 options that were antidilutive because the exercise price exceeded the average market price for the period. Antidilutive options have been omitted from the calculation of diluted earnings per share for the respective periods.

Note 6 – Securities

The book values and approximate fair values of investment securities at June 30, 2012 and December 31, 2011 are summarized as follows:

	June 30, 2012				December 31, 2011			
($ in thousands)	Amortized Cost	Fair Value	Unrealized Gains	(Losses)	Amortized Cost	Fair Value	Unrealized Gains	(Losses)
Securities available for sale:								
Government-sponsored enterprise securities	$29,504	29,626	122	—	34,511	34,665	170	(16)
Mortgage-backed securities	115,674	119,536	3,862	—	120,032	124,105	4,164	(91)
Corporate bonds	13,186	13,139	253	(300)	13,189	12,488	279	(980)
Equity securities	9,195	9,606	438	(27)	10,998	11,368	409	(39)
Total available for sale	$167,559	171,907	4,675	(327)	178,730	182,626	5,022	(1,126)
Securities held to maturity:								
State and local governments	$56,182	61,676	5,494	—	57,988	62,754	4,766	—
Total held to maturity	$56,182	61,676	5,494	—	57,988	62,754	4,766	—

Included in mortgage-backed securities at June 30, 2012 were collateralized mortgage obligations with an amortized cost of $663,000 and a fair value of $684,000. Included in mortgage-backed securities at December 31, 2011 were collateralized mortgage obligations with an amortized cost of $1,462,000 and a fair value of $1,515,000. All of the Company’s mortgage-backed securities, including collateralized mortgage obligations, were issued by government-sponsored corporations.

The Company owned Federal Home Loan Bank (FHLB) stock with a cost and fair value of $9,102,000 at June 30, 2012 and $10,904,000 at December 31, 2011, which is included in equity securities above and serves as part of the collateral for the Company’s line of credit with the FHLB. The investment in this stock is a requirement for membership in the FHLB system.

The following table presents information regarding securities with unrealized losses at June 30, 2012:

($ in thousands)	Securities in an Unrealized Loss Position for Less than 12 Months		Securities in an Unrealized Loss Position for More than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Government-sponsored enterprise securities	$ —	—	—	—	—	—
Mortgage-backed securities	—	—	—	—	—	—
Corporate bonds	—	—	5,029	300	5,029	300
Equity securities	—	—	31	27	31	27
State and local governments	—	—	—	—	—	—
Total temporarily impaired securities	$ —	—	5,060	327	5,060	327

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The following table presents information regarding securities with unrealized losses at December 31, 2011:

($ in thousands)	Securities in an Unrealized Loss Position for Less than 12 Months		Securities in an Unrealized Loss Position for More than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Government-sponsored enterprise securities	$ 8,984	16	—	—	8,984	16
Mortgage-backed securities	14,902	61	9,302	30	24,204	91
Corporate bonds	4,588	458	2,773	522	7,361	980
Equity securities	4	2	22	37	26	39
State and local governments	—	—	—	—	—	—
Total temporarily impaired securities	$ 28,478	537	12,097	589	40,575	1,126

In the above tables, all of the non-equity securities that were in an unrealized loss position at June 30, 2012 and December 31, 2011 are bonds that the Company has determined are in a loss position due to interest rate factors, the overall economic downturn in the financial sector, and the broader economy in general. The Company has evaluated the collectability of each of these bonds and has concluded that there is no other-than-temporary impairment. The Company does not intend to sell these securities, and it is more likely than not that the Company will not be required to sell these securities before recovery of the amortized cost. The Company has also concluded that each of the equity securities in an unrealized loss position at June 30, 2012 and December 31, 2011 was in such a position due to temporary fluctuations in the market prices of the securities. The Company's policy is to record an impairment charge for any of these equity securities that remains in an unrealized loss position for twelve consecutive months unless the amount is insignificant.

The aggregate carrying amount of cost-method investments was $9,102,000 at June 30, 2012 and $10,904,000 at December 31, 2011, respectively, which was the FHLB stock discussed above. The Company determined that none of its cost-method investments were impaired at either period end.

The book values and approximate fair values of investment securities at June 30, 2012, by contractual maturity, are summarized in the table below. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Securities Available for Sale		Securities Held to Maturity	
($ in thousands)	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Debt securities				
Due within one year	$ 3,004	3,040	350	358

Due after one year but within five years	26,497	26,679	2,958	3,210
Due after five years but within ten years	3,000	3,000	29,731	32,673
Due after ten years	10,189	10,046	23,143	25,435
Mortgage-backed securities	115,674	119,536	—	—
Total debt securities	158,364	162,301	56,182	61,676
Equity securities	9,195	9,606	—	—
Total securities	$ 167,559	171,907	56,182	61,676

At June 30, 2012 investment securities with a book value of $86,865,000 were pledged as collateral for public deposits. At December 31, 2011, investment securities with a book value of $47,418,000 were pledged as collateral for public and private deposits and securities sold under agreements to repurchase.

There were $9,641,000 in sales of securities during the six months ended June 30, 2012, which resulted in a net gain of $439,000. There were $2,518,000 in sales during the six months ended June 30, 2011, which resulted in a net gain of $8,000. During the six months ended June 30, 2012 and 2011, the Company recorded a net gain of $11,000 and $71,000, respectively, related to the call of several municipal and bond securities. Also, during the six months ended June 30, 2012 and 2011, the Company recorded a net loss of $1,000 and $5,000, respectively, related to write-downs of the Company’s equity portfolio.

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Note 7 – Loans and Asset Quality Information

The loans and foreclosed real estate that were acquired in FDIC-assisted transactions are covered by loss share agreements between the FDIC and the Company's banking subsidiary, First Bank, which afford First Bank significant loss protection. (See the Company's 2011 Annual Report on Form 10-K for more information regarding these transactions.) Because of the loss protection provided by the FDIC, the risk of the Cooperative Bank and The Bank of Asheville loans and foreclosed real estate are significantly different from those assets not covered under the loss share agreements. Accordingly, the Company presents separately loans subject to the loss share agreements as "covered loans" in the information below and loans that are not subject to the loss share agreements as "non-covered loans."

The following is a summary of the major categories of total loans outstanding:

($ in thousands)	June 30, 2012		December 31, 2011		June 30, 2011	
	Amount	Percentage	Amount	Percentage	Amount	Perce
All loans (non-covered and covered):						
Commercial, financial, and agricultural	$163,761	7%	162,099	7%	158,303	6%
Real estate – construction, land development & other land loans	343,620	14%	363,079	15%	386,354	16%
Real estate – mortgage – residential (1-4 family) first mortgages	815,605	34%	805,542	33%	803,209	33%
Real estate – mortgage – home equity loans / lines of credit	250,627	10%	256,509	11%	266,995	11%
Real estate – mortgage – commercial and other	789,290	32%	762,895	31%	745,858	31%
Installment loans to individuals	73,522	3%	78,982	3%	80,423	3%
Subtotal	2,436,425	100%	2,429,106	100%	2,441,142	100
Unamortized net deferred loan costs	1,376		1,280		1,298	
Total loans	$2,437,801		2,430,386		2,442,440	

As of June 30, 2012, December 31, 2011 and June 30, 2011, net loans include unamortized premiums of $717,000, $949,000, and $1,182,000, respectively, related to acquired loans.

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The following is a summary of the major categories of non-covered loans outstanding:

($ in thousands)	June 30, 2012		December 31, 2011		June 30, 2011	
	Amount	Percentage	Amount	Percentage	Amount	Percentage
Non-covered loans:						
Commercial, financial, and agricultural	$155,879	7%	152,627	8%	145,811	7%
Real estate – construction, land development & other land loans	283,818	13%	290,983	14%	306,140	15%
Real estate – mortgage – residential (1-4 family) first mortgages	669,088	32%	646,616	31%	631,640	31%
Real estate – mortgage – home equity loans / lines of credit	229,415	11%	233,171	11%	241,973	12%
Real estate – mortgage – commercial and other	702,717	33%	666,882	32%	635,103	31%
Installment loans to individuals	72,613	4%	77,593	4%	78,749	4%
Subtotal	2,113,530	100%	2,067,872	100%	2,039,416	100%
Unamortized net deferred loan costs	1,376		1,280		1,298	
Total non-covered loans	$2,114,906		2,069,152		2,040,714	

The carrying amount of the covered loans at June 30, 2012 consisted of impaired and nonimpaired purchased loans, as follows:

($ in thousands)	Impaired Purchased Loans – Carrying Value	Impaired Purchased Loans – Unpaid Principal Balance	Nonimpaired Purchased Loans – Carrying Value	Nonimpaired Purchased Loans - Unpaid Principal Balance	Total Covered Loans – Carrying Value	Total Covered Loans – Unpaid Principal Balance
Covered loans:						
Commercial, financial, and agricultural	$68	146	7,814	9,885	7,882	10,031
Real estate – construction, land development & other land loans	1,577	2,606	58,225	99,332	59,802	101,938
Real estate – mortgage – residential (1-4 family) first mortgages	827	1,915	145,690	173,707	146,517	175,622
Real estate – mortgage – home equity loans / lines of credit	12	309	21,200	26,400	21,212	26,709
Real estate – mortgage – commercial and other	2,332	4,153	84,241	113,936	86,573	118,089
Installment loans to individuals	3	4	906	990	909	994
Total	$4,819	9,133	318,076	424,250	322,895	433,383

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The carrying amount of the covered loans at December 31, 2011 consisted of impaired and nonimpaired purchased loans, as follows:

($ in thousands)	Impaired Purchased Loans – Carrying Value	Impaired Purchased Loans – Unpaid Principal Balance	Nonimpaired Purchased Loans – Carrying Value	Nonimpaired Purchased Loans - Unpaid Principal Balance	Total Covered Loans – Carrying Value	Total Covered Loans – Unpaid Principal Balance
Covered loans:						
Commercial, financial, and agricultural	$69	319	9,403	11,736	9,472	12,055
Real estate – construction, land development & other land loans	3,865	8,505	68,231	115,489	72,096	123,994
Real estate – mortgage – residential (1-4 family) first mortgages	1,214	2,639	157,712	189,436	158,926	192,075
Real estate – mortgage – home equity loans / lines of credit	127	577	23,211	29,249	23,338	29,826
Real estate – mortgage – commercial and other	2,585	4,986	93,428	125,450	96,013	130,436
Installment loans to individuals	4	6	1,385	1,583	1,389	1,589
Total	$7,864	17,032	353,370	472,943	361,234	489,975

The following table presents information regarding covered purchased nonimpaired loans since December 31, 2010. The amounts include principal only and do not reflect accrued interest as of the date of the acquisition or beyond.

($ in thousands)	
Carrying amount of nonimpaired covered loans at December 31, 2010	$366,521
Additions due to acquisition of The Bank of Asheville (at fair value)	84,623
Principal repayments	(40,576)
Transfers to foreclosed real estate	(53,999)
Loan charge-offs	(14,797)
Accretion of loan discount	11,598
Carrying amount of nonimpaired covered loans at December 31, 2011	$353,370
Principal repayments	(25,012)
Transfers to foreclosed real estate	(11,974)
Loan charge-offs	(4,176)
Accretion of loan discount	5,868
Carrying amount of nonimpaired covered loans at June 30, 2012	$318,076

As reflected in the table above, the Company accreted $5,868,000 of the loan discount on purchased nonimpaired loans into interest income during the first six months of 2012. As of June 30, 2012, there was remaining loan discount of $73,519,000 related to purchased nonimpaired loans. If these loans continue to be repaid by the borrowers, the Company will accrete the remaining loan discount into interest income over the lives of the respective loans. In such circumstances, a corresponding entry to reduce the indemnification asset will be recorded amounting to 80% of the loan discount accretion, which reduces noninterest income.

The following table presents information regarding all purchased impaired loans since December 31, 2010, substantially all of which are covered loans. The Company has applied the cost recovery method to all purchased impaired loans at their respective acquisition dates due to the uncertainty as to the timing of expected cash flows, as reflected in the following table.

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($ in thousands)

	Contractual Principal Receivable	Fair Market Value Adjustment – Write Down (Nonaccretable Difference)	Carrying Amount
Purchased Impaired Loans			
Balance at December 31, 2010	$ 8,080	2,329	5,751
Additions due to acquisition of The Bank of Asheville	38,452	20,807	17,645
Change due to payments received	(1,620)	(327)	(1,293)
Transfer to foreclosed real estate	(19,881)	(9,308)	(10,573)
Change due to loan charge-off	(7,522)	(4,193)	(3,329)
Other	807	224	583
Balance at December 31, 2011	$ 18,316	9,532	8,784
Change due to payments received	(287)	(54)	(233)
Transfer to foreclosed real estate	(7,636)	(3,487)	(4,149)
Change due to loan charge-off	(109)	(109)	—
Other	(1,151)	(1,568)	417
Balance at June 30, 2012	$ 9,133	4,314	4,819

Each of the purchased impaired loans is on nonaccrual status and considered to be impaired. Because of the uncertainty of the expected cash flows, the Company is accounting for each purchased impaired loan under the cost recovery method, in which all cash payments are applied to principal. Thus, there is no accretable yield associated with the above loans. During the first six months of 2012 and 2011, the Company received no payments that exceeded the initial carrying amount of the purchased impaired loans.

Nonperforming assets are defined as nonaccrual loans, restructured loans, loans past due 90 or more days and still accruing interest, and other real estate. Nonperforming assets are summarized as follows:

ASSET QUALITY DATA *($ in thousands)*	June 30, 2012	December 31, 2011	June 30, 2011
Non-covered nonperforming assets			
Nonaccrual loans	$73,918	73,566	71,570
Restructured loans - accruing	20,684	11,720	16,893
Accruing loans > 90 days past due	—	—	—
Total non-covered nonperforming loans	94,602	85,286	88,463

Other real estate	37,895	37,023	31,849
Total non-covered nonperforming assets	$132,497	122,309	120,312
Covered nonperforming assets			
Nonaccrual loans (1)	$39,075	41,472	37,057
Restructured loans - accruing	19,054	14,218	24,325
Accruing loans > 90 days past due	—	—	—
Total covered nonperforming loans	58,129	55,690	61,382
Other real estate	70,850	85,272	102,883
Total covered nonperforming assets	$128,979	140,962	164,265
Total nonperforming assets	$261,476	263,271	284,577

(1) At June 30, 2012, December 31, 2011, and June 30, 2011, the contractual balance of the nonaccrual loans covered by FDIC loss share agreements was $60.4 million, $69.0 million, and $69.4 million, respectively.

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The following table presents information related to the Company's impaired loans.

($ in thousands)	As of /for the six months ended June 30, 2012	As of /for the year ended December 31, 2011	As of /for the six months ended June 30, 2011
Impaired loans at period end			
Non-covered	$ 94,602	85,286	88,463
Covered	58,129	55,690	61,382
Total impaired loans at period end	$ 152,731	140,976	149,845
Average amount of impaired loans for period			
Non-covered	$ 86,723	89,023	91,187
Covered	56,449	63,289	69,102
Average amount of impaired loans for period – total	$ 143,172	152,312	160,289
Allowance for loan losses related to impaired loans at period end			
Non-covered	$ 11,051	5,804	6,019
Covered	5,158	5,106	4,727
Allowance for loan losses related to impaired loans - total	$ 16,209	10,910	10,746
Amount of impaired loans with no related allowance at period end			
Non-covered	$ 22,235	35,721	31,514
Covered	40,613	43,702	49,755
Total impaired loans with no related allowance at period end	$ 62,848	79,423	81,269

All of the impaired loans noted in the table above were on nonaccrual status at each respective period end except for those classified as restructured loans (see table on previous page for balances).

The remaining tables in this note present information derived from the Company's allowance for loan loss model. Relevant accounting guidance requires certain disclosures to be disaggregated based on how the Company develops its allowance for loan losses and manages its credit exposure. This model combines loan types in a different manner than the tables previously presented.

The following table presents the Company's nonaccrual loans as of June 30, 2012.

($ in thousands)	Non-covered	Covered	Total

Commercial, financial, and agricultural:			
Commercial – unsecured	$ 211	188	399
Commercial – secured	2,227	—	2,227
Secured by inventory and accounts receivable	637	—	637
Real estate – construction, land development & other land loans	19,781	16,963	36,744
Real estate – residential, farmland and multi-family	24,146	10,084	34,230
Real estate – home equity lines of credit	3,878	758	4,636
Real estate – commercial	20,277	11,009	31,286
Consumer	2,761	73	2,834
Total	$ 73,918	39,075	112,993

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The following table presents the Company's nonaccrual loans as of December 31, 2011.

($ in thousands)	Non-covered	Covered	Total
Commercial, financial, and agricultural:			
Commercial - unsecured	$ 452	—	452
Commercial - secured	2,190	358	2,548
Secured by inventory and accounts receivable	588	102	690
Real estate – construction, land development & other land loans	22,772	21,204	43,976
Real estate – residential, farmland and multi-family	25,430	11,050	36,480
Real estate – home equity lines of credit	3,161	1,068	4,229
Real estate - commercial	16,203	7,459	23,662
Consumer	2,770	231	3,001
Total	$ 73,566	41,472	115,038

The following table presents an analysis of the payment status of the Company's loans as of June 30, 2012.

($ in thousands)	30-59 Days Past Due	60-89 Days Past Due	Nonaccrual Loans	Current	Total Loans Receivable
Non-covered loans					
Commercial, financial, and agricultural:					
Commercial - unsecured	$83	58	211	37,991	38,343
Commercial - secured	446	443	2,227	110,248	113,364
Secured by inventory and accounts receivable	55	—	637	21,277	21,969
Real estate – construction, land development & other land loans	1,544	425	19,781	222,973	244,723
Real estate – residential, farmland, and multi-family	6,648	2,109	24,146	777,203	810,106
Real estate – home equity lines of credit	1,759	460	3,878	201,589	207,686
Real estate - commercial	4,715	381	20,277	597,135	622,508
Consumer	690	181	2,761	51,199	54,831
Total non-covered	$15,940	4,057	73,918	2,019,615	2,113,530
Unamortized net deferred loan costs					1,376
Total non-covered loans					$2,114,906

Covered loans	$5,253	2,147	39,075	276,420	322,895
Total loans	$21,193	6,204	112,993	2,296,035	2,437,801

The Company had no non-covered or covered loans that were past due greater than 90 days and accruing interest at June 30, 2012.

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The following table presents an analysis of the payment status of the Company's loans as of December 31, 2011.

($ in thousands)	30-59 Days Past Due	60-89 Days Past Due	Nonaccrual Loans	Current	Total Loans Receivable
Non-covered loans					
Commercial, financial, and agricultural:					
Commercial - unsecured	$67	591	452	37,668	38,778
Commercial - secured	672	207	2,190	108,682	111,751
Secured by inventory and accounts receivable	247	—	588	20,993	21,828
Real estate – construction, land development & other land loans	1,250	1,411	22,772	221,372	246,805
Real estate – residential, farmland, and multi-family	9,751	4,259	25,430	756,215	795,655
Real estate – home equity lines of credit	1,126	237	3,161	202,912	207,436
Real estate - commercial	2,620	1,006	16,203	567,354	587,183
Consumer	657	286	2,770	54,723	58,436
Total non-covered	$16,390	7,997	73,566	1,969,919	2,067,872
Unamortized net deferred loan costs					1,280
Total non-covered loans					$2,069,152
Covered loans	$6,511	3,388	41,472	309,863	361,234
Total loans	$22,901	11,385	115,038	2,279,782	2,430,386

The Company had no non-covered or covered loans that were past due greater than 90 days and accruing interest at December 31, 2011.

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The following table presents the activity in the allowance for loan losses for non-covered loans for the three and six months ended June 30, 2012.

($ in thousands)	Commercial, Financial, and Agricultural	Real Estate – Construction, Land Development, & Other Land Loans	Real Estate – Residential, Farmland, and Multi-family	Real Estate – Home Equity Lines of Credit	Real Estate – Commercial and Other	Consumer	Unallo-cated	Total
As of and for the three months ended June 30, 2012								
Beginning balance	$4,954	16,419	15,369	2,132	5,737	1,826	18	46,45
Charge-offs	(744)	(174)	(2,145)	(281)	(805)	(334)	—	(4,483
Recoveries	18	126	60	85	6	62	—	357
Provisions	833	1,448	1,675	210	781	237	10	5,194
Ending balance	$5,061	17,819	14,959	2,146	5,719	1,791	28	47,52
As of and for the six months ended June 30, 2012								
Beginning balance	$3,780	11,306	13,532	1,690	3,414	1,872	16	35,61
Charge-offs	(2,062)	(2,852)	(4,236)	(732)	(2,170)	(686)	—	(12,73
Recoveries	34	314	254	119	47	132	—	900
Provisions	3,309	9,051	5,409	1,069	4,428	473	12	23,75
Ending balance	$5,061	17,819	14,959	2,146	5,719	1,791	28	47,52
Ending balances as of June 30, 2012: Allowance for loan losses								
Individually evaluated for impairment	$869	4,819	635	439	1,480	—	—	8,242
Collectively evaluated for impairment	$4,192	13,000	14,324	1,707	4,239	1,791	28	39,28
Loans acquired with deteriorated credit quality	$—	—	—	—	—	—	—	—
Loans receivable as of June 30, 2012:								
Ending balance – total	$173,676	244,723	810,106	207,686	622,508	54,831	—	2,113
Ending balances as of June 30, 2012: Loans								
Individually evaluated for impairment	$1,009	23,860	9,508	1,331	21,918	—	—	57,62
Collectively evaluated for impairment	$172,667	220,863	800,598	206,355	600,590	54,831	—	2,055
Loans acquired with deteriorated credit quality	$—	—	—	—	—	—	—	—

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The following table presents the activity in the allowance for loan losses for non-covered loans for the year ended December 31, 2011.

($ in thousands)	Commercial, Financial, and Agricultural	Real Estate – Construction, Land Development, & Other Land Loans	Real Estate – Residential, Farmland, and Multi-family	Real Estate – Home Equity Lines of Credit	Real Estate – Commercial and Other	Consumer	Unallo-cated	Tota
Beginning balance	$4,731	12,520	11,283	3,634	3,972	1,961	174	38,2
Charge-offs	(2,703)	(16,240)	(9,045)	(1,147)	(3,355)	(845)	(524)	(33
Recoveries	389	1,142	719	107	37	182	93	2,6
Provisions	1,363	13,884	10,575	(904)	2,760	574	273	28,3
Ending balance	$3,780	11,306	13,532	1,690	3,414	1,872	16	35,6
Ending balances: Allowance for loan losses								
Individually evaluated for impairment	$60	607	150	—	200	—	—	1,0
Collectively evaluated for impairment	$3,720	10,699	13,382	1,690	3,214	1,872	16	34,3
Loans acquired with deteriorated credit quality	$—	—	—	—	—	—	—	—
Loans receivable:								
Ending balance – total	$172,357	246,805	795,655	207,436	587,183	58,436	—	2,0
Ending balances: Loans								
Individually evaluated for impairment	$2,526	34,750	11,880	527	30,846	12	—	80,3
Collectively evaluated for impairment	$169,831	212,055	783,775	206,909	556,337	58,424	—	1,9
Loans acquired with deteriorated credit quality	$—	920	—	—	—	—	—	920

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The following table presents the activity in the allowance for loan losses for non-covered loans for the three and six months ended June 30, 2011.

($ in thousands)	Commercial, Financial, and Agricultural	Real Estate – Construction, Land Development, & Other Land Loans	Real Estate – Residential, Farmland, and Multi-family	Real Estate – Home Equity Lines of Credit	Real Estate – Commercial and Other	Consumer	Unallo-cated	Tota
As of and for the three months ended June 30, 2011								
Beginning balance	$4,142	10,203	12,463	3,359	3,359	2,223	24	35,7
Charge-offs	(740)	(5,589)	(2,248)	(141)	(313)	(157)	(121)	(9,3
Recoveries	28	219	61	37	—	20	29	394
Provisions	475	6,957	1,808	(1,406)	(187)	(126)	86	7,60
Ending balance	$3,905	11,790	12,084	1,849	2,859	1,960	18	34,4
As of and for the six months ended June 30, 2011								
Beginning balance	$4,731	12,520	11,283	3,634	3,972	1,961	174	38,2
Charge-offs	(1,896)	(9,582)	(5,596)	(764)	(1,380)	(360)	(236)	(19
Recoveries	36	251	293	43	28	103	73	827
Provisions	1,034	8,601	6,104	(1,064)	239	256	7	15,1
Ending balance	$3,905	11,790	12,084	1,849	2,859	1,960	18	34,4
Ending balances as of June 30, 2011: Allowance for loan losses								
Individually evaluated for impairment	$50	1,221	235	—	340	—	—	1,84
Collectively evaluated for impairment	$3,855	10,569	11,849	1,849	2,519	1,960	18	32,6
Loans acquired with deteriorated credit quality	$—	—	—	—	—	—	—	—
Loans receivable as of June 30, 2011:								
Ending balance – total	$165,091	267,346	774,448	213,920	558,879	59,732	—	2,03
Ending balances as of June 30, 2011: Loans								
Individually evaluated for impairment	$2,049	47,181	7,656	531	34,198	20	—	91,6
Collectively evaluated for impairment	$163,042	220,165	766,792	213,389	524,681	59,712	—	1,94
Loans acquired with deteriorated credit quality	$—	1,234	—	—	—	—	—	1,23

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The following table presents the activity in the allowance for loan losses for covered loans for the three and six months ended June 30, 2012.

($ in thousands)	Covered Loans
As of and for the three months ended June 30, 2012	
Beginning balance	$ 6,372
Charge-offs	(1,714)
Recoveries	—
Provisions	1,273
Ending balance	$ 5,931
As of and for the six months ended June 30, 2012	
Beginning balance	$ 5,808
Charge-offs	(4,148)
Recoveries	—
Provisions	4,271
Ending balance	$ 5,931
Ending balances as of June 30, 2012: Allowance for loan losses	
Individually evaluated for impairment	$ 5,914
Collectively evaluated for impairment	—
Loans acquired with deteriorated credit quality	17
Loans receivable as of June 30, 2012:	
Ending balance – total	$ 322,895
Ending balances as of June 30, 2012: Loans	
Individually evaluated for impairment	$ 42,598
Collectively evaluated for impairment	280,297
Loans acquired with deteriorated credit quality	4,819

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The following table presents the activity in the allowance for loan losses for covered loans for the year ended December 31, 2011.

($ in thousands)	Covered Loans
As of and for the year ended December 31, 2011	
Beginning balance	$ 11,155
Charge-offs	(18,123)
Recoveries	—
Provisions	12,776
Ending balance	$ 5,808
Ending balances as of December 31, 2011: Allowance for loan losses	
Individually evaluated for impairment	$ 5,481
Collectively evaluated for impairment	—
Loans acquired with deteriorated credit quality	327
Loans receivable as of December 31, 2011:	
Ending balance – total	$ 361,234
Ending balances as of December 31, 2011: Loans	
Individually evaluated for impairment	$ 44,723
Collectively evaluated for impairment	316,511
Loans acquired with deteriorated credit quality	7,864

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The following table presents the activity in the allowance for loan losses for covered loans for the three and six months ended June 30, 2011.

($ in thousands)	Covered Loans
As of and for the three months ended June 30, 2011	
Beginning balance	$ 7,002
Charge-offs	(4,789)
Recoveries	—
Provisions	3,327
Ending balance	$ 5,540
As of and for the six months ended June 30, 2011	
Beginning balance	$ 11,155
Charge-offs	(12,715)
Recoveries	—
Provisions	7,100
Ending balance	$ 5,540
Ending balances as of June 30, 2011: Allowance for loan losses	
Individually evaluated for impairment	$ 5,540
Collectively evaluated for impairment	—
Loans acquired with deteriorated credit quality	—
Loans receivable as of June 30, 2011:	
Ending balance – total	$ 401,726
Ending balances as of June 30, 2011: Loans	
Individually evaluated for impairment	$ 37,149
Collectively evaluated for impairment	364,577
Loans acquired with deteriorated credit quality	13,538

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The following table presents the Company's impaired loans as of June 30, 2012.

($ in thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment
Non-covered loans with no related allowance recorded:				
Commercial, financial, and agricultural:				
Commercial - unsecured	$ —	—	—	—
Commercial - secured	69	225	—	144
Secured by inventory and accounts receivable	—	—	—	9
Real estate – construction, land development & other land loans	6,950	11,676	—	8,992
Real estate – residential, farmland, and multi-family	4,242	6,010	—	3,172
Real estate – home equity lines of credit	—	—	—	15
Real estate – commercial	10,974	12,683	—	12,554
Consumer	—	—	—	4
Total non-covered impaired loans with no allowance	$ 22,235	30,594	—	24,890
Total covered impaired loans with no allowance	$ 40,613	75,350	—	40,357
Total impaired loans with no allowance recorded	$ 62,848	105,944	—	65,247
Non-covered loans with an allowance recorded:				
Commercial, financial, and agricultural:				
Commercial - unsecured	$ 211	612	40	231
Commercial - secured	2,158	2,436	315	1,912
Secured by inventory and accounts receivable	637	1,112	143	673
Real estate – construction, land development & other land loans	18,156	22,302	6,093	15,360
Real estate – residential, farmland, and multi-family	23,476	26,658	2,361	24,792
Real estate – home equity lines of credit	3,877	4,493	453	3,300
Real estate – commercial	21,089	24,102	1,309	12,776
Consumer	2,763	2,801	337	2,789
Total non-covered impaired loans with allowance	$ 72,367	84,516	11,051	61,833
Total covered impaired loans with allowance	$ 17,516	19,421	5,158	16,092
Total impaired loans with an allowance recorded	$ 89,883	103,937	16,209	77,925

Interest income recorded on non-covered and covered impaired loans during the six months ended June 30, 2012 is considered insignificant.

The related allowance listed above includes both reserves on loans specifically reviewed for impairment and general reserves on impaired loans that were not specifically reviewed for impairment.

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The following table presents the Company's impaired loans as of December 31, 2011.

($ in thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment
Non-covered loans with no related allowance recorded:				
Commercial, financial, and agricultural:				
Commercial - unsecured	$ —	—	—	—
Commercial - secured	295	478	—	504
Secured by inventory and accounts receivable	27	493	—	124
Real estate – construction, land development & other land loans	15,105	20,941	—	17,876
Real estate – residential, farmland, and multi-family	3,442	4,741	—	5,278
Real estate – home equity lines of credit	46	300	—	79
Real estate – commercial	16,794	18,817	—	13,359
Consumer	12	39	—	15
Total non-covered impaired loans with no allowance	$ 35,721	45,809	—	37,235
Total covered impaired loans with no allowance	$ 43,702	78,578	—	49,030
Total impaired loans with no allowance recorded	$ 79,423	124,387	—	86,265
Non-covered loans with an allowance recorded:				
Commercial, financial, and agricultural:				
Commercial - unsecured	$ 452	454	59	226
Commercial - secured	1,895	1,899	295	1,427
Secured by inventory and accounts receivable	561	571	156	391
Real estate – construction, land development & other land loans	10,360	12,606	2,244	15,782
Real estate – residential, farmland, and multi-family	24,460	26,153	2,169	22,487
Real estate – home equity lines of credit	3,115	3,141	117	2,544
Real estate – commercial	5,965	6,421	283	6,602
Consumer	2,757	2,759	481	2,329
Total non-covered impaired loans with allowance	$ 49,565	54,004	5,804	51,788
Total covered impaired loans with allowance	$ 11,988	15,670	5,106	14,259
Total impaired loans with an allowance recorded	$ 61,553	69,674	10,910	66,047

Interest income recorded on non-covered and covered impaired loans during the year ended December 31, 2011 is considered insignificant.

The related allowance listed above includes both reserves on loans specifically reviewed for impairment and general reserves on impaired loans that were not specifically reviewed for impairment.

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The Company tracks credit quality based on its internal risk ratings. Upon origination a loan is assigned an initial risk grade, which is generally based on several factors such as the borrower's credit score, the loan-to-value ratio, the debt-to-income ratio, etc. Loans that are risk-graded as substandard during the origination process are declined. After loans are initially graded, they are monitored monthly for credit quality based on many factors, such as payment history, the borrower's financial status, and changes in collateral value. Loans can be downgraded or upgraded depending on management's evaluation of these factors. Internal risk-grading policies are consistent throughout each loan type.

The following describes the Company's internal risk grades in ascending order of likelihood of loss:

Numerical Risk Grade	Description
Pass:	
1	Cash secured loans.
2	Non-cash secured loans that have no minor or major exceptions to the lending guidelines.
3	Non-cash secured loans that have no major exceptions to the lending guidelines.
Weak Pass:	
4	Non-cash secured loans that have minor or major exceptions to the lending guidelines, but the exceptions are properly mitigated.
Watch or Standard:	
9	Loans that meet the guidelines for a Risk Graded 5 loan, except the collateral coverage is sufficient to satisfy the debt with no risk of loss under reasonable circumstances. This category also includes all loans to insiders and any other loan that management elects to monitor on the watch list.
Special Mention:	
5	Existing loans with major exceptions that cannot be mitigated.
Classified:	
6	Loans that have a well-defined weakness that may jeopardize the liquidation of the debt if deficiencies are not corrected.
7	Loans that have a well-defined weakness that make the collection or liquidation improbable.
8	Loans that are considered uncollectible and are in the process of being charged-off.

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The following table presents the Company's recorded investment in loans by credit quality indicators as of June 30, 2012.

($ in thousands)	Credit Quality Indicator (Grouped by Internally Assigned Gra					
	Pass (Grades 1, 2, & 3)	Weak Pass (Grade 4)	Watch or Standard Loans (Grade 9)	Special Mention Loans (Grade 5)	Classified Loans (Grades 6, 7, & 8)	Nonac Loans
Non-covered loans:						
Commercial, financial, and agricultural:						
Commercial - unsecured	$11,933	25,351	12	323	513	211
Commercial - secured	34,861	69,630	1,705	2,481	2,460	2,227
Secured by inventory and accounts receivable	3,688	16,539	265	695	145	637
Real estate – construction, land development & other land loans	32,230	161,242	5,304	11,971	14,195	19,78
Real estate – residential, farmland, and multi-family	250,715	476,852	9,105	17,883	31,405	24,14
Real estate – home equity lines of credit	131,210	66,044	2,521	2,338	1,695	3,878
Real estate - commercial	135,080	417,454	27,537	13,025	9,135	20,27
Consumer	28,153	22,676	86	514	641	2,761
Total	$627,870	1,255,788	46,535	49,230	60,189	73,91
Unamortized net deferred loan costs						
Total non-covered loans						
Total covered loans	$51,912	137,930	—	8,459	85,519	39,07
Total loans	$679,782	1,393,718	46,535	57,689	145,708	112,9

At June 30, 2012, there was an insignificant amount of non-covered loans that were graded "8" with an accruing status.
At June 30, 2012, there were no covered loans that were graded "8" with an accruing status.

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The following table presents the Company's recorded investment in loans by credit quality indicators as of December 31, 2011.

($ in thousands)	Credit Quality Indicator (Grouped by Internally Assigned Gra					
	Pass (Grades 1, 2, & 3)	Weak Pass (Grade 4)	Watch or Standard Loans (Grade 9)	Special Mention Loans (Grade 5)	Classified Loans (Grades 6, 7, & 8)	Nonac Loans
Non-covered loans:						
Commercial, financial, and agricultural:						
Commercial - unsecured	$13,516	23,735	13	217	845	452
Commercial - secured	36,587	66,105	1,912	2,196	2,761	2,190
Secured by inventory and accounts receivable	3,756	16,197	282	756	249	588
Real estate – construction, land development & other land loans	37,596	156,651	6,490	9,903	13,393	22,77
Real estate – residential, farmland, and multi-family	257,163	456,188	10,248	17,687	28,939	25,43
Real estate – home equity lines of credit	130,913	67,606	2,422	1,868	1,466	3,161
Real estate - commercial	140,577	372,614	30,722	11,502	15,565	16,20
Consumer	30,693	23,550	67	368	988	2,770
Total	$650,801	1,182,646	52,156	44,497	64,206	73,56
Unamortized net deferred loan costs						
Total non-covered loans						
Total covered loans	$62,052	161,508	—	8,033	88,169	41,47
Total loans	$712,853	1,344,154	52,156	52,530	152,375	115,0

At December 31, 2011, there was an insignificant amount of non-covered loans that were graded "8" with an accruing status. At December 31, 2011, there were no covered loans that were graded "8" with an accruing status.

Troubled Debt Restructurings

The restructuring of a loan is considered a "troubled debt restructuring" if both (i) the borrower is experiencing financial difficulties and (ii) the creditor has granted a concession. Concessions may include interest rate reductions or below market interest rates, principal forgiveness, restructuring amortization schedules and other actions intended to minimize potential losses.

The vast majority of the Company's troubled debt restructurings modified during the period ended June 30, 2012 related to interest rate reductions combined with restructured amortization schedules. The Company does not grant principal forgiveness.

All loans classified as troubled debt restructurings are considered to be impaired and are evaluated as such for determination of the allowance for loan losses. The Company's troubled debt restructurings can be classified as either nonaccrual or accruing based on the loan's payment status. The troubled debt restructurings that are nonaccrual are reported within the nonaccrual loan totals presented previously.

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The following table presents information related to loans modified in a troubled debt restructuring during the three and six months ended June 30, 2012.

($ in thousands)	For the three months ended June 30, 2012		For the six months ended June 30, 2012	
	Number of Contracts	Restructured Balances	Number of Contracts	Restructured Balances
Non-covered TDRs – Accruing				
Real estate – construction, land development & other land loans	1	$ 300	1	$ 300
Real estate – residential, farmland, and multi-family	1	303	1	303
Non-covered TDRs - Nonaccrual				
Real estate – construction, land development & other land loans	1	238	1	238
Total non-covered TDRs arising during period	3	$ 841	3	$ 841
Total covered TDRs arising during period– Accruing	3	$ 5,428	6	$ 7,342
Total covered TDRs arising during period – Nonaccrual	—	—	—	—
Total TDRs arising during period	6	$ 6,269	9	$ 8,183

Accruing restructured loans that defaulted during the three and six months ended June 30, 2012 are presented in the table below. The Company considers a loan to have defaulted when it becomes 90 or more days delinquent under the modified terms, has been transferred to nonaccrual status, or has been transferred to other real estate owned.

($ in thousands)	For the three months ended June 30, 2012		For the six months ended June 30, 2012	
	Number of Contracts	Recorded Investment	Number of Contracts	Recorded Investment
Non-covered accruing TDRs that subsequently defaulted				
Real estate – construction, land development & other land loans	—	$ —	2	$ 664
Real estate – residential, farmland, and multi-family	1	341	1	341
Real estate - commercial	1	180	1	180
Total non-covered TDRs that subsequently defaulted	2	$ 521	4	$ 1,185
Total accruing covered TDRs that subsequently defaulted	3	$ 716	14	$ 3,427
Total accruing TDRs that subsequently defaulted	5	$ 1,237	18	$ 4,612

Note 8 – Deferred Loan Costs

The amount of loans shown on the Consolidated Balance Sheets includes net deferred loan costs of approximately $1,376,000, $1,280,000, and $1,298,000 at June 30, 2012, December 31, 2011, and June 30, 2011, respectively.

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Note 9 – FDIC Indemnification Asset

The FDIC indemnification asset is the estimated amount that the Company will receive from the FDIC under loss share agreements associated with two FDIC-assisted failed bank acquisitions. See page 38 of the Company's 2011 Annual Report on Form 10-K for a detailed explanation of this asset.

The FDIC indemnification asset was comprised of the following components as of the dates shown:

($ in thousands)	June 30, 2012	December 31, 2011	June 30, 2011
Receivable related to claims submitted, not yet received	$18,574	13,377	27,668
Receivable related to estimated future claims on loans	79,308	90,275	100,953
Receivable related to estimated future claims on other real estate owned	19,020	18,025	14,273
FDIC indemnification asset	$116,902	121,677	142,894

The following presents a rollforward of the FDIC indemnification asset since December 31, 2011.

($ in thousands)	
Balance at December 31, 2011	$121,677
Increase related to unfavorable changes in loss estimates	12,298
Increase related to reimbursable expenses	3,183
Cash received	(15,286)
Accretion of loan discount	(4,694)
Other	(276)
Balance at June 30, 2012	$116,902

Note 10 – Goodwill and Other Intangible Assets

The following is a summary of the gross carrying amount and accumulated amortization of amortizable intangible assets as of June 30, 2012, December 31, 2011, and June 30, 2011 and the carrying amount of unamortized intangible assets as of those same dates.

	June 30, 2012	December 31, 2011	June 30, 2011

($ in thousands)	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Amortizable intangible assets:						
Customer lists	$678	387	678	357	678	328
Core deposit premiums	7,867	4,707	7,867	4,291	7,867	3,868
Total	$8,545	5,094	8,545	4,648	8,545	4,196
Unamortizable intangible assets:						
Goodwill	$65,835		65,835		65,835	

Amortization expense totaled $223,000 and $226,000 for the three months ended June 30, 2012 and 2011, respectively. Amortization expense totaled $446,000 and $450,000 for the six months ended June 30, 2012 and 2011, respectively

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The following table presents the estimated amortization expense for the last three quarters of calendar year 2012 and for each of the four calendar years ending December 31, 2016 and the estimated amount amortizable thereafter. These estimates are subject to change in future periods to the extent management determines it is necessary to make adjustments to the carrying value or estimated useful lives of amortized intangible assets.

($ in thousands)	Estimated Amortization Expense
July 1 to December 31, 2012	$ 446
2013	781
2014	678
2015	622
2016	555
Thereafter	369
Total	$ 3,451

Note 11 – Pension Plans

The Company sponsors two defined benefit pension plans – a qualified retirement plan (the “Pension Plan”) which is generally available to all employees, and a Supplemental Executive Retirement Plan (the “SERP”), which is for the benefit of certain senior management executives of the Company.

The Company recorded pension expense totaling $619,000 and $832,000 for the three months ended June 30, 2012 and 2011, respectively, related to the Pension Plan and the SERP. The following table contains the components of the pension expense.

	For the Three Months Ended June 30,					
($ in thousands)	2012 Pension Plan	2011 Pension Plan	2012 SERP	2011 SERP	2012 Total Both Plans	2011 Total Both Plans
Service cost – benefits earned during the period	$457	478	76	115	533	593
Interest cost	363	432	70	102	433	534
Expected return on plan assets	(492)	(444)			(492)	(444)
Amortization of transition obligation	1	1			1	1
Amortization of net (gain)/loss	136	114		26	136	140
Amortization of prior service cost	3	3	5	5	8	8
Net periodic pension cost	$468	584	151	248	619	832

The Company recorded pension expense totaling $1,658,000 and $1,664,000 for the six months ended June 30, 2012 and 2011, respectively, related to the Pension Plan and the SERP. The following table contains the components of the pension expense.

	For the Six Months Ended June 30,					
($ in thousands)	2012 Pension Plan	2011 Pension Plan	2012 SERP	2011 SERP	2012 Total Both Plans	2011 Total Both Plans
Service cost – benefits earned during the period	$1,061	956	170	230	1,231	1,186
Interest cost	799	864	157	204	956	1,068
Expected return on plan assets	(984)	(888)			(984)	(888)
Amortization of transition obligation	2	2			2	2
Amortization of net (gain)/loss	403	228	34	52	437	280
Amortization of prior service cost	6	6	10	10	16	16
Net periodic pension cost	$1,287	1,168	371	496	1,658	1,664

The Company’s contributions to the Pension Plan are based on computations by independent actuarial consultants and are intended to provide the Company with the maximum deduction for income tax purposes. The contributions are invested to provide for benefits under the Pension Plan. The Company expects that it will contribute $2,500,000 to the Pension Plan in 2012.

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The Company's funding policy with respect to the SERP is to fund the related benefits from the operating cash flow of the Company.

Note 12 – Comprehensive Income

Comprehensive income is defined as the change in equity during a period for non-owner transactions and is divided into net income and other comprehensive income. Other comprehensive income includes revenues, expenses, gains, and losses that are excluded from earnings under current accounting standards. The components of accumulated other comprehensive income (loss) for the Company are as follows:

($ in thousands)	June 30, 2012	December 31, 2011	June 30, 2011
Unrealized gain (loss) on securities available for sale	$ 4,348	3,896	3,790
Deferred tax asset (liability)	(1,694)	(1,520)	(1,478)
Net unrealized gain (loss) on securities available for sale	2,654	2,376	2,312
Additional pension liability	(17,879)	(18,278)	(10,608)
Deferred tax asset	7,064	7,220	4,190
Net additional pension liability	(10,815)	(11,058)	(6,418)
Total accumulated other comprehensive income (loss)	$ (8,161)	(8,682)	(4,106)

Note 13 – Fair Value

Relevant accounting guidance establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The guidance describes three levels of inputs that may be used to measure fair value:

Level 1: Quoted prices (unadjusted) of identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2: Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3: Significant unobservable inputs that reflect a reporting entity’s own assumptions about the assumptions that market participants would use in pricing an asset or liability.

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The following table summarizes the Company's financial instruments that were measured at fair value on a recurring and nonrecurring basis at June 30, 2012.

($ in thousands)

Description of Financial Instruments	Fair Value at June 30, 2012	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Recurring				
Securities available for sale:				
Government-sponsored enterprise securities	$29,626	—	29,626	—
Mortgage-backed securities	119,536	—	119,536	—
Corporate bonds	13,139	—	13,139	—
Equity securities	9,606	423	9,183	—
Total available for sale securities	$171,907	423	171,484	—
Nonrecurring				
Impaired loans – covered	$58,129	—	—	58,129
Impaired loans – non-covered	94,602	—	—	94,602
Other real estate – covered	70,850	—	70,850	—
Other real estate – non-covered	37,895	—	37,895	—

The following table summarizes the Company's financial instruments that were measured at fair value on a recurring and nonrecurring basis at December 31, 2011.

($ in thousands)

Description of Financial Instruments	Fair Value at December 31, 2011	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Recurring				
Securities available for sale:				
Government-sponsored enterprise securities	$34,665	—	34,665	—
Mortgage-backed securities	124,105	—	124,105	—
Corporate bonds	12,488	—	12,488	—
Equity securities	11,368	398	10,969	—
Total available for sale securities	$182,626	398	182,227	—
Nonrecurring				
Impaired loans – covered	$55,690	—	55,690	—
Impaired loans – non-covered	85,286	—	85,286	—

Other real estate – covered	85,272	—	85,272	—
Other real estate – non-covered	37,023	—	37,023	—

The following is a description of the valuation methodologies used for instruments measured at fair value.

Securities — When quoted market prices are available in an active market, the securities are classified as Level 1 in the valuation hierarchy. Level 1 securities for the Company include certain equity securities. If quoted market prices are not available, but fair values can be estimated by observing quoted prices of securities with similar characteristics, the securities are classified as Level 2 on the valuation hierarchy. Most of the fair values for the Company's Level 2 securities are determined by matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted securities. For the Company, Level 2 securities include mortgage-backed securities, collateralized mortgage obligations, government-sponsored entity securities, and corporate bonds. In cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy.

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Impaired loans —Fair values for impaired loans in the above table are collateral dependent and are estimated based on underlying collateral values, as determined by third-party appraisers, which are then adjusted for the cost related to liquidation of the collateral.

Other real estate – Other real estate, consisting of properties obtained through foreclosure or in satisfaction of loans, is reported at the lower of cost or fair value, determined on the basis of current appraisals, comparable sales, and other estimates of value obtained principally from independent sources, adjusted for estimated selling costs. At the time of foreclosure, any excess of the loan balance over the fair value of the real estate held as collateral is treated as a charge against the allowance for loan losses.

Transfers of assets or liabilities between levels within the fair value hierarchy are recognized when an event or change in circumstances occurs. There were no transfers between Level 1 and Level 2 for assets or liabilities measured on a recurring basis during the three months ended June 30, 2012 or 2011.

For the six months ended June 30, 2012 and 2011, the increase in the fair value of securities available for sale was $452,000 and $1,313,000, respectively, which is included in other comprehensive income (tax expense of $175,000 and $512,000, respectively). Fair value measurement methods at June 30, 2012 and 2011 are consistent with those used in prior reporting periods.

The carrying amounts and estimated fair values of financial instruments at June 30, 2012 and December 31, 2011 are as follows:

		June 30, 2012		December 31, 2011	
($ in thousands)	Level in Fair Value Hierarchy	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Cash and due from banks, noninterest-bearing	Level 1	$58,872	58,872	80,341	80,341
Due from banks, interest-bearing	Level 1	203,313	203,313	135,218	135,218
Federal funds sold	Level 1	—	—	608	608
Securities available for sale	Level 2	171,907	171,907	182,626	182,626
Securities held to maturity	Level 2	56,182	61,676	57,988	62,754
Presold mortgages in process of settlement	Level 1	4,053	4,053	6,090	6,090
Loans – non-covered, net of allowance	Level 3	2,067,383	2,006,670	2,033,542	1,987,979
Loans – covered, net of allowance	Level 3	316,964	316,964	355,426	355,426
FDIC indemnification asset	Level 3	116,902	116,501	121,677	121,004
Accrued interest receivable	Level 1	10,932	10,932	11,779	11,779
Deposits	Level 2	2,838,298	2,841,563	2,755,037	2,759,504
Securities sold under agreements to repurchase	Level 2	—	—	17,105	17,105
Borrowings	Level 2	111,394	86,451	133,925	106,333

Accrued interest payable	Level 2	1,549	1,549	1,872	1,872

Fair value methods and assumptions are set forth below for the Company’s financial instruments.

Cash and Due from Banks, Federal Funds Sold, Presold Mortgages in Process of Settlement, Accrued Interest Receivable, and Accrued Interest Payable - The carrying amounts approximate their fair value because of the short maturity of these financial instruments. (Level 1)

Available for Sale and Held to Maturity Securities - Fair values are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments or matrix pricing. (Level 2)

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Loans – For non-impaired loans, fair values are estimated for portfolios of loans with similar financial characteristics. Loans are segregated by type such as commercial, financial and agricultural, real estate construction, real estate mortgages and installment loans to individuals. Each loan category is further segmented into fixed and variable interest rate terms. The fair value for each category is determined by discounting scheduled future cash flows using current interest rates offered on loans with similar risk characteristics. (Level 3)

As discussed above, fair values for impaired loans are estimated based on estimated proceeds expected upon liquidation of the collateral. (Level 3)

FDIC Indemnification Asset – Fair value is equal to the FDIC reimbursement rate of the expected losses to be incurred and reimbursed by the FDIC and then discounted over the estimated period of receipt. (Level 3)

Deposits and Securities Sold Under Agreements to Repurchase - The fair value of securities sold under agreements to repurchase and deposits with no stated maturity, such as non-interest-bearing demand deposits, savings, checking, and money market accounts, is equal to the amount payable on demand as of the valuation date. The fair value of certificates of deposit is based on the discounted value of contractual cash flows. The discount rate is estimated using the rates currently offered for deposits of similar remaining maturities. (Level 2)

Borrowings - The fair value of borrowings is based on the discounted value of contractual cash flows. The discount rate is estimated using the rates currently offered by the Company’s lenders for debt of similar remaining maturities. (Level 2)

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company’s entire holdings of a particular financial instrument. Because no highly liquid market exists for a significant portion of the Company’s financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Fair value estimates are based on existing on- and off-balance sheet financial instruments without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. Significant assets and liabilities that are not considered financial assets or liabilities include net premises and equipment, intangible and other assets such as foreclosed properties, deferred income taxes, prepaid expense accounts, income taxes currently payable and other various accrued expenses. In addition, the income tax ramifications related to the realization of the unrealized gains and losses can have a significant effect on fair value

estimates and have not been considered in any of the estimates.

Note 14 – Participation in the Small Business Lending Fund

On September 1, 2011, the Company completed the sale of $63.5 million of Series B preferred stock to the Secretary of the Treasury under the Small Business Lending Fund (SBLF). The fund was established under the Small Business Jobs Act of 2010 that was created to encourage lending to small businesses by providing capital to qualified community banks with assets less than $10 billion.

Under the terms of the stock purchase agreement, the Treasury received 63,500 shares of non-cumulative perpetual preferred stock with a liquidation value of $1,000 per share, in exchange for $63.5 million.

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The Series B preferred stock qualifies as Tier 1 capital. The dividend rate, as a percentage of the liquidation amount, can fluctuate on a quarterly basis during the first 10 quarters during which the Series B preferred stock is outstanding, based upon changes in the level of "Qualified Small Business Lending" or "QBSL". For the first nine quarters after issuance, the dividend rate can range from one percent (1%) to five percent (5%) per annum based upon the increase in QBSL as compared to the baseline. For quarters subsequent to the issuance in 2011, the Company has paid a dividend rate ranging from 4.8% to 5.0%. Based upon an increase in the level of QBSL over the baseline level calculated under the terms of the related purchase agreement, the dividend rate for the next dividend period (which will end on September 30, 2012) is expected to be 5.0%, subject to confirmation by Treasury. For the tenth calendar quarter through four and one half years after issuance, the dividend rate will be fixed at between one percent (1%) and seven percent (7%) based upon the level of QBSL compared to the baseline. After four and one half years from the issuance, the dividend rate will increase to nine percent (9%). Subject to regulatory approval, the Company is generally permitted to redeem the Series B preferred shares at par plus unpaid dividends.

There was no discount recorded related to the SBLF preferred stock (because no warrants were issued in connection with this preferred stock issuance), and therefore there will be no future amounts recorded for preferred stock discount accretion.

For the first six months of 2012, the Company accrued approximately $1,589,000 in preferred dividend payments. This amount is deducted from net income in computing "Net income available to common shareholders."

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Item 2 - Management's Discussion and Analysis of Consolidated Results of Operations and Financial Condition

Critical Accounting Policies

The accounting principles we follow and our methods of applying these principles conform with accounting principles generally accepted in the United States of America and with general practices followed by the banking industry. Certain of these principles involve a significant amount of judgment and may involve the use of estimates based on our best assumptions at the time of the estimation. The allowance for loan losses, intangible assets, and the fair value and discount accretion of loans acquired in FDIC-assisted transactions are three policies we have identified as being more sensitive in terms of judgments and estimates, taking into account their overall potential impact to our consolidated financial statements.

Allowance for Loan Losses

Due to the estimation process and the potential materiality of the amounts involved, we have identified the accounting for the allowance for loan losses and the related provision for loan losses as an accounting policy critical to our consolidated financial statements. The provision for loan losses charged to operations is an amount sufficient to bring the allowance for loan losses to an estimated balance considered adequate to absorb losses inherent in the portfolio.

Our determination of the adequacy of the allowance is based primarily on a mathematical model that estimates the appropriate allowance for loan losses. This model has two components. The first component involves a review, and an estimation of losses, on loans or loan relationships that are significant in size and that are impaired (“impaired loans”). A loan is considered to be impaired when, based on current information and events, it is probable we will be unable to collect all amounts due according to the contractual terms of the loan agreement. The estimated valuation allowance is the difference, if any, between the loan balance outstanding and the value of the impaired loan as determined by either 1) an estimate of the cash flows that we expect to receive from the borrower discounted at the loan’s effective rate, or 2) in the case of a collateral-dependent loan, the fair value of the collateral.

The second component of the allowance model is an estimate of losses for smaller balance impaired loans and all loans not considered to be impaired loans (“general reserve loans”). General reserve loans having normal credit risk are segregated by loan type, and estimated loss percentages are assigned to each loan type, based on the historical losses, current economic conditions, and operational conditions specific to each loan type. For loans that we have risk graded as having more than “standard” risk, loss percentages are based on a multiple of the estimated loss rate for loans of a similar loan type with normal risk. The multiples assigned vary by type of loan, depending on risk, and we have consulted with an external credit review firm in assigning those multiples.

The reserve estimated for impaired loans is then added to the reserve estimated for general reserve loans. This becomes our “allocated allowance.” In addition to the allocated allowance derived from the model, we also evaluate other data such as the ratio of the allowance for loan losses to total loans, net loan growth information, nonperforming asset levels and trends in such data. Based on this additional analysis, we may determine that an additional amount of allowance for loan losses is necessary to reserve for probable losses. This additional amount, if any, is our “unallocated allowance.” The sum of the allocated allowance and the unallocated allowance is compared to the actual allowance for loan losses recorded on our books and any adjustment necessary for the recorded allowance to equal the computed allowance is recorded as a provision for loan losses. The provision for loan losses is a direct charge to earnings in the period recorded.

Loans covered under loss share agreements are recorded at fair value at acquisition date. Therefore, amounts deemed uncollectible at acquisition date become a part of the fair value calculation and are excluded from the allowance for loan losses. Subsequent decreases in the amount expected to be collected result in a provision for loan losses with a corresponding increase in the allowance for loan losses. Subsequent increases in the amount expected to be collected are accreted into income over the life of the loan. Proportional adjustments are also recorded to the FDIC indemnification asset.

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Although we use the best information available to make evaluations, future material adjustments may be necessary if economic, operational, or other conditions change. In addition, various regulatory agencies, as an integral part of their examination process, periodically review our allowance for loan losses. Such agencies may require us to recognize additions to the allowance based on the examiners' judgment about information available to them at the time of their examinations.

For further discussion, see "Nonperforming Assets" and "Summary of Loan Loss Experience" below.

Intangible Assets

Due to the estimation process and the potential materiality of the amounts involved, we have also identified the accounting for intangible assets as an accounting policy critical to our consolidated financial statements.

When we complete an acquisition transaction, the excess of the purchase price over the amount by which the fair market value of assets acquired exceeds the fair market value of liabilities assumed represents an intangible asset. We must then determine the identifiable portions of the intangible asset, with any remaining amount classified as goodwill. Identifiable intangible assets associated with these acquisitions are generally amortized over the estimated life of the related asset, whereas goodwill is tested annually for impairment, but not systematically amortized. Assuming no goodwill impairment, it is beneficial to our future earnings to have a lower amount assigned to identifiable intangible assets and higher amount of goodwill as opposed to having a higher amount considered to be identifiable intangible assets and a lower amount classified as goodwill.

The primary identifiable intangible asset we typically record in connection with a whole bank or bank branch acquisition is the value of the core deposit intangible, whereas when we acquire an insurance agency, the primary identifiable intangible asset is the value of the acquired customer list. Determining the amount of identifiable intangible assets and their average lives involves multiple assumptions and estimates and is typically determined by performing a discounted cash flow analysis, which involves a combination of any or all of the following assumptions: customer attrition/runoff, alternative funding costs, deposit servicing costs, and discount rates. We typically engage a third party consultant to assist in each analysis. For the whole bank and bank branch transactions recorded to date, the core deposit intangibles have generally been estimated to have a life ranging from seven to ten years, with an accelerated rate of amortization. For insurance agency acquisitions, the identifiable intangible assets related to the customer lists were determined to have a life of ten to fifteen years, with amortization occurring on a straight-line basis.

Subsequent to the initial recording of the identifiable intangible assets and goodwill, we amortize the identifiable intangible assets over their estimated average lives, as discussed above. In addition, on at least an annual basis, goodwill is evaluated for impairment by comparing the fair value of our reporting units to their related carrying value,

including goodwill (our community banking operation is our only material reporting unit). If the carrying value of a reporting unit were ever to exceed its fair value, we would determine whether the implied fair value of the goodwill, using a discounted cash flow analysis, exceeded the carrying value of the goodwill. If the carrying value of the goodwill exceeded the implied fair value of the goodwill, an impairment loss would be recorded in an amount equal to that excess. Performing such a discounted cash flow analysis would involve the significant use of estimates and assumptions.

At our last goodwill impairment evaluation as of September 30, 2011, we determined the fair value of our community banking operation was approximately $18.50 per common share, or 8% higher, than the $17.08 stated book value of our common stock at the date of valuation. To assist us in computing the fair value of our community banking operation, we engaged a consulting firm who used various valuation techniques as part of their analysis, which resulted in the conclusion of the $18.50 value.

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We review identifiable intangible assets for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Our policy is that an impairment loss is recognized, equal to the difference between the asset's carrying amount and its fair value, if the sum of the expected undiscounted future cash flows is less than the carrying amount of the asset. Estimating future cash flows involves the use of multiple estimates and assumptions, such as those listed above.

Fair Value and Discount Accretion of Loans Acquired in FDIC-Assisted Transactions

We consider the determination of the initial fair value of loans acquired in FDIC-assisted transactions, the initial fair value of the related FDIC indemnification asset, and the subsequent discount accretion of the purchased loans to involve a high degree of judgment and complexity. We determine fair value accounting estimates of newly assumed assets and liabilities in accordance with relevant accounting guidance. However, the amount that we realize on these assets could differ materially from the carrying value reflected in our financial statements, based upon the timing of collections on the acquired loans in future periods. To the extent the actual values realized for the acquired loans are different from the estimates, the FDIC indemnification asset will generally be impacted in an offsetting manner due to the loss-sharing support from the FDIC.

Because of the inherent credit losses associated with the acquired loans in a failed bank acquisition, the amount that we record as the fair values for the loans is generally less than the contractual unpaid principal balance due from the borrowers, with the difference being referred to as the "discount" on the acquired loans. We have applied the cost recovery method of accounting to all purchased impaired loans due to the uncertainty as to the timing of expected cash flows. This will result in the recognition of interest income on these impaired loans only when the cash payments received from the borrower exceed the recorded net book value of the related loans.

For nonimpaired purchased loans, we accrete the discount over the lives of the loans in a manner consistent with the guidance for accounting for loan origination fees and costs.

Current Accounting Matters

See Note 2 to the Consolidated Financial Statements above for information about accounting standards that we have recently adopted.

RESULTS OF OPERATIONS

Overview

Net income available to common shareholders for the second quarter of 2012 amounted to $2.5 million, or $0.15 per diluted common share, compared to $2.7 million, or $0.16 per diluted common share, recorded in the second quarter of 2011. For the six months ended June 30, 2012, we reported a net loss available to common shareholders of $3.5 million, or ($0.21) per diluted common share, compared to net income of $8.0 million, or $0.48 per diluted common share, for the six months ended June 30, 2011. The net loss reported for the first six months of 2012 was caused primarily by a higher provision for loan losses in the first quarter of 2012 related to non-covered loans.

Also impacting comparability from 2011 to 2012 was a significant gain we recorded in 2011. In the first quarter of 2011, we realized a $10.2 million bargain purchase gain related to the acquisition of The Bank of Asheville in Asheville, North Carolina. The after-tax impact of this gain was $6.2 million, or $0.37 per diluted common share.

Note Regarding Components of Earnings

Our results of operation are significantly affected by the on-going accounting for two FDIC-assisted failed bank acquisitions. In the discussion below, the term “covered” is used to describe assets included as part of FDIC loss share agreements, which generally result in the FDIC reimbursing the Company for 80% of losses incurred on those assets. The term “non-covered” refers to the Company’s legacy assets, which are not included in any type of loss share arrangement.

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For covered loans that deteriorate in terms of repayment expectations, we record immediate allowances through the provision for loan losses. For covered loans that experience favorable changes in credit quality compared to what was expected at the acquisition date, including loans that payoff, we record positive adjustments to interest income over the life of the respective loan – also referred to as loan discount accretion. For foreclosed properties that are sold at gains or losses or that are written down to lower values, we record the gains/losses within noninterest income.

The adjustments discussed above are recorded within the income statement line items noted without consideration of the FDIC loss share agreements. Because favorable changes in covered assets result in lower expected FDIC claims, and unfavorable changes in covered assets result in higher expected FDIC claims, the FDIC indemnification asset is adjusted to reflect those expectations. The net increase or decrease in the indemnification asset is reflected within noninterest income.

The adjustments noted above can result in volatility within individual income statement line items. Because of the FDIC loss share agreements and the associated indemnification asset, pretax income resulting from amounts recorded as provisions for loan losses on covered loans, discount accretion, and losses from covered foreclosed properties is generally only impacted by 20% of these amounts due to the corresponding adjustments made to the indemnification asset.

Net Interest Income and Net Interest Margin

Net interest income for the second quarter of 2012 amounted to $33.0 million, a 4.4% decrease from the $34.5 million recorded in the second quarter of 2011. Net interest income for the six months ended June 30, 2012 amounted to $65.0 million, a 2.6% decrease from the $66.8 million recorded in the comparable period of 2011.

The Company’s net interest margin (tax-equivalent net interest income divided by average earning assets) in the second quarter of 2012 was 4.68%, a 24 basis point decrease compared to the 4.92% margin realized in the second quarter of 2011. For the six month period ended June 30, 2012, the Company’s net interest margin was 4.64% compared to 4.77% for the same period in 2011. The lower margins were primarily due to lower loan yields, as well as the mix of the Company’s earning assets being more concentrated in lower yielding short-term investments in 2012 compared to a larger concentration of higher yielding loans and securities in 2011.

The 4.68% net interest margin realized in the second quarter of 2012 was a nine basis point increase from the 4.59% margin realized in the first quarter of 2012. The increase was primarily a result of higher amounts of discount accretion on loans purchased in failed bank acquisitions recognized during the respective periods. As previously discussed, the impact of the changes in discount accretion on pretax income is only 20% of the gross amount of the change.

Provision for Loan Losses and Asset Quality

We recorded total provisions for loan losses of $6.5 million in the second quarter of 2012 compared to $10.9 million for the second quarter of 2011. For the six months ended June 30, 2012, we recorded total provisions for loan losses of $28.0 million compared to $22.3 million for the comparable period of 2011.

The provision for loan losses on non-covered loans amounted to $5.2 million in the second quarter of 2012 compared to $7.6 million in the second quarter of 2011. This decline in provision was primarily due to stabilization in our assessment of the losses associated with our nonperforming non-covered loans. For the first six months of 2012 the provision for loan losses on non-covered loans amounted to $23.8 million compared to $15.2 million for the same period of 2011. The higher provision for loan losses was primarily a result of an internal review of non-covered loans that occurred in the first quarter of 2012 that applied more conservative assumptions to estimate the probable losses associated with some of our nonperforming loan relationships, which we believe may lead to a more timely resolution of the related credits.

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Our provisions for loan losses for covered loans amounted to $1.3 million and $3.3 million for the three months ended June 30, 2012 and 2011, respectively, and $4.3 million and $7.1 million for the six months ended June 30, 2012 and 2011, respectively. The lower provisions in 2012 were due to stabilization in our assessment of the losses associated with our nonperforming covered loans. The majority of the provisions for loan losses on covered loans in 2011 and 2012 relate to loans assumed in the Company's June 2009 acquisition of Cooperative Bank. As previously discussed, the provision for loan losses related to covered loans is offset by an 80% increase to the FDIC indemnification asset, which increases noninterest income.

Total non-covered nonperforming assets have remained fairly stable over the past five quarter ends, ranging from $117 million to $132 million, or approximately 4.5% of total non-covered assets at June 30, 2012. During the three months ended June 30, 2012, as a part of a routine regulatory exam, we reclassified approximately $12 million of performing loans to "restructured loans – accruing" that had been renewed or modified in prior periods. Other than reclassifying these loans to a nonperforming asset category for disclosure purposes, this reclassification did not impact our financial statements.

Covered nonperforming assets have generally declined over the past 12 months, amounting to $129 million at June 30, 2012 compared to $164 million at June 30, 2011.

Noninterest Income

Total noninterest income for the three months ended June 30, 2012 and 2011 was $1.8 million and $5.1 million, respectively, a decrease of $3.3 million, or 65.4%, which was primarily attributable to losses and write-downs on foreclosed properties (see discussion in section entitled "Components of Earnings"). For the six months ended June 30, 2012 and 2011, we recorded noninterest income of $7.1 million and $19.3 million, respectively. The significant decrease in noninterest income for the six month period comparison is primarily the result of the previously discussed $10.2 million bargain purchase gain recorded in the acquisition of The Bank of Asheville during the first quarter of 2011.

Noninterest Expenses

Noninterest expenses amounted to $23.4 million in the second quarter of 2012, a 2.3% increase from the $22.9 million recorded in the same period of 2011. Noninterest expenses for the six months ended June 30, 2012 amounted to $47.8 million, a 0.3% decrease from the $48.0 million recorded in the first six months of 2011. (See further discussion in section entitled "Components of Earnings".)

Balance Sheet and Capital

Total assets at June 30, 2012 amounted to $3.3 billion, a 0.1% decrease from a year earlier. Total loans at June 30, 2012 amounted to $2.4 billion, a 0.2% decrease from a year earlier, and total deposits amounted to $2.8 billion at June 30, 2012, a 3.3% increase from a year earlier.

For the fourth consecutive quarter, we experienced growth in our non-covered loan portfolio, with non-covered loans increasing by $20 million during the three months ended June 30, 2012. At June 30, 2012, non-covered loans amounted to $2.1 billion, an increase of $74 million, or 3.6%, from a year earlier. We are actively pursuing lending opportunities.

Our level of non-interest bearing checking accounts amounted to $381.4 million at June 30, 2012, an 18.0% increase from a year earlier, while interest-bearing checking accounts amounted to $472.3 million, an increase of 27.1% from a year earlier. Contributing to the increase in interest-bearing checking accounts was a shift into this category from customer repurchase agreements as a result of the repeal on the prohibition of banks paying interest on commercial deposit accounts. The overall growth in checking and other transaction accounts has allowed us to reduce our reliance on higher cost time deposits.

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In September 2011, we issued $63.5 million in preferred stock to the U.S. Treasury as part of the Company's participation in the Small Business Lending Fund ("SBLF"). The goal of the SBLF is to incentivize healthy banks to make loans to small businesses. Depending on the Bank's success in making small business loans, the dividend rate on the preferred stock could range from 5% to as low as 1% for several years. For the third quarter of 2012, we expect to pay a dividend rate of 4.3%.

We remain well-capitalized by all regulatory standards, with a Total Risk-Based Capital Ratio at June 30, 2012 of 16.23% compared to the 10.00% minimum to be considered well-capitalized. Our tangible common equity to tangible assets ratio was 6.36% at June 30, 2012, a decrease of 29 basis points from a year earlier.

Components of Earnings

Net interest income is the largest component of earnings, representing the difference between interest and fees generated from earning assets and the interest costs of deposits and other funds needed to support those assets. Net interest income for the three month period ended June 30, 2012 amounted to $33.0 million, a decrease of $1.5 million, or 4.4%, from the $34.5 million recorded in the second quarter of 2011. Net interest income on a tax-equivalent basis for the three month period ended June 30, 2012 amounted to $33.3 million, a decrease of $1.5 million, or 4.4%, from the $34.9 million recorded in the second quarter of 2011. We believe that analysis of net interest income on a tax-equivalent basis is useful and appropriate because it allows a comparison of net interest income amounts in different periods without taking into account the different mix of taxable versus non-taxable investments that may have existed during those periods.

	Three Months Ended June 30,	
($ in thousands)	2012	2011
Net interest income, as reported	$ 32,951	34,480
Tax-equivalent adjustment	387	388
Net interest income, tax-equivalent	$ 33,338	34,868

Net interest income for the six month period ended June 30, 2012 amounted to $65.0 million, a decrease of $1.8 million, or 2.6%, from the $66.8 million recorded in the second quarter of 2011. Net interest income on a tax-equivalent basis for the six month period ended June 30, 2012 amounted to $65.8 million, a decrease of $1.8 million, or 2.6%, from the $67.6 million recorded in the second quarter of 2011.

	Six Months Ended June 30,	
($ in thousands)	2012	2011
Net interest income, as reported	$ 65,042	66,794
Tax-equivalent adjustment	774	773
Net interest income, tax-equivalent	$ 65,816	67,567

There are two primary factors that cause changes in the amount of net interest income we record - 1) changes in our loans and deposits balances, and 2) our net interest margin (tax-equivalent net interest income divided by average interest-earning assets).

For the three and six months ended June 30, 2012, the lower net interest income compared to the same periods of 2011 was primarily due to a lower net interest margin, which is discussed in more detail below.

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The following table presents net interest income analysis on a tax-equivalent basis.

	For the Three Months Ended June 30,					
	2012			2011		
($ in thousands)	Average Volume	Average Rate	Interest Earned or Paid	Average Volume	Average Rate	Interest Earned or Paid
Assets						
Loans (1)	$2,438,471	5.88%	$35,636	$2,471,915	6.24%	$38,464
Taxable securities	164,053	2.82%	1,149	184,125	3.19%	1,463
Non-taxable securities (2)	56,650	6.23%	878	57,720	6.16%	887
Short-term investments, principally federal funds	204,692	0.35%	178	129,057	0.32%	103
Total interest-earning assets	2,863,866	5.31%	37,841	2,842,817	5.77%	40,917
Cash and due from banks	56,310			74,610		
Premises and equipment	73,096			68,336		
Other assets	320,492			341,475		
Total assets	$3,313,764			$3,327,238		
Liabilities						
Interest bearing checking	$454,923	0.17%	$190	$350,094	0.21%	$184
Money market deposits	536,288	0.37%	491	507,381	0.57%	723
Savings deposits	159,850	0.20%	78	154,624	0.51%	196
Time deposits >$100,000	733,630	1.14%	2,085	778,235	1.37%	2,661
Other time deposits	559,810	0.84%	1,169	660,551	1.07%	1,767
Total interest-bearing deposits	2,444,501	0.66%	4,013	2,450,885	0.91%	5,531
Securities sold under agreements to repurchase	—	—	—	56,756	0.34%	48
Borrowings	127,878	1.54%	490	109,481	1.72%	470
Total interest-bearing liabilities	2,572,379	0.70%	4,503	2,617,122	0.93%	6,049
Non-interest-bearing deposits	367,172			335,113		
Other liabilities	31,861			22,384		
Shareholders' equity	342,352			352,619		
Total liabilities and shareholders' equity	$3,313,764			$3,327,238		
Net yield on interest-earning assets and net interest income		4.68%	$33,338		4.92%	$34,868
Interest rate spread		4.61%			4.84%	
Average prime rate		3.25%			3.25%	

(1) Average loans include nonaccruing loans, the effect of which is to lower the average rate shown.

(2) Includes tax-equivalent adjustments of $387,000 and $388,000 in 2012 and 2011, respectively, to reflect the tax benefit that we receive related to tax-exempt securities, which carry interest rates lower than similar taxable investments due to their tax exempt status. This amount has been computed assuming a 39% tax rate and is reduced by the related nondeductible portion of interest expense.

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The following table presents net interest income analysis on a tax-equivalent basis.

	For the Six Months Ended June 30,					
	2012			2011		
($ in thousands)	Average Volume	Average Rate	Interest Earned or Paid	Average Volume	Average Rate	Interest Earned or Paid
Assets						
Loans (1)	$2,434,682	5.84%	$70,678	$2,486,963	6.10%	$75,271
Taxable securities	165,190	2.93%	2,407	184,914	3.16%	2,895
Non-taxable securities (2)	57,123	6.19%	1,758	57,265	6.24%	1,772
Short-term investments, principally federal funds	198,424	0.32%	317	128,287	0.30%	193
Total interest-earning assets	2,855,419	5.29%	75,160	2,857,429	5.66%	80,131
Cash and due from banks	57,532			70,747		
Premises and equipment	72,397			68,144		
Other assets	322,570			340,644		
Total assets	$3,307,918			$3,336,964		
Liabilities						
Interest bearing checking	$446,668	0.18%	$396	$337,401	0.25%	$411
Money market deposits	528,648	0.39%	1,019	509,141	0.58%	1,465
Savings deposits	156,359	0.25%	193	156,677	0.59%	457
Time deposits >$100,000	739,245	1.16%	4,260	787,888	1.35%	5,265
Other time deposits	567,346	0.86%	2,438	669,975	1.18%	3,936
Total interest-bearing deposits	2,438,266	0.69%	8,306	2,461,082	0.95%	11,534
Securities sold under agreements to repurchase	3,353	0.24%	4	57,570	0.34%	98
Borrowings	129,206	1.61%	1,034	109,147	1.72%	932
Total interest-bearing liabilities	2,570,825	0.73%	9,344	2,627,799	0.96%	12,564
Non-interest-bearing deposits	357,326			327,542		
Other liabilities	34,494			29,338		
Shareholders' equity	345,273			352,285		
Total liabilities and shareholders' equity	$3,307,918			$3,336,964		
Net yield on interest-earning assets and net interest income		4.64%	$65,816		4.77%	$67,567
Interest rate spread		4.56%			4.70%	
Average prime rate		3.25%			3.25%	

(1) Average loans include nonaccruing loans, the effect of which is to lower the average rate shown.

(2) Includes tax-equivalent adjustments of $774,000 and $773,000 in 2012 and 2011, respectively, to reflect the tax benefit that we receive related to tax-exempt securities, which carry interest rates lower than similar taxable investments due to their tax exempt status. This amount has been computed assuming a 39% tax rate and is reduced by the related nondeductible portion of interest expense.

Average loans outstanding for the second quarter of 2012 were $2.438 billion, which was 1.4% less than the average loans outstanding for the second quarter of 2011 ($2.472 billion). Average loans outstanding for the six months ended June 30, 2012 were $2.435 billion, which was 2.1% less than the average loans outstanding for the six months ended June 30, 2011 ($2.487 billion). The mix of our loan portfolio remained substantially the same at June 30, 2012 compared to December 31, 2011, with approximately 90% of our loans being real estate loans, 7% being commercial, financial, and agricultural loans, and the remaining 3% being consumer installment loans. The majority of our real estate loans are personal and commercial loans where real estate provides additional security for the loan.

The slightly lower amount of average loans outstanding in 2012 is primarily due to the resolution of loans within our “covered loan” portfolio that we assumed in two failed bank acquisitions. The resolution of $79 million of these covered loans through foreclosure, charge-off, or repayment since June 30, 2011 offset $74 million in non-covered loan growth that occurred during that same period.

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Average total deposits outstanding for the second quarter of 2012 were $2.812 billion, which was 0.9% greater than the average deposits outstanding for the second quarter of 2011 ($2.786 billion). Average deposits outstanding for the six months ended June 30, 2012 were $2.796 billion, which was 0.2% greater than the average deposits outstanding for the six months ended June 30, 2011 ($2.789 billion). Generally, we can reinvest funds from deposits at higher yields than the interest rate being paid on those deposits, and therefore increases in deposits typically result in higher amounts of net interest income.

Our net interest margin (tax-equivalent net interest income divided by average earning assets) for the second quarter of 2012 was 4.68% compared to 4.92% for the second quarter of 2011. For the six month period ended June 30, 2012, our net interest margin was 4.64% compared to 4.77% for the same period in 2011. The lower margins were primarily due to lower loan yields, as well as the mix of the Company's earning assets being more concentrated in lower yielding short-term investments in 2012 compared to a larger concentration of higher yielding loans and securities in 2011. As can be seen in the above table, average short-term investments amounted to $205 million for the second quarter of 2012, a 59% increase from the second quarter of 2011 average of $129 million, while average loan and securities balances declined during that same period. Our higher level of short-term investments was due to declining loan balances and our decision not to deploy our excess cash into higher yielding, but longer-term, securities due to the historically low interest rate environment that has been in effect.

Our net interest margin benefitted from the net accretion of purchase accounting premiums/discounts associated with the Cooperative acquisition in June 2009 and, to a lesser degree, the acquisition of Great Pee Dee Bancorp in April 2008 and the Bank of Asheville in January 2011. For the three and six months ended June 30, 2012, we recorded $3,196,000 and $5,721,000, respectively, in net accretion of purchase accounting premiums/discounts that increased net interest income. For the comparable periods of 2011, we recorded $4,065,000 and $6,565,000, respectively, in net accretion of purchase accounting premiums/discounts. The following table presents the detail of the purchase accounting adjustments that impacted net interest income.

$ in thousands	For the Three Months Ended		For the Six Months Ended	
	June 30, 2012	June 30, 2011	June 30, 2012	June 30, 2011
Interest income – reduced by premium amortization on loans	$ (116)	(116)	(232)	(221)
Interest income – increased by accretion of loan discount	3,290	4,014	5,868	6,529
Interest expense – reduced by premium amortization of deposits	22	130	55	183
Interest expense – reduced by premium amortization of borrowings	—	37	30	74
Impact on net interest income	$ 3,196	4,065	5,721	6,565

See additional information regarding net interest income in the section entitled "Interest Rate Risk."

Our provisions for loan losses and nonperforming assets remain at what we believe to be elevated levels, primarily due to high unemployment rates and declining property values in our market area that negatively impact collateral dependent real estate loans.

Our total provision for loan losses was $6.5 million for the second quarter of 2012 compared to $10.9 million in the second quarter of 2011. Our total provision for loan losses was $28.0 million for the first six months of 2012 compared to $22.3 million for the first six months of 2011. The total provision for loan losses is comprised of provision for loan losses for non-covered loans and provision for loan losses for covered loans. (See section entitled “Summary of Loan Loss Experience” below for further discussion.)

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Our non-covered nonperforming assets amounted to $132 million at June 30, 2012, compared to $122 million at December 31, 2011 and $120 million at June 30, 2011. At June 30, 2012, the ratio of non-covered nonperforming assets to total non-covered assets was 4.51%, compared to 4.30% at December 31, 2011, and 4.25% at June 30, 2011. Our outlook for nonperforming non-covered assets is consistent with the recent trend, which is that we do not expect material improvement, nor deterioration, in the near future.

Our ratio of annualized net charge-offs to average non-covered loans was 0.79% for the second quarter of 2012 compared to 1.75% in the second quarter of 2011. Our ratio of annualized net charge-offs for the six months ended June 30, 2012 was 1.14% compared to 1.87% for the first six months of 2011.

Our nonperforming assets that are covered by FDIC loss share agreements have generally declined over the past twelve months, amounting to $164 million at June 30, 2011 compared to $141 million at December 31, 2011 and $129 million at June 30, 2012. We expect covered nonperforming assets to continue to decline as we resolve covered nonperforming loans and dispose of covered other real estate owned.

Total noninterest income was $1.8 million in the second quarter of 2012 compared to $5.1 million for the second quarter of 2011, a decrease of $3.3 million that was primarily attributable to losses and write-downs on foreclosed properties (see discussion below). For the six months ended June 30, 2012 and 2011, we recorded noninterest income of $7.1 million and $19.3 million, respectively. The decrease for the six month period comparison is primarily the result of a $10.2 million bargain purchase gain recorded in the first quarter of 2011 related to our acquisition of The Bank of Asheville.

Service charges on deposit accounts amounted to $3.0 million in the second quarter of 2012 compared to $3.3 million in the second quarter of 2011. Service charges on deposit accounts amounted to $5.8 million for the first six months of 2012 compared to $5.9 million for the first six months of 2011. The decline in this category is primarily due to lower overdraft fees. The lower level of overdraft fees is primarily attributable to new regulations that took effect on July 1, 2011 that limit our ability to charge overdraft fees.

Other service charges, commissions and fees amounted to $2.3 million in the second quarter of 2012 compared to $2.1 million in the second quarter of 2011. Other service charges, commissions and fees amounted to $4.5 million for the first six months of 2012 compared to $4.0 million for the first six months of 2011. The increases in 2012 are primarily attributable to increased debit card usage by our customers. We earn a small fee each time our customers make a debit card transaction.

Fees from presold mortgages amounted to $0.5 million in the second quarter of 2012 compared to $0.3 million in the second quarter of 2011. Fees from presold mortgages amounted to $0.9 million for the first six months of 2012 compared to $0.6 million for the first six months of 2011. The increase in these fees is primarily attributable to the low interest rate environment for home loans, which has increased refinance activity.

We continue to experience losses and write-downs on our foreclosed properties due to declining property values in our market area. For the second quarter of 2012, these losses amounted to $6.6 million for covered properties compared to $2.6 million in the second quarter of 2011. For the first six months of 2012, losses on covered properties amounted to $11.1 million compared to $7.5 million for the same period in 2011.

Losses on non-covered foreclosed properties amounted to $1.3 million for the second quarter of 2012 compared to $0.3 million in 2011. For the six months ended June 30, 2012, losses on non-covered foreclosed properties amounted to $2.0 million compared to $1.6 million for the same period of 2011.

As previously discussed, indemnification asset income is recorded to reflect additional amounts expected to be received from the FDIC due to covered loan and foreclosed property losses arising during the period. For the second quarter of 2012, indemnification asset income totaled $3.6 million compared to $1.8 million in the second quarter of 2011. For the six months ended June 30, 2012, indemnification asset income amounted to $7.7 million compared to $6.9 million for the same period of 2011.

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We recorded $0.4 million in gains on sales of securities during the first six months of 2012 compared to $0.1 million in the comparable period of 2011.

Noninterest expenses amounted to $23.4 million in the second quarter of 2012, a 2.3% increase from the $22.9 million recorded in the same period of 2011. Noninterest expenses for the six months ended June 30, 2012 amounted to $47.8 million, a 0.3% decrease from the $48.0 million recorded in the first six months of 2011.

Salaries expense amounted to $10.2 million in the second quarter of 2012 compared to $9.7 million for the second quarter of 2011. Salaries expense amounted to $20.3 million for the first half of 2012 compared to $19.4 million for comparable period of 2011. The increase in salary expense in 2012 is primarily associated with the hiring of additional employees in order to build our infrastructure and an initiative to expand our wealth management capabilities.

Employee benefit expense amounted to $2.8 million in the second quarter of 2012 compared to $3.0 million for the second quarter of 2011. This decrease is primarily due lower pension expense, which amounted to $0.6 million in the second quarter of 2012 compared to $0.8 million in the second quarter of 2011. The $0.6 million in pension expense we recorded in the second quarter of 2012 was a decline from the $1.0 million in pension expense in the first quarter of 2012. During the second quarter of 2012, we reviewed and adjusted certain assumptions used to calculate pension expense. These included a change in expected salary increases, which was changed from 5% to 3.5%, and a change in the assumption that all employees retire at age 65, which was changed to assume retirements occur on a graded basis from age 58 to age 70 based on a study of actual historical retirements. Employee benefit expense amounted to $6.7 million for the first half of 2012 compared to $6.2 million for comparable period of 2011. The increase was primarily due to higher health care costs in 2012.

Other operating expenses amounted to $7.5 million and $7.1 million for the second quarters of 2012 and 2011, respectively, and $14.7 million and $15.9 million for six month periods ended June 30, 2012 and 2011, respectively. The increase in the second quarter of 2012 compared to the second quarter of 2011 was due to generally higher expenses, with other operating expenses for the second quarter of 2011 being somewhat lower than most recent quarters. The decline in other operating expenses when comparing the first half of 2012 to the first half of 2011 was primarily due to lower FDIC insurance premiums as a result of a change in the FDIC’s assessment methodology that was effective April 1, 2011.

One of the largest categories of other operating expenses is collection expenses. Collection expenses on non-covered assets remained relatively stable for the periods presented amounting to approximately $0.8 million for both the second quarter of 2012 and 2011, and $1.45 million for the first half of both 2012 and 2011. Collection expenses on covered assets (net of FDIC reimbursement) decreased in both periods and amounted to $0.3 and $0.8 million for the three and six months ended June 30, 2012, respectively, compared to $0.6 million and $1.4 million for the three and six months ended June 30, 2011, respectively.

Merger expenses associated with The Bank of Asheville acquisition in January 2011 amounted to $243,000 and $594,000 for the three and six months ended June 30, 2011. There were no comparable merger expenses in 2012.

For the second quarter of 2012, the provision for income taxes was $1.5 million, an effective tax rate of 31.5%, compared to $2.0 million, an effective tax rate of 35.2%, for the same period of 2011. We recorded an income tax benefit of $1.8 million for the first six months of 2012 due to the net loss reported in the first quarter of 2012. For the first six months of 2011, the provision for income taxes was $5.8 million, an effective tax rate of 36.3%.

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The Consolidated Statements of Comprehensive Income reflect other comprehensive income of $171,000 and $783,000 during the second quarters of 2012 and 2011, respectively, and other comprehensive income of $521,000 and $979,000 for the six months ended June 30, 2012 and 2011, respectively. The primary component of other comprehensive income for the periods presented was changes in unrealized holding gains of our available for sale securities. Our available for sale securities portfolio is predominantly comprised of fixed rate bonds that generally increase in value when market yields for fixed rate bonds decrease and decline in value when market yields for fixed rate bonds increase. Management has evaluated any unrealized losses on individual securities at each period end and determined that there is no other-than-temporary impairment.

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FINANCIAL CONDITION

Total assets at June 30, 2012 amounted to $3.33 billion, 0.1% lower than a year earlier. Total loans at June 30, 2012 amounted to $2.44 billion, a 0.2% decrease from a year earlier, and total deposits amounted to $2.84 billion, a 3.3% increase from a year earlier.

The following table presents information regarding the nature of our growth for the twelve months ended June 30, 2012 and for the first six months of 2012.

July 1, 2011 to June 30, 2012	Balance at beginning of period ($ in thousands)	Internal Growth	Growth from Acquisitions	Balance at end of period	Total percentage growth	Percentage growth, excluding acquisitions
Loans – Non-covered	$2,040,714	74,192	—	2,114,906	3.6%	3.6%
Loans – Covered	401,726	(78,831)	—	322,895	-19.6%	-19.6%
Total loans	$2,442,440	(4,639)	—	2,437,801	-0.2%	-0.2%
Deposits – Noninterest bearing checking	$323,223	58,130	—	381,353	18.0%	18.0%
Deposits – Interest bearing checking	371,693	100,649	—	472,342	27.1%	27.1%
Deposits – Money market	497,112	44,207	—	541,319	8.9%	8.9%
Deposits – Savings	145,576	14,561	—	160,137	10.0%	10.0%
Deposits – Brokered	175,161	(23,074)	—	152,087	-13.2%	-13.2%
Deposits – Internet time	40,677	(17,238)	—	23,439	-42.4%	-42.4%
Deposits – Time>$100,000	567,722	(9,894)	—	557,828	-1.7%	-1.7%
Deposits – Time<$100,000	626,254	(76,461)	—	549,793	-12.2%	-12.2%
Total deposits	$2,747,418	90,880	—	2,838,298	3.3%	3.3%
January 1, 2012 to June 30, 2012						
Loans – Non-covered	$2,069,152	45,754	—	2,114,906	2.2%	2.2%
Loans – Covered	361,234	(38,339)	—	322,895	-10.6%	-10.6%
Total loans	$2,430,386	7,415	—	2,437,801	0.3%	0.3%
Deposits – Noninterest bearing checking	$335,833	45,520	—	381,353	13.6%	13.6%
Deposits – Interest bearing checking	423,452	48,890	—	472,342	11.5%	11.5%
Deposits – Money market	509,801	31,518	—	541,319	6.2%	6.2%
Deposits – Savings	146,481	13,656	—	160,137	9.3%	9.3%
Deposits – Brokered	157,408	(5,321)	—	152,087	-3.4%	-3.4%
Deposits – Internet time	29,902	(6,463)	—	23,439	-21.6%	-21.6%
Deposits – Time>$100,000	575,408	(17,580)	—	557,828	-3.1%	-3.1%

Deposits – Time<$100,000	576,752	(26,959)	—	549,793	-4.7%	-4.7%
Total deposits	$2,755,037	83,261	—	2,838,298	3.0%	3.0%

As derived from the table above, for the twelve months preceding June 30, 2012, our non-covered loans increased by $74 million, or 3.6%, which was offset by declines in our covered loans of $79 million. Over that same period, total deposits increased $91 million, or 3.3%. For the first six months of 2012, non-covered loans increased $46 million, or 2.2%, which was partially offset by declines in our covered loans of $38 million. During the first six months of 2012, total deposits increased by $83 million, or 3.0%. We had no acquisitions during the periods presented. We have experienced growth in our non-covered loan portfolio during the periods presented, and we are actively pursuing lending opportunities in order to improve our asset yields, as well as to potentially decrease the dividend rate on our SBLF preferred stock (see Note 14 to the consolidated financial statements for more information).

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For the six and twelve months preceding June 30, 2012, internal growth in our lowest cost deposits outpaced the decline in our higher cost deposits, which resulted in a net increase in deposits. A portion of the $101 million increase in interest bearing checking accounts during the twelve months preceding June 30, 2012 was caused by the shifting of repurchase agreements (securities sold under agreements to repurchase) to interest bearing checking accounts during late 2011 and early 2012. In July 2011, the Dodd-Frank Act repealed certain sections of the Federal Reserve Act that prohibited payment of interest on commercial demand accounts. With this prohibition removed, we began to pay interest on certain types of commercial demand accounts, as we encouraged our customers with repurchase agreements to switch to commercial checking accounts, which eliminated the need to sell/pledge our investment securities. Securities sold under agreements to repurchase were $69 million at June 30, 2011, $17 million at December 31, 2011 and $0 at June 30, 2012.

The mix of our loan portfolio remains substantially the same at June 30, 2012 compared to December 31, 2011. The majority of our real estate loans are personal and commercial loans where real estate provides additional security for the loan.

Note 7 to the consolidated financial statements presents additional detailed information regarding our mix of loans, including a break-out between loans covered by FDIC loss share agreements and non-covered loans.

Nonperforming Assets

Nonperforming assets include nonaccrual loans, troubled debt restructurings, loans past due 90 or more days and still accruing interest, and other real estate. As previously discussed, as a result of two FDIC-assisted transactions, we entered into loss share agreements that afford us significant protection from losses from all loans and other real estate acquired in those acquisitions.

Because of the loss protection provided by the FDIC, the financial risk of the acquired loans and foreclosed real estate is significantly different from the risk associated with assets not covered under the loss share agreements. Accordingly, we present separately nonperforming assets subject to the loss share agreements as “covered” nonperforming assets, and nonperforming assets that are not subject to the loss share agreements as “non-covered.”

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Nonperforming assets are summarized as follows:

ASSET QUALITY DATA *($ in thousands)*	June 30, 2012	December 31, 2011	June 30, 2011
Non-covered nonperforming assets			
Nonaccrual loans	$73,918	73,566	71,570
Restructured loans – accruing	20,684	11,720	16,893
Accruing loans >90 days past due	—	—	—
Total non-covered nonperforming loans	94,602	85,286	88,463
Other real estate	37,895	37,023	31,849
Total non-covered nonperforming assets	$132,497	122,309	120,312
Covered nonperforming assets (1)			
Nonaccrual loans (2)	$39,075	41,472	37,057
Restructured loans – accruing	19,054	14,218	24,325
Accruing loans > 90 days past due	—	—	—
Total covered nonperforming loans	58,129	55,690	61,382
Other real estate	70,850	85,272	102,883
Total covered nonperforming assets	$128,979	140,962	164,265
Total nonperforming assets	$261,476	263,271	284,577
Asset Quality Ratios – All Assets			
Net charge-offs to average loans – annualized	0.96% QTD, 1.32% YTD	1.00% YTD	2.22% QTD, 2.57% YTD
Nonperforming loans to total loans	6.27%	5.80%	6.14%
Nonperforming assets to total assets	7.86%	8.00%	8.54%
Allowance for loan losses to total loans	2.19%	1.70%	1.64%
Allowance for loan losses to nonperforming loans	35.00%	29.38%	27.31%
Asset Quality Ratios – Based on Non-covered Assets only			
Net charge-offs to average non-covered loans - annualized	0.79% QTD, 1.14% YTD	1.09% YTD	1.74% QTD, 1.87% YTD
Non-covered nonperforming loans to non-covered loans	4.47%	4.12%	4.33%
Non-covered nonperforming assets to total non-covered assets	4.51%	4.30%	4.25%
Allowance for loan losses to non-covered loans	2.25%	1.72%	1.69%
Allowance for loan losses to non-covered nonperforming loans	50.23%	41.75%	38.96%

(1) Covered nonperforming assets consist of assets that are included in loss share agreements with the FDIC.

(2) At June 30, 2012, the contractual balance of the nonaccrual loans covered by FDIC loss share agreements was $60.4 million.

We have reviewed the collateral for our nonperforming assets, including nonaccrual loans, and have included this review among the factors considered in the evaluation of the allowance for loan losses discussed below.

Consistent with the weak economy in our market area, we have experienced high levels of loan losses, delinquencies and nonperforming assets compared to our historical averages.

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The following is the composition, by loan type, of all of our nonaccrual loans (covered and non-covered) at each period end, as classified for regulatory purposes:

($ in thousands)	At June 30, 2012	At December 31, 2011	At June 30, 2011
Commercial, financial, and agricultural	$ 3,270	3,300	2,755
Real estate – construction, land development, and other land loans	40,051	48,467	45,694
Real estate – mortgage – residential (1-4 family) first mortgages	25,453	24,133	27,981
Real estate – mortgage – home equity loans/lines of credit	7,574	7,255	6,534
Real estate – mortgage – commercial and other	33,819	28,491	22,907
Installment loans to individuals	2,826	3,392	2,756
Total nonaccrual loans	$ 112,993	115,038	108,627

The following segregates our nonaccrual loans at June 30, 2012 into covered and non-covered loans, as classified for regulatory purposes:

($ in thousands)	Covered Nonaccrual Loans	Non-covered Nonaccrual Loans	Total Nonaccrual Loans
Commercial, financial, and agricultural	$ 195	3,075	3,270
Real estate – construction, land development, and other land loans	16,963	23,088	40,051
Real estate – mortgage – residential (1-4 family) first mortgages	9,184	16,269	25,453
Real estate – mortgage – home equity loans/lines of credit	910	6,664	7,574
Real estate – mortgage – commercial and other	11,759	22,060	33,819
Installment loans to individuals	64	2,762	2,826
Total nonaccrual loans	$ 39,075	73,918	112,993

The following segregates our nonaccrual loans at December 31, 2011 into covered and non-covered loans, as classified for regulatory purposes:

($ in thousands)	Covered Nonaccrual Loans	Non-covered Nonaccrual Loans	Total Nonaccrual Loans
Commercial, financial, and agricultural	$ 469	2,831	3,300
Real estate – construction, land development, and other land loans	21,203	27,264	48,467
Real estate – mortgage – residential (1-4 family) first mortgages	10,134	13,999	24,133
Real estate – mortgage – home equity loans/lines of credit	1,231	6,024	7,255
Real estate – mortgage – commercial and other	8,212	20,279	28,491
Installment loans to individuals	223	3,169	3,392
Total nonaccrual loans	$ 41,472	73,566	115,038

At June 30, 2012, troubled debt restructurings (covered and non-covered) amounted to $39.7 million, compared to $25.9 million at December 31, 2011, and $41.2 million at June 30, 2011. During the three months ended June 30, 2012, as a part of a routine regulatory exam, we reclassified approximately $12 million of performing loans to “restructured loans – accruing” that had been renewed or modified in prior periods. The reclassification was for disclosure purposes only and did not impact our financial statements beyond the reclassification of these assets to a nonperforming asset category.

Other real estate includes foreclosed, repossessed, and idled properties. Non-covered other real estate has increased over the past year, amounting to $37.9 million at June 30, 2012, $37.0 million at December 31, 2011, and $31.8 million at June 30, 2011. At June 30, 2012, we also held $70.9 million in other real estate that is subject to the loss share agreements with the FDIC, which is a decline from $85.3 million at December 31, 2011 and $102.9 million at June 30, 2011. We believe that the fair values of the items of other real estate, less estimated costs to sell, equal or exceed their respective carrying values at the dates presented.

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The following table presents the detail of all of our other real estate at each period end (covered and non-covered):

($ in thousands)	At June 30, 2012	At December 31, 2011	At June 30, 2011
Vacant land	$ 67,128	76,341	88,239
1-4 family residential properties	28,475	33,724	37,349
Commercial real estate	13,142	12,230	9,144
Total other real estate	$ 108,745	122,295	134,732

The following segregates our other real estate at June 30, 2012 into covered and non-covered:

($ in thousands)	Covered Other Real Estate	Non-covered Other Real Estate	Total Other Real Estate
Vacant land	$ 50,572	16,556	67,128
1-4 family residential properties	12,870	15,605	28,475
Commercial real estate	7,408	5,734	13,142
Total other real estate	$ 70,850	37,895	108,745

The following segregates our other real estate at December 31, 2011 into covered and non-covered:

($ in thousands)	Covered Other Real Estate	Non-covered Other Real Estate	Total Other Real Estate
Vacant land	$ 59,994	16,347	76,341
1-4 family residential properties	17,362	16,362	33,724
Commercial real estate	7,916	4,314	12,230
Total other real estate	$ 85,272	37,023	122,295

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The following table presents geographical information regarding our nonperforming assets at June 30, 2012.

	As of June 30, 2012					
($ in thousands)	Covered	Non-covered	Total	Total Loans	Nonperforming Loans to Total Loans	
Nonaccrual loans and Troubled Debt Restructurings (1)						
Eastern Region (NC)	$51,367	26,960	78,327	$542,000	14.5	%
Triangle Region (NC)	—	29,953	29,953	780,000	3.8	%
Triad Region (NC)	—	14,722	14,722	383,000	3.8	%
Charlotte Region (NC)	—	3,546	3,546	97,000	3.7	%
Southern Piedmont Region (NC)	642	3,440	4,082	219,000	1.9	%
Western Region (NC)	6,072	5	6,077	62,000	9.8	%
South Carolina Region	48	9,397	9,445	135,000	7.0	%
Virginia Region	—	5,170	5,170	210,000	2.5	%
Other	—	1,409	1,409	10,000	14.1	%
Total nonaccrual loans and troubled debt restructurings	$58,129	94,602	152,731	$2,438,000	6.3	%
Other Real Estate (1)						
Eastern Region (NC)	$57,263	10,492	67,755			
Triangle Region (NC)	—	8,426	8,426			
Triad Region (NC)	—	8,481	8,481			
Charlotte Region (NC)	—	3,638	3,638			
Southern Piedmont Region (NC)	—	1,259	1,259			
Western Region (NC)	13,499	—	13,499			
South Carolina Region	88	4,890	4,978			
Virginia Region	—	709	709			
Other	—	—	—			
Total other real estate	70,850	37,895	108,745			

(1) The counties comprising each region are as follows:

Eastern North Carolina Region - New Hanover, Brunswick, Duplin, Dare, Beaufort, Onslow, Carteret

Triangle North Carolina Region - Moore, Lee, Harnett, Chatham, Wake

Triad North Carolina Region - Montgomery, Randolph, Davidson, Rockingham, Guilford, Stanly

Southern Piedmont North Carolina Region - Anson, Richmond, Scotland, Robeson, Bladen, Columbus

Western North Carolina Region – Buncombe

South Carolina Region - Chesterfield, Dillon, Florence, Horry

Virginia Region - Wythe, Washington, Montgomery, Pulaski

Charlotte North Carolina Region - Iredell, Cabarrus, Rowan

Summary of Loan Loss Experience

The allowance for loan losses is created by direct charges to operations. Losses on loans are charged against the allowance in the period in which such loans, in management's opinion, become uncollectible. The recoveries realized during the period are credited to this allowance.

We have no foreign loans, few agricultural loans and do not engage in significant lease financing or highly leveraged transactions. Commercial loans are diversified among a variety of industries. The majority of our real estate loans are primarily personal and commercial loans where real estate provides additional security for the loan. Collateral for virtually all of these loans is located within our principal market area.

The current economic environment has resulted in an increase in our classified and nonperforming assets, which has led to elevated provisions for loan losses. Our total provision for loan losses was $28.0 million for the first six months of 2012 compared to $22.3 million in the first six months of 2011. The total provision for loan losses is comprised of provisions for loan losses for non-covered loans and provisions for loan losses for covered loans, as discussed in the following paragraphs.

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The provision for loan losses on non-covered loans amounted to $5.2 million in the second quarter of 2012 compared to $7.6 million in the second quarter of 2011. The decline in provision was primarily due to stabilization in our assessment of the losses associated with our nonperforming non-covered loans. For the six months ended June 30, 2012 and 2011, our provision for loan losses on non-covered loans amounted to $23.8 million and $15.2 million, respectively. The increase resulted from refinements to our loan loss model and internal control changes that resulted in a realignment of departmental responsibilities for determining our allowance for loan losses. As a result of the changes, an internal review of selected nonperforming loan relationships was conducted, which applied more conservative assumptions to estimate the probable losses. We believe that the additional reserves established may lead to a more timely resolution of the related credits.

A part of the departmental realignment involved a reassignment of the responsibility for determining our allowance for loan loss amount at period end. Concurrent with this change, we performed a new review of the Company's nonperforming loans and significant classified lending relationships. As a result of this review, approximately 30 loan relationships were identified in which additional provisions for loan losses were necessary when more conservative judgments were applied to the repayment assumptions associated with the borrowers. The total additional provisions for losses associated with these borrowers was approximately $11 million. The majority of the additional provision was concentrated in construction and land development real estate, commercial real estate, and residential real estate loan categories.

For the three months ended June 30, 2012 and 2011, we recorded $1.3 million and $3.3 million in provisions for loan losses for covered loans, respectively. We recorded $4.3 million and $7.1 million in provisions for loan losses for covered loans for the six months ended June 30, 2012 and 2011, respectively. The lower provisions in 2012 were due to stabilization in our assessment of the losses associated with our nonperforming covered loans. Because of the FDIC loss-share agreements in place for these loans, the FDIC indemnification asset was adjusted upwards by recording noninterest income of $1.0 million and $2.7 million in the second quarters of 2012 and 2011, respectively, and $3.4 million and $5.7 million for the first six months of 2012 and 2011, respectively, or 80% of the amount of the provisions.

For the first six months of 2012, we recorded $16.0 million in net charge-offs, compared to $31.7 million for the comparable period of 2011. The net charge-offs in 2012 included $4.1 million of covered loans and $11.8 million of non-covered loans, whereas in 2011 net charge-offs included $12.7 million of covered loans and $19.0 million of non-covered loans. During 2011, a large amount of loans that had specific reserves due to concerns about collectability were determined to be confirmed losses and partial charge-offs were recorded. The charge-offs in 2012 continue a trend that began in 2010, with charge-offs being concentrated in the construction and land development real estate categories. These types of loans have been impacted the most by the recession and decline in new housing.

The allowance for loan losses amounted to $53.5 million at June 30, 2012, compared to $41.4 million at December 31, 2011 and $40.0 million at June 30, 2011. At June 30, 2012, December 31, 2011, and June 30, 2011, the allowance for loan losses attributable to covered loans was $5.9 million, $5.8 million, and $5.5 million, respectively. The allowance for loan losses for non-covered loans amounted to $47.5 million, $35.6 million, and $34.5 million at June 30, 2012, December 31, 2011, and June 30, 2011, respectively. The increase in the allowance for losses at June 30, 2012

compared to prior periods is primarily due to the high provision for loan losses recorded in the first quarter of 2012 that was recorded as an addition to the allowance for loan losses without a corresponding increase in charge-offs.

We believe our reserve levels are adequate to cover probable loan losses on the loans outstanding as of each reporting date. It must be emphasized, however, that the determination of the reserve using our procedures and methods rests upon various judgments and assumptions about economic conditions and other factors affecting loans. No assurance can be given that we will not in any particular period sustain loan losses that are sizable in relation to the amounts reserved or that subsequent evaluations of the loan portfolio, in light of conditions and factors then prevailing, will not require significant changes in the allowance for loan losses or future charges to earnings. See “Critical Accounting Policies – Allowance for Loan Losses” above.

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In addition, various regulatory agencies, as an integral part of their examination process, periodically review our allowance for loan losses and value of other real estate. Such agencies may require us to recognize adjustments to the allowance or the carrying value of other real estate based on their judgments about information available at the time of their examinations.

For the periods indicated, the following table summarizes our balances of loans outstanding, average loans outstanding, changes in the allowance for loan losses arising from charge-offs and recoveries, additions to the allowance for loan losses that have been charged to expense, and additions that were recorded related to acquisitions.

($ in thousands)	Six Months Ended June 30, 2012	Twelve Months Ended December 31, 2011	Six Months Ended June 30, 2011
Loans outstanding at end of period	$2,437,801	2,430,386	2,442,440
Average amount of loans outstanding	$2,434,682	2,461,995	2,486,963
Allowance for loan losses, at beginning of year	$41,418	49,430	49,430
Provision for loan losses	28,022	41,301	22,277
	69,440	90,731	71,707
Loans charged off:			
Commercial, financial, and agricultural	(1,627)	(2,358)	(1,077)
Real estate – construction, land development & other land loans	(6,773)	(25,604)	(17,528)
Real estate – mortgage – residential (1-4 family) first mortgages	(3,007)	(12,045)	(7,966)
Real estate – mortgage – home equity loans / lines of credit	(1,261)	(3,195)	(1,458)
Real estate – mortgage – commercial and other	(2,939)	(7,180)	(3,434)
Installment loans to individuals	(1,279)	(1,600)	(1,066)
Total charge-offs	(16,886)	(51,982)	(32,529)
Recoveries of loans previously charged-off:			
Commercial, financial, and agricultural	31	314	27
Real estate – construction, land development & other land loans	490	919	255
Real estate – mortgage – residential (1-4 family) first mortgages	50	492	140
Real estate – mortgage – home equity loans / lines of credit	146	375	121
Real estate – mortgage – commercial and other	29	119	32
Installment loans to individuals	154	450	252
Total recoveries	900	2,669	827
Net charge-offs	(15,986)	(49,313)	(31,702)
Allowance for loan losses, at end of period	$53,454	41,418	40,005
Ratios:			
Net charge-offs as a percent of average loans	1.32%	2.00%	2.57%
Allowance for loan losses as a percent of loans at end of period	2.19%	1.70%	1.64%

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The following table discloses the activity in the allowance for loan losses for the six months ended June 30, 2012, segregated into covered and non-covered.

($ in thousands)	As of and for the six months ended June 30, 2012 Covered	Non-covered	Total
Loans outstanding at end of period	$322,895	2,114,906	2,437,801
Average amount of loans outstanding	$342,077	2,092,605	2,434,682
Allowance for loan losses, at beginning of year	$5,808	35,610	41,418
Provision for loan losses	4,271	23,751	28,022
	10,079	59,361	69,440
Loans charged off:			
Commercial, financial, and agricultural	—	(1,627)	(1,627)
Real estate – construction, land development & other land loans	(2,522)	(4,251)	(6,773)
Real estate – mortgage – residential (1-4 family) first mortgages	(881)	(2,126)	(3,007)
Real estate – mortgage – home equity loans / lines of credit	(153)	(1,108)	(1,261)
Real estate – mortgage – commercial and other	(445)	(2,494)	(2,939)
Installment loans to individuals	(147)	(1,132)	(1,279)
Total charge-offs	(4,148)	(12,738)	(16,886)
Recoveries of loans previously charged-off:			
Commercial, financial, and agricultural	—	31	31
Real estate – construction, land development & other land loans	—	490	490
Real estate – mortgage – residential (1-4 family) first mortgages	—	50	50
Real estate – mortgage – home equity loans / lines of credit	—	146	146
Real estate – mortgage – commercial and other	—	29	29
Installment loans to individuals	—	154	154
Total recoveries	—	900	900
Net charge-offs	(4,148)	(11,838)	(15,986)
Allowance for loan losses, at end of period	$5,931	47,523	53,454

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The following table discloses the activity in the allowance for loan losses for the six months ended June 30, 2011, segregated into covered and non-covered.

($ in thousands)	As of and for the six months ended June 30, 2011 Covered	Non-covered	Total
Loans outstanding at end of period	$401,726	2,040,714	2,442,440
Average amount of loans outstanding	$436,859	2,050,104	2,486,963
Allowance for loan losses, at beginning of year	$11,155	38,275	49,430
Provision for loan losses	7,100	15,177	22,277
	18,255	53,452	71,707
Loans charged off:			
Commercial, financial, and agricultural	(13)	(1,064)	(1,077)
Real estate – construction, land development & other land loans	(7,954)	(9,574)	(17,528)
Real estate – mortgage – residential (1-4 family) first mortgages	(3,393)	(4,573)	(7,966)
Real estate – mortgage – home equity loans / lines of credit	(198)	(1,260)	(1,458)
Real estate – mortgage – commercial and other	(1,052)	(2,382)	(3,434)
Installment loans to individuals	(105)	(961)	(1,066)
Total charge-offs	(12,715)	(19,814)	(32,529)
Recoveries of loans previously charged-off:			
Commercial, financial, and agricultural	—	27	27
Real estate – construction, land development & other land loans	—	255	255
Real estate – mortgage – residential (1-4 family) first mortgages	—	140	140
Real estate – mortgage – home equity loans / lines of credit	—	121	121
Real estate – mortgage – commercial and other	—	32	32
Installment loans to individuals	—	252	252
Total recoveries	—	827	827
Net charge-offs	(12,715)	(18,987)	(31,702)
Allowance for loan losses, at end of period	$5,540	34,465	40,005

Based on the results of our loan analysis and grading program and our evaluation of the allowance for loan losses at June 30, 2012, there have been no material changes to the allocation of the allowance for loan losses among the various categories of loans since December 31, 2011.

Liquidity, Commitments, and Contingencies

Our liquidity is determined by our ability to convert assets to cash or acquire alternative sources of funds to meet the needs of our customers who are withdrawing or borrowing funds, and to maintain required reserve levels, pay expenses and operate the Company on an ongoing basis. Our primary liquidity sources are net income from operations, cash and due from banks, federal funds sold and other short-term investments. Our securities portfolio is comprised almost entirely of readily marketable securities, which could also be sold to provide cash.

In addition to internally generated liquidity sources, we have the ability to obtain borrowings from the following sources - 1) an approximately $393 million line of credit with the Federal Home Loan Bank (of which $65 million was outstanding at June 30, 2012), 2) a $50 million overnight federal funds line of credit with a correspondent bank (none of which was outstanding at June 30, 2012), and 3) an approximately $92 million line of credit through the Federal Reserve Bank of Richmond’s discount window (none of which was outstanding at June 30, 2012). In addition to the outstanding borrowings from the FHLB that reduce the available borrowing capacity of that line of credit, our borrowing capacity was further reduced by $143 million at June 30, 2012 and $203 million at December 31, 2011, as a result of our pledging letters of credit for public deposits at each of those dates. Unused and available lines of credit amounted to $327 million at June 30, 2012 compared to $227 million at December 31, 2011.

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Our overall liquidity has increased since June 30, 2011. Our loans have decreased $5 million, while our deposits have increased by $91 million. As a result, our liquid assets (cash and securities) as a percentage of our total deposits and borrowings increased from 15.8% at June 30, 2011 to 16.6% at June 30, 2012.

We believe our liquidity sources, including unused lines of credit, are at an acceptable level and remain adequate to meet our operating needs in the foreseeable future. We will continue to monitor our liquidity position carefully and will explore and implement strategies to increase liquidity if deemed appropriate.

The amount and timing of our contractual obligations and commercial commitments has not changed materially since December 31, 2011, detail of which is presented in Table 18 on page 80 of our 2011 Annual Report on Form 10-K.

We are not involved in any legal proceedings that, in our opinion, are likely to have a material effect on our consolidated financial position.

Off-Balance Sheet Arrangements and Derivative Financial Instruments

Off-balance sheet arrangements include transactions, agreements, or other contractual arrangements pursuant to which we have obligations or provide guarantees on behalf of an unconsolidated entity. We have no off-balance sheet arrangements of this kind other than letters of credit and repayment guarantees associated with our trust preferred securities.

Derivative financial instruments include futures, forwards, interest rate swaps, options contracts, and other financial instruments with similar characteristics. We have not engaged in derivative activities through June 30, 2012, and have no current plans to do so.

Capital Resources

We are regulated by the Board of Governors of the Federal Reserve Board (FED) and are subject to the securities registration and public reporting regulations of the Securities and Exchange Commission. Our banking subsidiary is regulated by the Federal Deposit Insurance Corporation (FDIC) and the North Carolina Office of the Commissioner of Banks. We are not aware of any recommendations of regulatory authorities or otherwise which, if they were to be implemented, would have a material effect on our liquidity, capital resources, or operations.

We must comply with regulatory capital requirements established by the FED and FDIC. Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional discretionary, actions by regulators that, if undertaken, could have a direct material effect on our financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, we must meet specific capital guidelines that involve quantitative measures of our assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. Our capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. These capital standards require us to maintain minimum ratios of “Tier 1” capital to total risk-weighted assets and total capital to risk-weighted assets of 4.00% and 8.00%, respectively. Tier 1 capital is comprised of total shareholders’ equity calculated in accordance with generally accepted accounting principles, excluding accumulated other comprehensive income (loss), less intangible assets, and total capital is comprised of Tier 1 capital plus certain adjustments, the largest of which is our allowance for loan losses. Risk-weighted assets refer to our on- and off-balance sheet exposures, adjusted for their related risk levels using formulas set forth in FED and FDIC regulations.

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In addition to the risk-based capital requirements described above, we are subject to a leverage capital requirement, which calls for a minimum ratio of Tier 1 capital (as defined above) to quarterly average total assets of 3.00% to 5.00%, depending upon the institution's composite ratings as determined by its regulators. The FED has not advised us of any requirement specifically applicable to us.

At June 30, 2012, our capital ratios exceeded the regulatory minimum ratios discussed above. The following table presents our capital ratios and the regulatory minimums discussed above for the periods indicated.

	June 30, 2012	March 31, 2012	December 31, 2011	June 30, 2011
Risk-based capital ratios:				
Tier I capital to Tier I risk adjusted assets	14.96%	15.07%	15.46%	15.74%
Minimum required Tier I capital	4.00%	4.00%	4.00%	4.00%
Total risk-based capital to Tier II risk-adjusted assets	16.23%	16.34%	16.72%	17.00%
Minimum required total risk-based capital	8.00%	8.00%	8.00%	8.00%
Leverage capital ratios:				
Tier I leverage capital to adjusted most recent quarter average assets	9.98%	9.97%	10.21%	10.17%
Minimum required Tier I leverage capital	4.00%	4.00%	4.00%	4.00%

Our bank subsidiary is also subject to capital requirements similar to those discussed above. The bank subsidiary's capital ratios do not vary materially from our capital ratios presented above. At June 30, 2012, our bank subsidiary exceeded the minimum ratios established by the FED and FDIC.

In addition to regulatory capital ratios, we also closely monitor our ratio of tangible common equity to tangible assets ("TCE Ratio"). Our TCE ratio was 6.36% at June 30, 2012 compared to 6.58% at December 31, 2011 and 6.65% at June 30, 2011.

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BUSINESS DEVELOPMENT MATTERS

The following is a list of business development and other miscellaneous matters affecting First Bancorp and First Bank, our bank subsidiary.

- On April 30, 2012, First Bank entered into an agreement to assume all of the deposits and acquire certain loans of the Gateway Bank & Trust Co. branch located in Wilmington, North Carolina. The acquired accounts will be transferred to one of our existing branches that is located nearby. The transaction is subject to regulatory approval and is expected to occur in the third quarter of 2012.

- On July 2, 2012, we opened our new branch in Salem, Virginia. This branch is our 7th branch in southwestern Virginia.

- On July 3, 2012, the Branch Purchase and Assumption Agreement between Waccamaw Bank and First Bank was terminated. Waccamaw Bank was closed by the North Carolina Commissioner of Banks, which named the Federal Deposit Insurance Corporation as receiver, during June 2012.

- We are relocating our Biscoe, North Carolina branch and expect completion of the new building in the fourth quarter of 2012.

- We expect to complete the relocation of our branch in Fort Chiswell, Virginia in the fourth quarter of 2012.

- On June 18, 2012, the Company announced a quarterly cash dividend of $0.08 cents per share payable on July 25, 2012 to shareholders of record on June 30, 2012. This is the same dividend rate as the Company declared in the second quarter of 2011.

SHARE REPURCHASES

We repurchased 148 shares of our common stock during the first six months of 2012 in two private transactions. At June 30, 2012, we had approximately 214,000 shares available for repurchase under existing authority from our board of directors. We may repurchase these shares in open market and privately negotiated transactions, as market conditions and our liquidity warrants, subject to compliance with applicable regulations. See also Part II, Item 2 “Unregistered Sales of Equity Securities and Use of Proceeds.”

Item 3 – Quantitative and Qualitative Disclosures About Market Risk

INTEREST RATE RISK (INCLUDING QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK)

Net interest income is our most significant component of earnings. Notwithstanding changes in volumes of loans and deposits, our level of net interest income is continually at risk due to the effect that changes in general market interest rate trends have on interest yields earned and paid with respect to our various categories of earning assets and interest-bearing liabilities. It is our policy to maintain portfolios of earning assets and interest-bearing liabilities with maturities and repricing opportunities that will afford protection, to the extent practical, against wide interest rate fluctuations. Our exposure to interest rate risk is analyzed on a regular basis by management using standard GAP reports, maturity reports, and an asset/liability software model that simulates future levels of interest income and expense based on current interest rates, expected future interest rates, and various intervals of “shock” interest rates. Over the years, we have been able to maintain a fairly consistent yield on average earning assets (net interest margin). Over the past five calendar years, our net interest margin has ranged from a low of 3.74% (realized in 2008) to a high of 4.72% (realized in 2011). During that five year period, the prime rate of interest has ranged from a low of 3.25% (which was the rate as of June 30, 2012) to a high of 8.25% (2007). The consistency of the net interest margin is aided by the relatively low level of long-term interest rate exposure that we maintain. At June 30, 2012, approximately 83% of our interest-earning assets are subject to repricing within five years (because they are either adjustable rate assets or they are fixed rate assets that mature) and substantially all of our interest-bearing liabilities reprice within five years.

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Using stated maturities for all fixed rate instruments except mortgage-backed securities (which are allocated in the periods of their expected payback) and securities and borrowings with call features that are expected to be called (which are shown in the period of their expected call), at June 30, 2012, we had approximately $594 million more in interest-bearing liabilities that are subject to interest rate changes within one year than we had in earning assets. This generally would indicate that net interest income would experience downward pressure in a rising interest rate environment and would benefit from a declining interest rate environment. However, this method of analyzing interest sensitivity only measures the magnitude of the timing differences and does not address earnings, market value, or management actions. Also, interest rates on certain types of assets and liabilities may fluctuate in advance of changes in market interest rates, while interest rates on other types may lag behind changes in market rates. In addition to the effects of “when” various rate-sensitive products reprice, market rate changes may not result in uniform changes in rates among all products. For example, included in interest-bearing liabilities subject to interest rate changes within one year at June 30, 2012 are deposits totaling $1.2 billion comprised of checking, savings, and certain types of money market deposits with interest rates set by management. These types of deposits historically have not repriced with, or in the same proportion, as general market indicators.

Overall we believe that in the near term (twelve months), net interest income will not likely experience significant downward pressure from rising interest rates. Similarly, we would not expect a significant increase in near term net interest income from falling interest rates. Generally, when rates change, our interest-sensitive assets that are subject to adjustment reprice immediately at the full amount of the change, while our interest-sensitive liabilities that are subject to adjustment reprice at a lag to the rate change and typically not to the full extent of the rate change. In the short term (less than six months), this results in us being asset-sensitive, meaning that our net interest income benefits from an increase in interest rates and is negatively impacted by a decrease in interest rates. However, in the twelve-month horizon, the impact of having a higher level of interest-sensitive liabilities lessens the short-term effects of changes in interest rates.

The Federal Reserve has made no changes to interest rates since 2008, and since that time the difference between market driven short-term interest rates and longer-term interest rates has generally widened, with short-term interest rates steadily declining and longer-term interest rates not declining by as much. The higher long term interest rate environment enhanced our ability to require higher interest rates on loans. As it relates to funding, we have been able to reprice many of our maturing time deposits at lower interest rates. We were also able to generally decrease the rates we paid on other categories of deposits as a result of declining short-term interest rates in the marketplace and an increase in liquidity that lessened our need to offer premium interest rates.

As previously discussed in the section entitled “Net Interest Income and Net Interest Margin,” our net interest income was impacted by certain purchase accounting adjustments related primarily to our acquisitions of Cooperative Bank and The Bank of Asheville. The purchase accounting adjustments related to the premium amortization on loans, deposits and borrowings are based on amortization schedules and are thus systematic and predictable. The accretion of the loan discount on loans acquired from Cooperative Bank and The Bank of Asheville, which amounted to $5.9 million and $6.5 million for the first six months of 2012 and 2011, respectively, is less predictable and could be materially different among periods. This is because of the magnitude of the discounts that were initially recorded ($280 million in total) and the fact that the accretion being recorded is dependent on both the credit quality of the acquired loans and the impact of any accelerated loan repayments, including payoffs. If the credit quality of the loans declines, some or all of the remaining discount will cease to be accreted into income. If the underlying loans

experience accelerated paydowns or are paid off, the remaining discount will be accreted into income on an accelerated basis, which in the event of total payoff will result in the remaining discount being entirely accreted into income in the period of the payoff. Each of these factors is difficult to predict and susceptible to volatility.

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Based on our most recent interest rate modeling, which assumes no changes in interest rates for 2012 (federal funds rate = 0.25%, prime = 3.25%), we project that our net interest margin for the remainder of 2012 will remain relatively consistent with the net interest margins recently realized. We expect loan yields and deposit costs to continue to trend downwards.

We have no market risk sensitive instruments held for trading purposes, nor do we maintain any foreign currency positions.

See additional discussion regarding net interest income, as well as discussion of the changes in the annual net interest margin in the section entitled “Net Interest Income and Net Interest Margin” above.

Item 4 – Controls and Procedures

As of the end of the period covered by this report, we carried out an evaluation, under the supervision and with the participation of our chief executive officer and chief financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures, which are our controls and other procedures that are designed to ensure that information required to be disclosed in our periodic reports with the SEC is recorded, processed, summarized and reported within the required time periods. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed is communicated to our management to allow timely decisions regarding required disclosure. Based on the evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures are effective in allowing timely decisions regarding disclosure to be made about material information required to be included in our periodic reports with the SEC. In addition, no change in our internal control over financial reporting has occurred during, or subsequent to, the period covered by this report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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Part II. Other Information

Item 2 – Unregistered Sales of Equity Securities and Use of Proceeds

Issuer Purchases of Equity Securities

Period	Total Number of Shares Purchased (2)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (1)	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs (1)
April 1, 2012 to April 30, 2012				214,241
May 1, 2012 to May 31, 2012				214,241
June 1, 2012 to June 30, 2012				214,241
Total				214,241

Footnotes to the Above Table

(1) All shares available for repurchase are pursuant to publicly announced share repurchase authorizations. On July 30, 2004, the Company announced that its board of directors had approved the repurchase of 375,000 shares of the Company's common stock. The repurchase authorization does not have an expiration date. There are no plans or programs the Company has determined to terminate prior to expiration, or under which we do not intend to make further purchases.

(2) The table above does not include shares that were used by option holders to satisfy the exercise price of the call options issued by the Company to its employees and directors pursuant to the Company's stock option plans. There were no such exercises during the three months ended June 30, 2012.

There were no unregistered sales of our securities during the three months ended June 30, 2012.

Item 6 - Exhibits

The following exhibits are filed with this report or, as noted, are incorporated by reference. Management contracts, compensatory plans and arrangements are marked with an asterisk (*).

3.a Articles of Incorporation of the Company and amendments thereto were filed as Exhibits 3.a.i through 3.a.v to the Company's Quarterly Report on Form 10-Q for the period ended June 30, 2002, and are incorporated herein by reference. Articles of Amendment to the Articles of Incorporation were filed as Exhibits 3.1 and 3.2 to the

Company’s Current Report on Form 8-K filed on January 13, 2009, and are incorporated herein by reference. Articles of Amendment to the Articles of Incorporation were filed as Exhibit 3.1.b to the Company’s Registration Statement on Form S-3D filed on June 29, 2010, and are incorporated herein by reference. Articles of Amendment to the Articles of Incorporation were filed as Exhibit 3.1 to the Company’s Current Report on Form 8-K filed on September 6, 2011, and are incorporated herein by reference.

3.b	Amended and Restated Bylaws of the Company were filed as Exhibit 3.1 to the Company's Current Report on Form 8-K filed on November 23, 2009, and are incorporated herein by reference.

4.a	Form of Common Stock Certificate was filed as Exhibit 4 to the Company’s Quarterly Report on Form 10-Q for the quarter ended June 30, 1999, and is incorporated herein by reference.

4.b	Form of Certificate for Series A Preferred Stock was filed as Exhibit 4.1 to the Company’s Current Report on Form 8-K filed on January 13, 2009, and is incorporated herein by reference.

4.c	Warrant for Purchase of Shares of Common Stock was filed as Exhibit 4.2 to the Company’s Current Report on Form 8-K filed on January 13, 2009, and is incorporated herein by reference.

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4.d	Form of Certificate for Series B Preferred Stock was filed as Exhibit 4.1 to the Company's Current Report on Form 8-K filed on September 6, 2011, and is incorporated herein by reference.
12	Computation of Ratio of Earnings to Fixed Charges.
31.1	Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 302(a) of the Sarbanes-Oxley Act of 2002.
31.2	Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 302(a) of the Sarbanes-Oxley Act of 2002.
32.1	Chief Executive Officer Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Chief Financial Officer Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101	The following financial information from the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2012, formatted in eXtensible Business Reporting Language (XBRL): (i) the Consolidated Balance Sheets, (ii) the Consolidated Statements of Income, (iii) the Consolidated Statements of Comprehensive Income, (iv) the Consolidated Statements of Shareholders' Equity, (v) the Consolidated Statements of Cash Flows, and (vi) the Notes to Consolidated Financial Statements. (1)

Copies of exhibits are available upon written request to: First Bancorp, Anna G. Hollers, Executive Vice President, P.O. Box 508, Troy, NC 27371

(1) As provided in Rule 406T of Regulation S-T, this information shall not be deemed "filed" for purposes of Section 11 and 12 of the Securities Act of 1933 and Section 18 of the Securities Exchange Act of 1934 or otherwise subject to liability under those sections.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

FIRST BANCORP

August 9, 2012 BY:/s/ Richard H. Moore
Richard H. Moore
President
(Principal Executive Officer),
Treasurer and Director

August 9, 2012 BY:/s/ Anna G. Hollers
Anna G. Hollers
Executive Vice President,
Secretary
and Chief Operating Officer

August 9, 2012 BY:/s/ Eric P. Credle
Eric P. Credle
Executive Vice President
and Chief Financial Officer