

Uwharrie

CAPITAL CORP

First Quarter Report – March 31, 2014

www.Uwharrie.com

June 25, 2014

Dear Shareholders:

With economic conditions showing signs of improvement, including lower unemployment rates, growing consumer confidence and expanding housing markets, first quarter 2014 proved to be a solid start of the year for Uwharrie Capital Corp. Our asset problems, for the most part, appear now to be behind us. Uwharrie Bank's classified assets, a measurement of problem loans, are one-third the level of just two years ago, reflecting substantial loan quality improvement. Total risk-based capital for the period of 16.41% compares favorably to our peers.

Ongoing operating expenses for first quarter 2014 were down \$383 thousand, as compared to first quarter 2013. This is a result of efficiencies gained through the consolidation of our three bank charters and lower expenses with improving asset quality. Net income for the first quarter was \$537 thousand. When comparing this to first quarter 2013 income of \$763 thousand, it does not appear to be favorable at first glance. However, the make-up of first quarter 2013 earnings had the benefit of a one-time \$229 thousand gain from the sale of bank-owned property and \$840 thousand from the mortgage refinancing boon that was still taking place. When taking all these factors into consideration, the income reported for first quarter represents earnings from ongoing operations, net of one-time gains and mortgage banking operations, improving \$534 thousand. Our first quarter earnings for 2014 reflect a more sustainable source of earnings from a stronger balance sheet. Asset quality, capital and operating expenses have all improved since year-end.

Our biggest challenge now is to find sources of revenue in a recovering economy. Traditionally, community banks' bread and butter, the main source of income, has been loans. At this point in the recovery, we are not seeing sufficient new loan demand in our local markets to offset the scheduled pay-downs of existing loans on our balance sheet. As a result, total assets declined marginally, down less than 1/2% from year-end, but our cash liquidity is growing (money available to lend). A greater portion of our earning assets is ending up in our securities portfolio, with much lower yields, contributing to a compression of our net interest margin. Moving from problem loans to weak loan demand and the compression of net interest margin is an issue that is common to our industry at this stage of the recovery and not unique to Uwharrie Capital Corp. Total assets at quarter-end March 2014 were \$515 million.

One area of growth that does not show up on our balance sheet is the assets under management in our wealth management group. Strategic Investment Advisors continues to provide sound advice and solutions for each customer's investment of their nest egg. Independent of a slow economic recovery, the growing number of retiring baby boomers continues. Total assets under management at the end of first quarter 2014 were \$147 million, which is a 6.52% growth over assets under management at end of first quarter 2013.

Let me close by reminding you to refer your family members, friends and neighbors to Uwharrie Bank and Strategic Investment Advisors. By so doing, you are helping to increase the value of your investment as well as contributing to the creation of greater wealth in the community.

We remain committed to *making a difference* in the communities we serve. We thank you for your continued investment and for the trust and confidence you have placed in our Company.

Sincerely,

UWHARRIE CAPITAL CORP



Roger L. Dick
President and Chief Executive Officer



Brendan P. Duffey
Chief Operating Officer

Uwharrie Capital Corp and Subsidiaries

Consolidated Balance Sheets

(Amounts in thousands except share and per share data)	March 31, 2014	March 31, 2013
Assets		
Cash and due from banks	\$ 6,607	\$ 7,350
Interest-earning deposits with banks	54,267	65,112
Investment securities available for sale	111,508	112,070
Loans held for sale	364	1,045
Loans held for investment	304,735	323,764
Less: Allowance for loan losses	4,198	5,973
Net loans held for investment	<u>300,537</u>	<u>317,791</u>
Interest receivable	1,651	1,646
Premises and equipment, net	15,356	14,150
Restricted stock	1,038	1,938
Bank-owned life insurance	6,557	6,426
Other real estate owned	7,447	10,922
Other assets	10,260	8,471
Total assets	<u>\$ 515,592</u>	<u>\$ 546,921</u>
Liabilities		
Deposits:		
Demand, noninterest-bearing	\$ 80,139	\$ 72,237
Interest checking and money market accounts	227,737	220,744
Savings accounts	38,654	45,639
Time deposits, \$100,000 and over	44,176	50,534
Other time deposits	61,503	75,321
Total deposits	<u>452,209</u>	<u>464,475</u>
Interest payable	193	262
Short-term borrowed funds	5,887	12,127
Long-term debt	9,567	12,671
Other liabilities	4,755	12,681
Total liabilities	<u>472,611</u>	<u>502,216</u>
Redeemable common stock held by the Employee Stock Ownership Plan (ESOP)	1,864	1,639
Shareholders' Equity		
Preferred stock, no par value: 10,000,000 shares authorized; 2,258 shares of series A issued and outstanding, 2013	-	2,258
500 shares of series B issued and outstanding, 2013	-	500
Discount on preferred stock	-	(75)
Common stock, \$1.25 par value: 20,000,000 shares authorized; issued and outstanding or in process of issuance 7,193,485 and 7,484,771 shares, respectively	8,992	9,356
Additional paid-in capital	11,130	12,103
Unearned ESOP compensation	-	(851)
Undivided profits	10,680	10,637
Accumulated other comprehensive income (loss)	(234)	1,396
Total Uwharrie Capital shareholders' equity	<u>30,568</u>	<u>35,324</u>
Noncontrolling interest	10,549	7,742
Total shareholders' equity	<u>41,117</u>	<u>43,066</u>
Total liabilities and shareholders' equity	<u>\$ 515,592</u>	<u>\$ 546,921</u>

Uwharrie Capital Corp and Subsidiaries

Consolidated Statements of Income

Three Months Ended
March 31,

(Amounts in thousands except share and per share data)

2014 2013

Interest Income

Interest and fees on loans	\$ 4,059	\$ 4,427
Interest on investment securities	475	338
Interest-earning deposits with banks and federal funds sold	45	55
Total interest income	<u>4,579</u>	<u>4,820</u>

Interest Expense

Interest paid on deposits	373	545
Interest on borrowed funds	175	251
Total interest expense	<u>548</u>	<u>796</u>

Net Interest Income

Provision for (recovery of) loan losses	(424)	(369)
Net interest income after provision (recovery of) for loan losses	<u>4,455</u>	<u>4,393</u>

Noninterest Income

Service charges on deposit accounts	378	405
Other service fees and commissions	937	793
Gain (loss) on sale of securities	21	14
Gain on sale of other assets	1	247
Income from mortgage loan sales	162	840
Other income	97	115
Total noninterest income	<u>1,596</u>	<u>2,414</u>

Noninterest Expense

Salaries and employee benefits	3,006	3,092
Occupancy expense	286	274
Equipment expense	170	168
Data processing	179	200
Other operating expenses	1,605	1,895
Total noninterest expense	<u>5,246</u>	<u>5,629</u>

Income before income taxes	805	1,178
Provision for income taxes	268	415
Net Income	<u>\$ 537</u>	<u>\$ 763</u>

Consolidated net income

Less: Net income attributable to noncontrolling interest	\$ (146)	\$ (103)
Net income attributable to Uwharrie Capital	<u>\$ 391</u>	<u>\$ 660</u>
Dividends - preferred stock	-	(161)
Net income available to common shareholders	<u>\$ 391</u>	<u>\$ 499</u>

Net Income Per Common Share

Basic	\$ 0.05	\$ 0.07
Assuming dilution	\$ 0.05	\$ 0.07

Weighted Average Common Shares Outstanding

Basic	7,190,614	7,307,912
Assuming dilution	7,190,614	7,307,912

Uwharrie Capital Corp

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