



April 26, 2013

CONSOLIDATED BALANCE SHEET

(UNAUDITED)

In thousands of dollars

| | March 31, | |
|---|------------------|------------------|
| | 2013 | 2012 |
| ASSETS | | |
| Cash and due from banks | \$ 10,200 | \$ 5,755 |
| Interest-bearing deposits with other financial institutions | 3,078 | 18,186 |
| Total cash and cash equivalents | 13,278 | 23,941 |
| Time deposits with other financial institutions | 14,262 | 14,054 |
| Securities available for sale | 97,739 | 74,076 |
| Securities held to maturity | 6,482 | 4,578 |
| <i>(Market value of \$6,851 in 2013 and \$4,995 in 2012)</i> | | |
| Other securities | 997 | 997 |
| Total investment securities | 105,218 | 79,651 |
| Loans | 110,238 | 119,699 |
| Less: allowance for loan losses | (3,637) | (3,804) |
| Net loans | 106,601 | 115,895 |
| Premises and equipment, net | 5,108 | 5,160 |
| Other assets | 12,216 | 13,425 |
| Total assets | <u>\$256,683</u> | <u>\$252,126</u> |
| LIABILITIES | | |
| Deposits: | | |
| Noninterest-bearing demand | \$ 54,081 | \$ 54,056 |
| Interest-bearing deposits | 178,886 | 175,572 |
| Total deposits | 232,967 | 229,628 |
| Other liabilities | 4,228 | 4,414 |
| Total liabilities | 237,195 | 234,042 |
| SHAREHOLDERS' EQUITY | | |
| Common Stock | 3,030 | 3,030 |
| Surplus | 19,499 | 19,499 |
| Retained Earnings and Accumulated other Comprehensive Income / (Loss) | (3,041) | (4,445) |
| Total shareholders' equity | 19,488 | 18,084 |
| Total liabilities and shareholders' equity | <u>\$256,683</u> | <u>\$252,126</u> |

CONSOLIDATED STATEMENT OF INCOME

(UNAUDITED)

In thousands of dollars, except per share data

| | For the three months ended March 31, | | |
|--|--------------------------------------|---------------|---------------|
| | 2013 | 2012 | 2011 |
| INTEREST INCOME | | | |
| Interest and fees on loans | \$ 1,613 | \$ 1,855 | \$ 1,938 |
| Interest on securities: | | | |
| Taxable | 217 | 196 | 281 |
| Tax exempt | 70 | 86 | 129 |
| Other interest income | 45 | 55 | 57 |
| Total interest income | 1,945 | 2,192 | 2,405 |
| INTEREST EXPENSE ON DEPOSITS | 233 | 284 | 406 |
| NET INTEREST INCOME | 1,712 | 1,908 | 1,999 |
| Provision for loan losses | 0 | 710 | 300 |
| NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES | 1,712 | 1,198 | 1,699 |
| NONINTEREST INCOME | | | |
| Service charges and fees | 220 | 232 | 237 |
| Net realized gains from sale of loans | 160 | 160 | 27 |
| Loan servicing fees, net of amortization | 4 | 2 | 23 |
| Gain on the sale of other real estate owned | - | 400 | - |
| Gain on sale of securities | 556 | 253 | - |
| Other income | 84 | 101 | 127 |
| Total noninterest income | 1,024 | 1,148 | 414 |
| NONINTEREST EXPENSES | | | |
| Salaries and benefits | 1,070 | 1,017 | 962 |
| Occupancy | 256 | 230 | 264 |
| FDIC insurance premiums | 89 | 87 | 139 |
| ORE losses and carrying costs | (30) | 31 | 40 |
| Other Expenses | 456 | 493 | 511 |
| Total noninterest expenses | 1,841 | 1,858 | 1,916 |
| INCOME BEFORE INCOME TAXES | 895 | 488 | 197 |
| Income tax expense | 268 | 123 | 13 |
| NET INCOME | <u>\$ 627</u> | <u>\$ 365</u> | <u>\$ 184</u> |
| BASIC NET INCOME PER SHARE | \$ 0.52 | \$ 0.30 | \$ 0.15 |

Dear Shareholder:

Highlights of financial performance for the first three months of 2013 follows:

- Assets totaled \$256.7 million, an increase of 1.8% compared to March 31, 2012.
- Outstanding loans were \$110.2 million, compared to \$119.7 million for the same period 2012.
- Allowance for loan losses was \$3.6 million, or 3.3% of total loans, with no loan loss provision expense for the first quarter 2013. Given the low delinquencies and decline in problems assets, the existing allowance for loan loss was determined to be adequate.
- Deposits were \$233.0 million at March 31, 2013, compared to \$229.6 million at March 31, 2012; an increase of 1.45%.
- Noninterest income included a \$556,000 gain (\$366,960 net of taxes) on the sale of securities from the partial distribution of the asset purchase proceeds from the sale of Cheboygan Memorial Hospital (CMH) to McLaren Health System. Income for the first quarter 2012 reflected a \$400,000 gain on the sale of other real estate owned as well as a \$253,000 gain on the sale of securities. These were all extraordinary items contributing to income and helping to offset prior years' related losses.
- Net income per share was \$0.52, an increase from \$0.30 for the first quarter 2012.

With respect to the asset purchase proceeds remaining from the sale of CMH, as noted \$556,000 has already been received and as the settlement process continues management remains cautiously optimistic there will be an additional recovery.

I know the improvement in financial performance results in questions relating to the resumption of dividends. Although net income for 2012 and 2013 to-date was positive, as communicated in an earlier message, by regulation the ability to pay a dividend is based on earnings for the current year, plus the aggregate of the prior two calendar years, being positive. Under this calculation, considering the loss of \$2.76 million in 2011, additional income of \$671,000 is necessary before the resumption of dividends can be considered.

I look forward to seeing you at the annual meeting on Tuesday, May 21, 2013.

Sincerely,

Susan A. Eno
President & CEO