UNITED STATES DEPARTMENT OF THE TREASURY
1500 PENNSYLVANIA AVENUE, NW
WASHINGTON, D.C. 20220

Dear Ladies and Gentlemen:

The company set forth on the signature page hereto (the "*Company*") intends to issue in a private placement the number of shares of a series of its preferred stock set forth on Schedule A hereto (the "*Preferred Shares*") and a warrant to purchase the number of shares of a series of its preferred stock set forth on Schedule A hereto (the "*Warrant*" and, together with the Preferred Shares, the "*Purchased Securities*") and the United States Department of the Treasury (the "*Investor*") intends to purchase from the Company the Purchased Securities.

The purpose of this letter agreement is to confirm the terms and conditions of the purchase by the Investor of the Purchased Securities. Except to the extent supplemented or superseded by the terms set forth herein or in the Schedules hereto, the provisions contained in the Securities Purchase Agreement – Standard Terms attached hereto as Exhibit A (the "*Securities Purchase Agreement*") are incorporated by reference herein. Terms that are defined in the Securities Purchase Agreement are used in this letter agreement as so defined. In the event of any inconsistency between this letter agreement and the Securities Purchase Agreement, the terms of this letter agreement shall govern.

Each of the Company and the Investor hereby confirms its agreement with the other party with respect to the issuance by the Company of the Purchased Securities and the purchase by the Investor of the Purchased Securities pursuant to this letter agreement and the Securities Purchase Agreement on the terms specified on Schedule A hereto.

This letter agreement (including the Schedules hereto), the Securities Purchase Agreement (including the Annexes thereto), the Disclosure Schedules and the Warrant constitute the entire agreement, and supersede all other prior agreements, understandings, representations and warranties, both written and oral, between the parties, with respect to the subject matter hereof. This letter agreement constitutes the "Letter Agreement" referred to in the Securities Purchase Agreement.

This letter agreement may be executed in any number of separate counterparts, each such counterpart being deemed to be an original instrument, and all such counterparts will together constitute the same agreement. Executed signature pages to this letter agreement may be delivered by facsimile and such facsimiles will be deemed as sufficient as if actual signature pages had been delivered.

* * *

UST No. 129

In witness whereof, this letter agreement has been duly executed and delivered by the duly authorized representatives of the parties hereto as of the date written below.

UNITED STATES DEPARTMENT OF THE TREASURY

By: ______________________________

Name: Neel Kashkari

Title: Interim Assistant Secretary For Financial Stability

COMPANY: Uwharrie Capital Corp

By: ______________________________

Name: Roger L. Dick

Title: President & CEO

Date: DEC 23 2008

UST No. 129

EXHIBIT A
(Non-Exchange-Traded QFIs, excluding S Corps
and Mutual Organizations)

SECURITIES PURCHASE AGREEMENT

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SECURITIES PURCHASE AGREEMENT – STANDARD TERMS

Recitals:

WHEREAS, the United States Department of the Treasury (the "*Investor*") may from time to time agree to purchase shares of preferred stock and warrants from eligible financial institutions which elect to participate in the Troubled Asset Relief Program Capital Purchase Program ("*CPP*");

WHEREAS, an eligible financial institution electing to participate in the CPP and issue securities to the Investor (referred to herein as the "*Company*") shall enter into a letter agreement (the "*Letter Agreement*") with the Investor which incorporates this Securities Purchase Agreement – Standard Terms;

WHEREAS, the Company agrees to expand the flow of credit to U.S. consumers and businesses on competitive terms to promote the sustained growth and vitality of the U.S. economy;

WHEREAS, the Company agrees to work diligently, under existing programs, to modify the terms of residential mortgages as appropriate to strengthen the health of the U.S. housing market;

WHEREAS, the Company intends to issue in a private placement the number of shares of the series of its Preferred Stock ("*Preferred Stock*") set forth on Schedule A to the Letter Agreement (the "*Preferred Shares*") and a warrant to purchase the number of shares of the series of its Preferred Stock ("*Warrant Preferred Stock*") set forth on Schedule A to the Letter Agreement (the "*Warrant*" and, together with the Preferred Shares, the "*Purchased Securities*") and the Investor intends to purchase (the "*Purchase*") from the Company the Purchased Securities; and

WHEREAS, the Purchase will be governed by this Securities Purchase Agreement – Standard Terms and the Letter Agreement, including the schedules thereto (the "*Schedules*"), specifying additional terms of the Purchase. This Securities Purchase Agreement – Standard Terms (including the Annexes hereto) and the Letter Agreement (including the Schedules thereto) are together referred to as this "Agreement". All references in this Securities Purchase Agreement – Standard Terms to "Schedules" are to the Schedules attached to the Letter Agreement.

NOW, THEREFORE, in consideration of the premises, and of the representations, warranties, covenants and agreements set forth herein, the parties agree as follows:

Article I
Purchase; Closing

1.1 Purchase. On the terms and subject to the conditions set forth in this Agreement, the Company agrees to sell to the Investor, and the Investor agrees to purchase from the Company, at the Closing (as hereinafter defined), the Purchased Securities for the price set forth on Schedule A (the "*Purchase Price*").

1.2 Closing.

(a) On the terms and subject to the conditions set forth in this Agreement, the closing of the Purchase (the "*Closing*") will take place at the location specified in Schedule A, at the time and on the date set forth in Schedule A or as soon as practicable thereafter, or at such other place, time and date as shall be agreed between the Company and the Investor. The time and date on which the Closing occurs is referred to in this Agreement as the "*Closing Date*".

(b) Subject to the fulfillment or waiver of the conditions to the Closing in this Section 1.2, at the Closing the Company will deliver the Preferred Shares and the Warrant, in each case as evidenced by one or more certificates dated the Closing Date and bearing appropriate legends as hereinafter provided for, in exchange for payment in full of the Purchase Price by wire transfer of immediately available United States funds to a bank account designated by the Company on Schedule A.

(c) The respective obligations of each of the Investor and the Company to consummate the Purchase are subject to the fulfillment (or waiver by the Investor and the Company, as applicable) prior to the Closing of the conditions that (i) any approvals or authorizations of all United States and other governmental, regulatory or judicial authorities (collectively, "*Governmental Entities*") required for the consummation of the Purchase shall have been obtained or made in form and substance reasonably satisfactory to each party and shall be in full force and effect and all waiting periods required by United States and other applicable law, if any, shall have expired and (ii) no provision of any applicable United States or other law and no judgment, injunction, order or decree of any Governmental Entity shall prohibit the purchase and sale of the Purchased Securities as contemplated by this Agreement.

(d) The obligation of the Investor to consummate the Purchase is also subject to the fulfillment (or waiver by the Investor) at or prior to the Closing of each of the following conditions:

(i) (A) the representations and warranties of the Company set forth in (x) Section 2.2(g) of this Agreement shall be true and correct in all respects as though made on and as of the Closing Date, (y) Sections 2.2(a) through (f) shall be true and correct in all material respects as though made on and as of the Closing Date (other than representations and warranties that by their terms speak as of another date, which representations and warranties shall be true and correct in all material respects as of such other date) and (z) Sections 2.2(h) through (v) (disregarding all qualifications or limitations set forth in such representations and warranties as to "materiality", "Company Material Adverse Effect" and words of similar import) shall be true and correct as though made on and as of the Closing Date (other than representations and warranties that by their terms speak as of another date, which representations and warranties shall be true and correct as of such other date), except to the extent that the failure of such representations and warranties referred to in this Section 1.2(d)(i)(A)(z) to be so true and correct, individually or in the aggregate, does not have and would not reasonably be expected to have a Company Material Adverse Effect and (B) the Company shall have performed in all material respects all obligations required to be performed by it under this Agreement at or prior to the Closing;

(ii) the Investor shall have received a certificate signed on behalf of the Company by a senior executive officer certifying to the effect that the conditions set forth in Section 1.2(d)(i) have been satisfied;

(iii) the Company shall have duly adopted and filed with the Secretary of State of its jurisdiction of organization or other applicable Governmental Entity the amendments to its certificate or articles of incorporation, articles of association, or similar organizational document ("*Charter*") in substantially the forms attached hereto as Annex A and Annex B (the "*Certificates of Designations*") and such filing shall have been accepted;

(iv) (A) the Company shall have effected such changes to its compensation, bonus, incentive and other benefit plans, arrangements and agreements (including golden parachute, severance and employment agreements) (collectively, "*Benefit Plans*") with respect to its Senior Executive Officers (and to the extent necessary for such changes to be legally enforceable, each of its Senior Executive Officers shall have duly consented in writing to such changes), as may be necessary, during the period that the Investor owns any debt or equity securities of the Company acquired pursuant to this Agreement or the Warrant, in order to comply with Section 111(b) of the Emergency Economic Stabilization Act of 2008 ("*EESA*") as implemented by guidance or regulation thereunder that has been issued and is in effect as of the Closing Date, and (B) the Investor shall have received a certificate signed on behalf of the Company by a senior executive officer certifying to the effect that the condition set forth in Section 1.2(d)(iv)(A) has been satisfied;

(v) each of the Company's Senior Executive Officers shall have delivered to the Investor a written waiver in the form attached hereto as Annex C releasing the Investor from any claims that such Senior Executive Officers may otherwise have as a result of the issuance, on or prior to the Closing Date, of any regulations which require the modification of, and the agreement of the Company hereunder to modify, the terms of any Benefit Plans with respect to its Senior Executive Officers to eliminate any provisions of such Benefit Plans that would not be in compliance with the requirements of Section 111(b) of the EESA as implemented by guidance or regulation thereunder that has been issued and is in effect as of the Closing Date;

(vi) the Company shall have delivered to the Investor a written opinion from counsel to the Company (which may be internal counsel), addressed to the Investor and dated as of the Closing Date, in substantially the form attached hereto as Annex D;

(vii) the Company shall have delivered certificates in proper form or, with the prior consent of the Investor, evidence of shares in book-entry form, evidencing the Preferred Shares to Investor or its designee(s); and

(viii) the Company shall have duly executed the Warrant in substantially the form attached hereto as Annex E and delivered such executed Warrant to the Investor or its designee(s).

1.3 Interpretation. When a reference is made in this Agreement to “Recitals,” “Articles,” “Sections,” or “Annexes” such reference shall be to a Recital, Article or Section of, or Annex to, this Securities Purchase Agreement – Standard Terms, and a reference to “Schedules” shall be to a Schedule to the Letter Agreement, in each case, unless otherwise indicated. The terms defined in the singular have a comparable meaning when used in the plural, and vice versa. References to “herein”, “hereof”, “hereunder” and the like refer to this Agreement as a whole and not to any particular section or provision, unless the context requires otherwise. The table of contents and headings contained in this Agreement are for reference purposes only and are not part of this Agreement. Whenever the words “include,” "includes” or “including” are used in this Agreement, they shall be deemed followed by the words “without limitation.” No rule of construction against the draftsperson shall be applied in connection with the interpretation or enforcement of this Agreement, as this Agreement is the product of negotiation between sophisticated parties advised by counsel. All references to “$” or “dollars” mean the lawful currency of the United States of America. Except as expressly stated in this Agreement, all references to any statute, rule or regulation are to the statute, rule or regulation as amended, modified, supplemented or replaced from time to time (and, in the case of statutes, include any rules and regulations promulgated under the statute) and to any section of any statute, rule or regulation include any successor to the section. References to a “*business day*” shall mean any day except Saturday, Sunday and any day on which banking institutions in the State of New York generally are authorized or required by law or other governmental actions to close.

Article II
Representations and Warranties

2.1 Disclosure.

(a) On or prior to the Signing Date, the Company delivered to the Investor a schedule (“*Disclosure Schedule*”) setting forth, among other things, items the disclosure of which is necessary or appropriate either in response to an express disclosure requirement contained in a provision hereof or as an exception to one or more representations or warranties contained in Section 2.2.

(b) “*Company Material Adverse Effect*” means a material adverse effect on (i) the business, results of operation or financial condition of the Company and its consolidated subsidiaries taken as a whole; *provided*, *however*, that Company Material Adverse Effect shall not be deemed to include the effects of (A) changes after the date of the Letter Agreement (the “*Signing Date*”) in general business, economic or market conditions (including changes generally in prevailing interest rates, credit availability and liquidity, currency exchange rates and price levels or trading volumes in the United States or foreign securities or credit markets), or any outbreak or escalation of hostilities, declared or undeclared acts of war or terrorism, in each case generally affecting the industries in which the Company and its subsidiaries operate, (B) changes or proposed changes after the Signing Date in generally accepted accounting principles in the United States ("*GAAP*") or regulatory accounting requirements, or authoritative interpretations thereof, or (C) changes or proposed changes after the Signing Date in securities, banking and other laws of general applicability or related policies or interpretations of Governmental Entities (in the case of each of these clauses (A), (B) and (C), other than changes or occurrences to the extent that such changes or occurrences have or would reasonably be expected to have a materially disproportionate adverse effect on the Company and its consolidated subsidiaries taken as a whole relative to comparable U.S. banking or financial services organizations); or (ii) the ability of the Company to consummate the Purchase and other transactions contemplated by this Agreement and the Warrant and perform its obligations hereunder or thereunder on a timely basis.

(c) "*Previously Disclosed*" means information set forth on the Disclosure Schedule, provided, however, that disclosure in any section of such Disclosure Schedule shall apply only to the indicated section of this Agreement except to the extent that it is reasonably apparent from the face of such disclosure that such disclosure is relevant to another section of this Agreement.

2.2 Representations and Warranties of the Company. Except as Previously Disclosed, the Company represents and warrants to the Investor that as of the Signing Date and as of the Closing Date (or such other date specified herein):

(a) Organization, Authority and Significant Subsidiaries. The Company has been duly incorporated and is validly existing and in good standing under the laws of its jurisdiction of organization, with the necessary power and authority to own its properties and conduct its business in all material respects as currently conducted, and except as has not, individually or in the aggregate, had and would not reasonably be expected to have a Company Material Adverse Effect, has been duly qualified as a foreign corporation for the transaction of business and is in good standing under the laws of each other jurisdiction in which it owns or leases properties or conducts any business so as to require such qualification; each subsidiary of the Company that would be considered a "significant subsidiary" within the meaning of Rule 1-02(w) of Regulation S-X under the Securities Act of 1933 (the "*Securities Act*"), has been duly organized and is validly existing in good standing under the laws of its jurisdiction of organization. The Charter and bylaws of the Company, copies of which have been provided to the Investor prior to the Signing Date, are true, complete and correct copies of such documents as in full force and effect as of the Signing Date.

(b) Capitalization. The authorized capital stock of the Company, and the outstanding capital stock of the Company (including securities convertible into, or exercisable or exchangeable for, capital stock of the Company) as of the most recent fiscal month-end preceding the Signing Date (the "*Capitalization Date*") is set forth on Schedule B. The outstanding shares of capital stock of the Company have been duly authorized and are validly issued and outstanding, fully paid and nonassessable, and subject to no preemptive rights (and were not issued in violation of any preemptive rights). As of the Signing Date, the Company does not have outstanding any securities or other obligations providing the holder the right to acquire its Common Stock ("*Common Stock*") that is not reserved for issuance as specified on Schedule B, and the Company has not made any other commitment to authorize, issue or sell any Common Stock. Since the Capitalization Date, the Company has not issued any shares of Common Stock, other than (i) shares issued upon the exercise of stock options or delivered under other equity-based awards or other convertible securities or warrants which were issued and outstanding on the Capitalization Date and disclosed on Schedule B and (ii) shares disclosed on Schedule B. Each holder of 5% or more of any class of capital stock of the Company and such holder's primary address are set forth on Schedule B.

(c) Preferred Shares. The Preferred Shares have been duly and validly authorized, and, when issued and delivered pursuant to this Agreement, such Preferred Shares will be duly and validly issued and fully paid and non-assessable, will not be issued in violation of any preemptive rights, and will rank *pari passu* with or senior to all other series or classes of Preferred Stock, whether or not issued or outstanding, with respect to the payment of dividends and the distribution of assets in the event of any dissolution, liquidation or winding up of the Company.

(d) The Warrant and Warrant Shares. The Warrant has been duly authorized and, when executed and delivered as contemplated hereby, will constitute a valid and legally binding obligation of the Company enforceable against the Company in accordance with its terms, except as the same may be limited by applicable bankruptcy, insolvency, reorganization, moratorium or similar laws affecting the enforcement of creditors' rights generally and general equitable principles, regardless of whether such enforceability is considered in a proceeding at law or in equity ("*Bankruptcy Exceptions*"). The shares of Warrant Preferred Stock issuable upon exercise of the Warrant (the "*Warrant Shares*") have been duly authorized and reserved for issuance upon exercise of the Warrant and when so issued in accordance with the terms of the Warrant will be validly issued, fully paid and non-assessable, and will rank *pari passu* with or senior to all other series or classes of Preferred Stock, whether or not issued or outstanding, with respect to the payment of dividends and the distribution of assets in the event of any dissolution, liquidation or winding up of the Company.

(e) Authorization, Enforceability.

(i) The Company has the corporate power and authority to execute and deliver this Agreement and the Warrant and to carry out its obligations hereunder and thereunder (which includes the issuance of the Preferred Shares, Warrant and Warrant Shares). The execution, delivery and performance by the Company of this Agreement and the Warrant and the consummation of the transactions contemplated hereby and thereby have been duly authorized by all necessary corporate action on the part of the Company and its stockholders, and no further approval or authorization is required on the part of the Company. This Agreement is a valid and binding obligation of the Company enforceable against the Company in accordance with its terms, subject to the Bankruptcy Exceptions.

(ii) The execution, delivery and performance by the Company of this Agreement and the Warrant and the consummation of the transactions contemplated hereby and thereby and compliance by the Company with the provisions hereof and thereof, will not (A) violate, conflict with, or result in a breach of any provision of, or constitute a default (or an event which, with notice or lapse of time or both, would constitute a default) under, or result in the termination of, or accelerate the performance required by, or result in a right of termination or acceleration of, or result in the creation of, any lien, security interest, charge or encumbrance upon any of the properties or assets of the Company or any subsidiary of the Company (each a "*Company Subsidiary*" and, collectively, the "*Company Subsidiaries*") under any of the terms, conditions or provisions of (i) its organizational documents or (ii) any note, bond, mortgage, indenture, deed of trust, license, lease, agreement or other instrument or obligation to which the Company or any Company Subsidiary is a party or by which it or any Company Subsidiary may be bound, or to which the Company or any Company Subsidiary or any of the properties or assets of the Company or any Company Subsidiary may be subject, or (B) subject to compliance with the statutes and regulations referred to in the next paragraph, violate any statute, rule or regulation or any judgment, ruling, order, writ, injunction or decree applicable to the Company or any Company Subsidiary or any of their respective properties or assets except, in the case of clauses (A)(ii) and (B), for those occurrences that, individually or in the aggregate, have not had and would not reasonably be expected to have a Company Material Adverse Effect.

(iii) Other than the filing of the Certificates of Designations with the Secretary of State of its jurisdiction of organization or other applicable Governmental Entity, such filings and approvals as are required to be made or obtained under any state "blue sky" laws and such as have been made or obtained, no notice to, filing with, exemption or review by, or authorization, consent or approval of, any Governmental Entity is required to be made or obtained by the Company in connection with the consummation by the Company of the Purchase except for any such notices, filings, exemptions, reviews, authorizations, consents and approvals the failure of which to make or obtain would not, individually or in the aggregate, reasonably be expected to have a Company Material Adverse Effect.

(f) Anti-takeover Provisions and Rights Plan. The Board of Directors of the Company (the "*Board of Directors*") has taken all necessary action to ensure that the transactions contemplated by this Agreement and the Warrant and the consummation of the transactions contemplated hereby and thereby, including the exercise of the Warrant in accordance with its terms, will be exempt from any anti-takeover or similar provisions of the Company's Charter and bylaws, and any other provisions of any applicable "moratorium", "control share", "fair price", "interested stockholder" or other anti-takeover laws and regulations of any jurisdiction.

(g) No Company Material Adverse Effect. Since the last day of the last completed fiscal period for which financial statements are included in the Company Financial Statements (as defined below), no fact, circumstance, event, change, occurrence, condition or development has occurred that, individually or in the aggregate, has had or would reasonably be expected to have a Company Material Adverse Effect.

(h) Company Financial Statements. The Company has Previously Disclosed each of the consolidated financial statements of the Company and its consolidated subsidiaries for each of the last three completed fiscal years of the Company (which shall be audited to the extent audited financial statements are available prior to the Signing Date) and each completed quarterly period since the last completed fiscal year (collectively the "*Company Financial Statements*"). The Company Financial Statements present fairly in all material respects the consolidated financial position of the Company and its consolidated subsidiaries as of the dates indicated therein and the consolidated results of their operations for the periods specified therein; and except as stated therein, such financial statements (A) were prepared in conformity with GAAP applied on a consistent basis (except as may be noted therein) and (B) have been prepared from, and are in accordance with, the books and records of the Company and the Company Subsidiaries.

(i) Reports.

(i) Since December 31, 2006, the Company and each Company Subsidiary has filed all reports, registrations, documents, filings, statements and submissions, together with any amendments thereto, that it was required to file with any Governmental Entity (the foregoing, collectively, the "*Company Reports*") and has paid all fees and assessments due and payable in connection therewith, except, in each case, as would not, individually or in the aggregate, reasonably be expected to have a Company Material Adverse Effect. As of their respective dates of filing, the Company Reports complied in all material respects with all statutes and applicable rules and regulations of the applicable Governmental Entities.

(ii) The records, systems, controls, data and information of the Company and the Company Subsidiaries are recorded, stored, maintained and operated under means (including any electronic, mechanical or photographic process, whether computerized or not) that are under the exclusive ownership and direct control of the Company or the Company Subsidiaries or their accountants (including all means of access thereto and therefrom), except for any non-exclusive ownership and non-direct control that would not reasonably be expected to have a material adverse effect on the system of internal accounting controls described below in this Section 2.2(i)(ii). The Company (A) has implemented and maintains adequate disclosure controls and procedures to ensure that material information relating to the Company, including the consolidated Company Subsidiaries, is made known to the chief executive officer and the chief financial officer of the Company by others within those entities, and (B) has disclosed, based on its most recent evaluation prior to the Signing Date, to the Company's outside auditors and the audit committee of the Board of Directors (x) any significant deficiencies and material weaknesses in the design or operation of internal controls that are reasonably likely to adversely affect the Company's ability to record, process, summarize and report financial information and (y) any fraud, whether or not material, that involves management or other employees who have a significant role in the Company's internal controls over financial reporting.

(j) No Undisclosed Liabilities. Neither the Company nor any of the Company Subsidiaries has any liabilities or obligations of any nature (absolute, accrued, contingent or otherwise) which are not properly reflected or reserved against in the Company Financial Statements to the extent required to be so reflected or reserved against in accordance with GAAP, except for (A) liabilities that have arisen since the last fiscal year end in the ordinary and usual course of business and consistent with past practice and (B) liabilities that, individually or in the aggregate, have not had and would not reasonably be expected to have a Company Material Adverse Effect.

(k) Offering of Securities. Neither the Company nor any person acting on its behalf has taken any action (including any offering of any securities of the Company under circumstances which would require the integration of such offering with the offering of any of the Purchased Securities under the Securities Act, and the rules and regulations of the Securities and Exchange Commission (the "*SEC*") promulgated thereunder), which might subject the offering, issuance or sale of any of the Purchased Securities to Investor pursuant to this Agreement to the registration requirements of the Securities Act.

(l) Litigation and Other Proceedings. Except (i) as set forth on Schedule C or (ii) as would not, individually or in the aggregate, reasonably be expected to have a Company Material Adverse Effect, there is no (A) pending or, to the knowledge of the Company, threatened, claim, action, suit, investigation or proceeding, against the Company or any Company Subsidiary or to which any of their assets are subject nor is the Company or any Company Subsidiary subject to any order, judgment or decree or (B) unresolved violation, criticism or exception by any Governmental Entity with respect to any report or relating to any examinations or inspections of the Company or any Company Subsidiaries.

(m) Compliance with Laws. Except as would not, individually or in the aggregate, reasonably be expected to have a Company Material Adverse Effect, the Company and the Company Subsidiaries have all permits, licenses, franchises, authorizations, orders and approvals of, and have made all filings, applications and registrations with, Governmental Entities that are required in order to permit them to own or lease their properties and assets and to carry on their business as presently conducted and that are material to the business of the Company or such Company Subsidiary. Except as set forth on Schedule D, the Company and the Company Subsidiaries have complied in all respects and are not in default or violation of, and none of them is, to the knowledge of the Company, under investigation with respect to or, to the knowledge of the Company, have been threatened to be charged with or given notice of any violation of, any applicable domestic (federal, state or local) or foreign law, statute, ordinance, license, rule, regulation, policy or guideline, order, demand, writ, injunction, decree or judgment of any Governmental Entity, other than such noncompliance, defaults or violations that would not, individually or in the aggregate, reasonably be expected to have a Company Material Adverse Effect. Except for statutory or regulatory restrictions of general application or as set forth on Schedule D, no Governmental Entity has placed any restriction on the business or properties of the Company or any Company Subsidiary that would, individually or in the aggregate, reasonably be expected to have a Company Material Adverse Effect.

(n) Employee Benefit Matters. Except as would not reasonably be expected to have, either individually or in the aggregate, a Company Material Adverse Effect: (A) each "employee benefit plan" (within the meaning of Section 3(3) of the Employee Retirement Income Security Act of 1974, as amended ("*ERISA*")) providing benefits to any current or former employee, officer or director of the Company or any member of its "*Controlled Group*" (defined as any organization which is a member of a controlled group of corporations within the meaning of Section 414 of the Internal Revenue Code of 1986, as amended (the "*Code*")) that is sponsored, maintained or contributed to by the Company or any member of its Controlled Group and for which the Company or any member of its Controlled Group would have any liability, whether actual or contingent (each, a "*Plan*") has been maintained in compliance with its terms and with the requirements of all applicable statutes, rules and regulations, including ERISA and the Code; (B) with respect to each Plan subject to Title IV of ERISA (including, for purposes of this clause (B), any plan subject to Title IV of ERISA that the Company or any member of its Controlled Group previously maintained or contributed to in the six years prior to the Signing Date), (1) no "reportable event" (within the meaning of Section 4043(c) of ERISA), other than a reportable event for which the notice period referred to in Section 4043(c) of ERISA has been waived, has occurred in the three years prior to the Signing Date or is reasonably expected to occur, (2) no "accumulated funding deficiency" (within the meaning of Section 302 of ERISA or Section 412 of the Code), whether or not waived, has occurred in the three years prior to the Signing Date or is reasonably expected to occur, (3) the fair market value of the assets under each Plan exceeds the present value of all benefits accrued under such Plan (determined based on the assumptions used to fund such Plan) and (4) neither the Company nor any member of its Controlled Group has incurred in the six years prior to the Signing Date, or reasonably expects to incur, any liability under Title IV of ERISA (other than contributions to the Plan or premiums to the PBGC in the ordinary course and without default) in respect of a Plan (including any Plan that is a "multiemployer plan", within the meaning of Section 4001(c)(3) of ERISA); and (C) each Plan that is intended to be qualified under Section 401(a) of the Code has received a favorable determination letter from the Internal Revenue Service with respect to its qualified status that has not been revoked, or such a determination letter has been timely applied for but not received by the Signing Date, and nothing has occurred, whether by action or by failure to act, which could reasonably be expected to cause the loss, revocation or denial of such qualified status or favorable determination letter.

(o) Taxes. Except as would not, individually or in the aggregate, reasonably be expected to have a Company Material Adverse Effect, (i) the Company and the Company Subsidiaries have filed all federal, state, local and foreign income and franchise Tax returns required to be filed through the Signing Date, subject to permitted extensions, and have paid all Taxes due thereon, and (ii) no Tax deficiency has been determined adversely to the Company or any of the Company Subsidiaries, nor does the Company have any knowledge of any Tax deficiencies. "*Tax*" or "*Taxes*" means any federal, state, local or foreign income, gross receipts, property, sales, use, license, excise, franchise, employment, payroll, withholding, alternative or add on minimum, ad valorem, transfer or excise tax, or any other tax, custom, duty, governmental fee or other like assessment or charge of any kind whatsoever, together with any interest or penalty, imposed by any Governmental Entity.

(p) Properties and Leases. Except as would not, individually or in the aggregate, reasonably be expected to have a Company Material Adverse Effect, the Company and the Company Subsidiaries have good and marketable title to all real properties and all other properties and assets owned by them, in each case free from liens, encumbrances, claims and defects that would affect the value thereof or interfere with the use made or to be made thereof by them. Except as would not, individually or in the aggregate, reasonably be expected to have a Company Material Adverse Effect, the Company and the Company Subsidiaries hold all leased real or personal property under valid and enforceable leases with no exceptions that would interfere with the use made or to be made thereof by them.

(q) Environmental Liability. Except as would not, individually or in the aggregate, reasonably be expected to have a Company Material Adverse Effect:

(i) there is no legal, administrative, or other proceeding, claim or action of any nature seeking to impose, or that would reasonably be expected to result in the imposition of, on the Company or any Company Subsidiary, any liability relating to the release of hazardous substances as defined under any local, state or federal environmental statute, regulation or ordinance, including the Comprehensive Environmental Response, Compensation and Liability Act of 1980, pending or, to the Company's knowledge, threatened against the Company or any Company Subsidiary;

(ii) to the Company's knowledge, there is no reasonable basis for any such proceeding, claim or action; and

(iii) neither the Company nor any Company Subsidiary is subject to any agreement, order, judgment or decree by or with any court, Governmental Entity or third party imposing any such environmental liability.

(r) Risk Management Instruments. Except as would not, individually or in the aggregate, reasonably be expected to have a Company Material Adverse Effect, all derivative instruments, including, swaps, caps, floors and option agreements, whether entered into for the Company's own account, or for the account of one or more of the Company Subsidiaries or its or their customers, were entered into (i) only in the ordinary course of business, (ii) in accordance with prudent practices and in all material respects with all applicable laws, rules, regulations and regulatory policies and (iii) with counterparties believed to be financially responsible at the time; and each of such instruments constitutes the valid and legally binding obligation of the Company or one of the Company Subsidiaries, enforceable in accordance with its terms, except as may be limited by the Bankruptcy Exceptions. Neither the Company or the Company Subsidiaries, nor, to the knowledge of the Company, any other party thereto, is in breach of any of its obligations under any such agreement or arrangement other than such breaches that would not, individually or in the aggregate, reasonably be expected to have a Company Material Adverse Effect.

(s) Agreements with Regulatory Agencies. Except as set forth on Schedule E, neither the Company nor any Company Subsidiary is subject to any material cease-and-desist or other similar order or enforcement action issued by, or is a party to any material written agreement, consent agreement or memorandum of understanding with, or is a party to any commitment letter or similar undertaking to, or is subject to any capital directive by, or since December 31, 2006, has adopted any board resolutions at the request of, any Governmental Entity (other than the Appropriate Federal Banking Agencies with jurisdiction over the Company and the Company Subsidiaries) that currently restricts in any material respect the conduct of its business or that in any material manner relates to its capital adequacy, its liquidity and funding policies and practices, its ability to pay dividends, its credit, risk management or compliance policies or procedures, its internal controls, its management or its operations or business (each item in this sentence, a "*Regulatory Agreement*"), nor has the Company or any Company Subsidiary been advised since December 31, 2006 by any such Governmental Entity that it is considering issuing, initiating, ordering, or requesting any such Regulatory Agreement. The Company and each Company Subsidiary are in compliance in all material respects with each Regulatory Agreement to which it is party or subject, and neither the Company nor any Company Subsidiary has received any notice from any Governmental Entity indicating that either the Company or any Company Subsidiary is not in compliance in all material respects with any such Regulatory Agreement. "*Appropriate Federal Banking Agency*" means the "appropriate Federal banking agency" with respect to the Company or such Company Subsidiaries, as applicable, as defined in Section 3(q) of the Federal Deposit Insurance Act (12 U.S.C. Section 1813(q)).

(t) Insurance. The Company and the Company Subsidiaries are insured with reputable insurers against such risks and in such amounts as the management of the Company reasonably has determined to be prudent and consistent with industry practice. The Company and the Company Subsidiaries are in material compliance with their insurance policies and are not in default under any of the material terms thereof, each such policy is outstanding and in full force and effect, all premiums and other payments due under any material policy have been paid, and all claims thereunder have been filed in due and timely fashion, except, in each case, as would not, individually or in the aggregate, reasonably be expected to have a Company Material Adverse Effect.

(u) Intellectual Property. Except as would not, individually or in the aggregate, reasonably be expected to have a Company Material Adverse Effect, (i) the Company and each Company Subsidiary owns or otherwise has the right to use, all intellectual property rights, including all trademarks, trade dress, trade names, service marks, domain names, patents, inventions, trade secrets, know-how, works of authorship and copyrights therein, that are used in the conduct of their existing businesses and all rights relating to the plans, design and specifications of any of its branch facilities ("*Proprietary Rights*") free and clear of all liens and any claims of ownership by current or former employees, contractors, designers or others and (ii) neither the Company nor any of the Company Subsidiaries is materially infringing, diluting, misappropriating or violating, nor has the Company or any or the Company Subsidiaries received any written (or, to the knowledge of the Company, oral) communications alleging that any of them has materially infringed, diluted, misappropriated or violated, any of the Proprietary Rights owned by any other person. Except as would not, individually or in the aggregate, reasonably be expected to have a Company Material Adverse Effect, to the Company's knowledge, no other person is infringing, diluting, misappropriating or violating, nor has the Company or any or the Company Subsidiaries sent any written communications since January 1, 2006 alleging that any person has infringed, diluted, misappropriated or violated, any of the Proprietary Rights owned by the Company and the Company Subsidiaries.

(v) Brokers and Finders. No broker, finder or investment banker is entitled to any financial advisory, brokerage, finder's or other fee or commission in connection with this Agreement or the Warrant or the transactions contemplated hereby or thereby based upon arrangements made by or on behalf of the Company or any Company Subsidiary for which the Investor could have any liability.

Article III
Covenants

3.1 Commercially Reasonable Efforts. Subject to the terms and conditions of this Agreement, each of the parties will use its commercially reasonable efforts in good faith to take, or cause to be taken, all actions, and to do, or cause to be done, all things necessary, proper or desirable, or advisable under applicable laws, so as to permit consummation of the Purchase as promptly as practicable and otherwise to enable consummation of the transactions contemplated hereby and shall use commercially reasonable efforts to cooperate with the other party to that end.

3.2 Expenses. Unless otherwise provided in this Agreement or the Warrant, each of the parties hereto will bear and pay all costs and expenses incurred by it or on its behalf in connection with the transactions contemplated under this Agreement and the Warrant, including fees and expenses of its own financial or other consultants, investment bankers, accountants and counsel.

3.3 Sufficiency of Authorized Warrant Preferred Stock; Exchange Listing.

(a) During the period from the Closing Date until the date on which the Warrant has been fully exercised, the Company shall at all times have reserved for issuance, free of preemptive or similar rights, a sufficient number of authorized and unissued Warrant Shares to effectuate such exercise.

(b) If the Company lists its Common Stock on any national securities exchange, the Company shall, if requested by the Investor, promptly use its reasonable best efforts to cause the Preferred Shares and Warrant Shares to be approved for listing on a national securities exchange as promptly as practicable following such request.

3.4 Certain Notifications Until Closing. From the Signing Date until the Closing, the Company shall promptly notify the Investor of (i) any fact, event or circumstance of which it is aware and which would reasonably be expected to cause any representation or warranty of the Company contained in this Agreement to be untrue or inaccurate in any material respect or to cause any covenant or agreement of the Company contained in this Agreement not to be complied with or satisfied in any material respect and (ii) except as Previously Disclosed, any fact, circumstance, event, change, occurrence, condition or development of which the Company is aware and which, individually or in the aggregate, has had or would reasonably be expected to have a Company Material Adverse Effect; *provided*, *however*, that delivery of any notice pursuant to this Section 3.4 shall not limit or affect any rights of or remedies available to the Investor; *provided*, *further*, that a failure to comply with this Section 3.4 shall not constitute a breach of this Agreement or the failure of any condition set forth in Section 1.2 to be satisfied unless the underlying Company Material Adverse Effect or material breach would independently result in the failure of a condition set forth in Section 1.2 to be satisfied.

3.5 Access, Information and Confidentiality.

(a) From the Signing Date until the date when the Investor holds an amount of Preferred Shares having an aggregate liquidation value of less than 10% of the Purchase Price, the Company will permit the Investor and its agents, consultants, contractors and advisors (x) acting through the Appropriate Federal Banking Agency, or otherwise to the extent necessary to evaluate, manage, or transfer its investment in the Company, to examine the corporate books and make copies thereof and to discuss the affairs, finances and accounts of the Company and the Company Subsidiaries with the principal officers of the Company, all upon reasonable notice and at such reasonable times and as often as the Investor may reasonably request and (y) to review any information material to the Investor's investment in the Company provided by the Company to its Appropriate Federal Banking Agency. Any investigation pursuant to this Section 3.5 shall be conducted during normal business hours and in such manner as not to interfere unreasonably with the conduct of the business of the Company, and nothing herein shall require the Company or any Company Subsidiary to disclose any information to the Investor to the extent (i) prohibited by applicable law or regulation, or (ii) that such disclosure would reasonably be expected to cause a violation of any agreement to which the Company or any Company Subsidiary is a party or would cause a risk of a loss of privilege to the Company or any Company Subsidiary (*provided* that the Company shall use commercially reasonable efforts to make appropriate substitute disclosure arrangements under circumstances where the restrictions in this clause (ii) apply).

(b) From the Signing Date until the date on which all of the Preferred Shares and Warrant Shares have been redeemed in whole, the Company will deliver, or will cause to be delivered, to the Investor:

(i) as soon as available after the end of each fiscal year of the Company, and in any event within 90 days thereafter, a consolidated balance sheet of the Company as of the end of such fiscal year, and consolidated statements of income, retained earnings and cash flows of the Company for such year, in each case prepared in accordance with GAAP and setting forth in each case in comparative form the figures for the previous fiscal year of the Company, and which shall be audited to the extent audited financial statements are available; and

(ii) as soon as available after the end of the first, second and third quarterly periods in each fiscal year of the Company, a copy of any quarterly reports provided to other stockholders of the Company or Company management.

(c) The Investor will use reasonable best efforts to hold, and will use reasonable best efforts to cause its agents, consultants, contractors and advisors to hold, in confidence all non-public records, books, contracts, instruments, computer data and other data and information (collectively, "*Information*") concerning the Company furnished or made available to it by the Company or its representatives pursuant to this Agreement (except to the extent that such information can be shown to have been (i) previously known by such party on a non-confidential basis, (ii) in the public domain through no fault of such party or (iii) later lawfully acquired from other sources by the party to which it was furnished (and without violation of any other confidentiality obligation)); *provided* that nothing herein shall prevent the Investor from disclosing any Information to the extent required by applicable laws or regulations or by any subpoena or similar legal process.

(d) The Investor's information rights pursuant to Section 3.5(b) may be assigned by the Investor to a transferee or assignee of the Purchased Securities or the Warrant Shares or with a liquidation preference or, in the case of the Warrant, the liquidation preference of the underlying shares of Warrant Preferred Stock, no less than an amount equal to 2% of the initial aggregate liquidation preference of the Preferred Shares.

Article IV
Additional Agreements

4.1 Purchase for Investment. The Investor acknowledges that the Purchased Securities and the Warrant Shares have not been registered under the Securities Act or under any state securities laws. The Investor (a) is acquiring the Purchased Securities pursuant to an exemption from registration under the Securities Act solely for investment with no present intention to distribute them to any person in violation of the Securities Act or any applicable U.S. state securities laws, (b) will not sell or otherwise dispose of any of the Purchased Securities or the Warrant Shares, except in compliance with the registration requirements or exemption provisions of the Securities Act and any applicable U.S. state securities laws, and (c) has such knowledge and experience in financial and business matters and in investments of this type that it is capable of evaluating the merits and risks of the Purchase and of making an informed investment decision.

4.2 Legends.

(a) The Investor agrees that all certificates or other instruments representing the Warrant will bear a legend substantially to the following effect:

> "THE SECURITIES REPRESENTED BY THIS INSTRUMENT HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, OR THE SECURITIES LAWS OF ANY STATE AND MAY NOT BE TRANSFERRED, SOLD

OR OTHERWISE DISPOSED OF EXCEPT WHILE A REGISTRATION STATEMENT RELATING THERETO IS IN EFFECT UNDER SUCH ACT AND APPLICABLE STATE SECURITIES LAWS OR PURSUANT TO AN EXEMPTION FROM REGISTRATION UNDER SUCH ACT OR SUCH LAWS.

THIS INSTRUMENT IS ISSUED SUBJECT TO THE RESTRICTIONS ON TRANSFER AND OTHER PROVISIONS OF A SECURITIES PURCHASE AGREEMENT BETWEEN THE ISSUER OF THESE SECURITIES AND THE INVESTOR REFERRED TO THEREIN, A COPY OF WHICH IS ON FILE WITH THE ISSUER. THE SECURITIES REPRESENTED BY THIS INSTRUMENT MAY NOT BE SOLD OR OTHERWISE TRANSFERRED EXCEPT IN COMPLIANCE WITH SAID AGREEMENT. ANY SALE OR OTHER TRANSFER NOT IN COMPLIANCE WITH SAID AGREEMENT WILL BE VOID."

(b) In addition, the Investor agrees that all certificates or other instruments representing the Preferred Shares and the Warrant Shares will bear a legend substantially to the following effect:

"THE SECURITIES REPRESENTED BY THIS INSTRUMENT ARE NOT SAVINGS ACCOUNTS, DEPOSITS OR OTHER OBLIGATIONS OF A BANK AND ARE NOT INSURED BY THE FEDERAL DEPOSIT INSURANCE CORPORATION OR ANY OTHER GOVERNMENTAL AGENCY.

THE SECURITIES REPRESENTED BY THIS INSTRUMENT HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE "SECURITIES ACT"), OR THE SECURITIES LAWS OF ANY STATE AND MAY NOT BE TRANSFERRED, SOLD OR OTHERWISE DISPOSED OF EXCEPT WHILE A REGISTRATION STATEMENT RELATING THERETO IS IN EFFECT UNDER SUCH ACT AND APPLICABLE STATE SECURITIES LAWS OR PURSUANT TO AN EXEMPTION FROM REGISTRATION UNDER SUCH ACT OR SUCH LAWS. EACH PURCHASER OF THE SECURITIES REPRESENTED BY THIS INSTRUMENT IS NOTIFIED THAT THE SELLER MAY BE RELYING ON THE EXEMPTION FROM SECTION 5 OF THE SECURITIES ACT PROVIDED BY RULE 144A THEREUNDER. ANY TRANSFEREE OF THE SECURITIES REPRESENTED BY THIS INSTRUMENT BY ITS ACCEPTANCE HEREOF (1) REPRESENTS THAT IT IS A "QUALIFIED INSTITUTIONAL BUYER" (AS DEFINED IN RULE 144A UNDER THE SECURITIES ACT), (2) AGREES THAT IT WILL NOT OFFER, SELL OR OTHERWISE TRANSFER THE SECURITIES REPRESENTED BY THIS INSTRUMENT EXCEPT (A) PURSUANT TO A REGISTRATION STATEMENT WHICH IS THEN EFFECTIVE UNDER THE SECURITIES ACT, (B) FOR SO LONG AS THE SECURITIES REPRESENTED BY THIS INSTRUMENT ARE ELIGIBLE FOR RESALE PURSUANT TO RULE 144A, TO A PERSON IT REASONABLY BELIEVES IS A "QUALIFIED INSTITUTIONAL BUYER" AS DEFINED IN RULE 144A UNDER THE SECURITIES ACT THAT PURCHASES FOR ITS OWN ACCOUNT OR FOR THE ACCOUNT OF A QUALIFIED INSTITUTIONAL BUYER

TO WHOM NOTICE IS GIVEN THAT THE TRANSFER IS BEING MADE IN RELIANCE ON RULE 144A, (C) TO THE ISSUER OR (D) PURSUANT TO ANY OTHER AVAILABLE EXEMPTION FROM THE REGISTRATION REQUIREMENTS OF THE SECURITIES ACT AND (3) AGREES THAT IT WILL GIVE TO EACH PERSON TO WHOM THE SECURITIES REPRESENTED BY THIS INSTRUMENT ARE TRANSFERRED A NOTICE SUBSTANTIALLY TO THE EFFECT OF THIS LEGEND.

THIS INSTRUMENT IS ISSUED SUBJECT TO THE RESTRICTIONS ON TRANSFER AND OTHER PROVISIONS OF A SECURITIES PURCHASE AGREEMENT BETWEEN THE ISSUER OF THESE SECURITIES AND THE INVESTOR REFERRED TO THEREIN, A COPY OF WHICH IS ON FILE WITH THE ISSUER. THE SECURITIES REPRESENTED BY THIS INSTRUMENT MAY NOT BE SOLD OR OTHERWISE TRANSFERRED EXCEPT IN COMPLIANCE WITH SAID AGREEMENT. ANY SALE OR OTHER TRANSFER NOT IN COMPLIANCE WITH SAID AGREEMENT WILL BE VOID."

(c) In the event that any Purchased Securities or Warrant Shares (i) become registered under the Securities Act or (ii) are eligible to be transferred without restriction in accordance with Rule 144 or another exemption from registration under the Securities Act (other than Rule 144A), the Company shall issue new certificates or other instruments representing such Purchased Securities or Warrant Shares, which shall not contain the applicable legends in Sections 4.2(a) and (b) above; *provided* that the Investor surrenders to the Company the previously issued certificates or other instruments.

4.3 Certain Transactions. The Company will not merge or consolidate with, or sell, transfer or lease all or substantially all of its property or assets to, any other party unless the successor, transferee or lessee party (or its ultimate parent entity), as the case may be (if not the Company), expressly assumes the due and punctual performance and observance of each and every covenant, agreement and condition of this Agreement to be performed and observed by the Company.

4.4 Transfer of Purchased Securities and Warrant Shares; Restrictions on Exercise of the Warrant. Subject to compliance with applicable securities laws, the Investor shall be permitted to transfer, sell, assign or otherwise dispose of ("*Transfer*") all or a portion of the Purchased Securities or Warrant Shares at any time, and the Company shall take all steps as may be reasonably requested by the Investor to facilitate the Transfer of the Purchased Securities and the Warrant Shares; *provided* that the Investor shall not Transfer any Purchased Securities or Warrant Shares if such transfer would require the Company to be subject to the periodic reporting requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934 (the "*Exchange Act*"). In furtherance of the foregoing, the Company shall provide reasonable cooperation to facilitate any Transfers of the Purchased Securities or Warrant Shares, including, as is reasonable under the circumstances, by furnishing such information concerning the Company and its business as a proposed transferee may reasonably request (including such information as is required by Section 4.5(k)) and making management of the Company reasonably available to respond to questions of a proposed transferee in accordance with customary practice, subject in all cases to the proposed transferee agreeing to a customary confidentiality agreement.

4.5 Registration Rights.

(a) Unless and until the Company becomes subject to the reporting requirements of Section 13 or 15(d) of the Exchange Act, the Company shall have no obligation to comply with the provisions of this Section 4.5 (other than Section 4.5(b)(iv)-(vi)); *provided* that the Company covenants and agrees that it shall comply with this Section 4.5 as soon as practicable after the date that it becomes subject to such reporting requirements.

(b) Registration.

(i) Subject to the terms and conditions of this Agreement, the Company covenants and agrees that as promptly as practicable after the date that the Company becomes subject to the reporting requirements of Section 13 or 15(d) of the Exchange Act (and in any event no later than 30 days thereafter), the Company shall prepare and file with the SEC a Shelf Registration Statement covering all Registrable Securities (or otherwise designate an existing Shelf Registration Statement filed with the SEC to cover the Registrable Securities), and, to the extent the Shelf Registration Statement has not theretofore been declared effective or is not automatically effective upon such filing, the Company shall use reasonable best efforts to cause such Shelf Registration Statement to be declared or become effective and to keep such Shelf Registration Statement continuously effective and in compliance with the Securities Act and usable for resale of such Registrable Securities for a period from the date of its initial effectiveness until such time as there are no Registrable Securities remaining (including by refiling such Shelf Registration Statement (or a new Shelf Registration Statement) if the initial Shelf Registration Statement expires). Notwithstanding the foregoing, if the Company is not eligible to file a registration statement on Form S-3, then the Company shall not be obligated to file a Shelf Registration Statement unless and until requested to do so in writing by the Investor.

(ii) Any registration pursuant to Section 4.5(b)(i) shall be effected by means of a shelf registration on an appropriate form under Rule 415 under the Securities Act (a "*Shelf Registration Statement*"). If the Investor or any other Holder intends to distribute any Registrable Securities by means of an underwritten offering it shall promptly so advise the Company and the Company shall take all reasonable steps to facilitate such distribution, including the actions required pursuant to Section 4.5(d); *provided* that the Company shall not be required to facilitate an underwritten offering of Registrable Securities unless the expected gross proceeds from such offering exceed (i) 2% of the initial aggregate liquidation preference of the Preferred Shares if such initial aggregate liquidation preference is less than $2 billion and (ii) $200 million if the initial aggregate liquidation preference of the Preferred Shares is equal to or greater than $2 billion. The lead underwriters in any such distribution shall be selected by the Holders of a majority of the Registrable Securities to be distributed; *provided* that to the extent appropriate and permitted under applicable law, such Holders shall consider the qualifications of any broker-dealer Affiliate of the Company in selecting the lead underwriters in any such distribution.

(iii) The Company shall not be required to effect a registration (including a resale of Registrable Securities from an effective Shelf Registration Statement) or an underwritten offering pursuant to Section 4.5(b): (A) with respect to securities that are not Registrable Securities; or (B) if the Company has notified the Investor and all other Holders that in the good faith judgment of the Board of Directors, it would be materially detrimental to the Company or its securityholders for such registration or underwritten offering to be effected at such time, in which event the Company shall have the right to defer such registration for a period of not more than 45 days after receipt of the request of the Investor or any other Holder; *provided* that such right to delay a registration or underwritten offering shall be exercised by the Company (1) only if the Company has generally exercised (or is concurrently exercising) similar black-out rights against holders of similar securities that have registration rights and (2) not more than three times in any 12-month period and not more than 90 days in the aggregate in any 12-month period.

(iv) If during any period when an effective Shelf Registration Statement is not available, the Company proposes to register any of its equity securities, other than a registration pursuant to Section 4.5(b)(i) or a Special Registration, and the registration form to be filed may be used for the registration or qualification for distribution of Registrable Securities, the Company will give prompt written notice to the Investor and all other Holders of its intention to effect such a registration (but in no event less than ten days prior to the anticipated filing date) and will include in such registration all Registrable Securities with respect to which the Company has received written requests for inclusion therein within ten business days after the date of the Company's notice (a "*Piggyback Registration*"). Any such person that has made such a written request may withdraw its Registrable Securities from such Piggyback Registration by giving written notice to the Company and the managing underwriter, if any, on or before the fifth business day prior to the planned effective date of such Piggyback Registration. The Company may terminate or withdraw any registration under this Section 4.5(b)(iv) prior to the effectiveness of such registration, whether or not Investor or any other Holders have elected to include Registrable Securities in such registration.

(v) If the registration referred to in Section 4.5(b)(iv) is proposed to be underwritten, the Company will so advise Investor and all other Holders as a part of the written notice given pursuant to Section 4.5(b)(iv). In such event, the right of Investor and all other Holders to registration pursuant to Section 4.5(b) will be conditioned upon such persons' participation in such underwriting and the inclusion of such person's Registrable Securities in the underwriting if such securities are of the same class of securities as the securities to be offered in the underwritten offering, and each such person will (together with the Company and the other persons distributing their securities through such underwriting) enter into an underwriting agreement in customary form with the underwriter or underwriters selected for such underwriting by the Company; *provided* that the Investor (as opposed to other Holders) shall not be required to indemnify any person in connection with any registration. If any participating person disapproves of the terms of the underwriting, such person may elect to withdraw therefrom by written notice to the Company, the managing underwriters and the Investor (if the Investor is participating in the underwriting).

(vi) If either (x) the Company grants "piggyback" registration rights to one or more third parties to include their securities in an underwritten offering under the Shelf Registration Statement pursuant to Section 4.5(b)(ii) or (y) a Piggyback Registration under Section 4.5(b)(iv) relates to an underwritten offering on behalf of the Company, and in either case the managing underwriters advise the Company that in their reasonable opinion the number of securities requested to be included in such offering exceeds the number which can be sold without adversely affecting the marketability of such offering (including an adverse effect on the per share offering price), the Company will include in such offering only such number of securities that in the reasonable opinion of such managing underwriters can be sold without adversely affecting the marketability of the offering (including an adverse effect on the per share offering price), which securities will be so included in the following order of priority: (A) first, in the case of a Piggyback Registration under Section 4.5(b)(iv), the securities the Company proposes to sell, (B) then the Registrable Securities of the Investor and all other Holders who have requested inclusion of Registrable Securities pursuant to Section 4.5(b)(ii) or Section 4.5(b)(iv), as applicable, *pro rata* on the basis of the aggregate number of such securities or shares owned by each such person and (C) lastly, any other securities of the Company that have been requested to be so included, subject to the terms of this Agreement; *provided, however,* that if the Company has, prior to the Signing Date, entered into an agreement with respect to its securities that is inconsistent with the order of priority contemplated hereby then it shall apply the order of priority in such conflicting agreement to the extent that it would otherwise result in a breach under such agreement.

(c) <u>Expenses of Registration</u>. All Registration Expenses incurred in connection with any registration, qualification or compliance hereunder shall be borne by the Company. All Selling Expenses incurred in connection with any registrations hereunder shall be borne by the holders of the securities so registered *pro rata* on the basis of the aggregate offering or sale price of the securities so registered.

(d) <u>Obligations of the Company</u>. Whenever required to effect the registration of any Registrable Securities or facilitate the distribution of Registrable Securities pursuant to an effective Shelf Registration Statement, the Company shall, as expeditiously as reasonably practicable:

(i) Prepare and file with the SEC a prospectus supplement or post-effective amendment with respect to a proposed offering of Registrable Securities pursuant to an effective registration statement, subject to Section 4.5(d), keep such registration statement effective and keep such prospectus supplement current until the securities described therein are no longer Registrable Securities.

(ii) Prepare and file with the SEC such amendments and supplements to the applicable registration statement and the prospectus or prospectus supplement used in connection with such registration statement as may be necessary to comply with the provisions of the Securities Act with respect to the disposition of all securities covered by such registration statement.

(iii) Furnish to the Holders and any underwriters such number of copies of the applicable registration statement and each such amendment and supplement thereto (including in each case all exhibits) and of a prospectus, including a preliminary prospectus, in conformity with the requirements of the Securities Act, and such other documents as they may reasonably request in order to facilitate the disposition of Registrable Securities owned or to be distributed by them.

(iv) Use its reasonable best efforts to register and qualify the securities covered by such registration statement under such other securities or Blue Sky laws of such jurisdictions as shall be reasonably requested by the Holders or any managing underwriter(s), to keep such registration or qualification in effect for so long as such registration statement remains in effect, and to take any other action which may be reasonably necessary to enable such seller to consummate the disposition in such jurisdictions of the securities owned by such Holder; *provided* that the Company shall not be required in connection therewith or as a condition thereto to qualify to do business or to file a general consent to service of process in any such states or jurisdictions.

(v) Notify each Holder of Registrable Securities at any time when a prospectus relating thereto is required to be delivered under the Securities Act of the happening of any event as a result of which the applicable prospectus, as then in effect, includes an untrue statement of a material fact or omits to state a material fact required to be stated therein or necessary to make the statements therein not misleading in light of the circumstances then existing.

(vi) Give written notice to the Holders:

(A) when any registration statement filed pursuant to Section 4.5(a) or any amendment thereto has been filed with the SEC (except for any amendment effected by the filing of a document with the SEC pursuant to the Exchange Act) and when such registration statement or any post-effective amendment thereto has become effective;

(B) of any request by the SEC for amendments or supplements to any registration statement or the prospectus included therein or for additional information;

(C) of the issuance by the SEC of any stop order suspending the effectiveness of any registration statement or the initiation of any proceedings for that purpose;

(D) of the receipt by the Company or its legal counsel of any notification with respect to the suspension of the qualification of the applicable Registrable Securities for sale in any jurisdiction or the initiation or threatening of any proceeding for such purpose;

(E) of the happening of any event that requires the Company to make changes in any effective registration statement or the prospectus related to the registration statement in order to make the statements therein not misleading (which notice shall be accompanied by an instruction to suspend the use of the prospectus until the requisite changes have been made); and

(F) if at any time the representations and warranties of the Company contained in any underwriting agreement contemplated by Section 4.5(d)(x) cease to be true and correct.

(vii) Use its reasonable best efforts to prevent the issuance or obtain the withdrawal of any order suspending the effectiveness of any registration statement referred to in Section 4.5(d)(vi)(C) at the earliest practicable time.

(viii) Upon the occurrence of any event contemplated by Section 4.5(d)(v) or 4.5(d)(vi)(E), promptly prepare a post-effective amendment to such registration statement or a supplement to the related prospectus or file any other required document so that, as thereafter delivered to the Holders and any underwriters, the prospectus will not contain an untrue statement of a material fact or omit to state any material fact necessary to make the statements therein, in light of the circumstances under which they were made, not misleading. If the Company notifies the Holders in accordance with Section 4.5(d)(vi)(E) to suspend the use of the prospectus until the requisite changes to the prospectus have been made, then the Holders and any underwriters shall suspend use of such prospectus and use their reasonable best efforts to return to the Company all copies of such prospectus (at the Company's expense) other than permanent file copies then in such Holders' or underwriters' possession. The total number of days that any such suspension may be in effect in any 12-month period shall not exceed 90 days.

(ix) Use reasonable best efforts to procure the cooperation of the Company's transfer agent in settling any offering or sale of Registrable Securities, including with respect to the transfer of physical stock certificates into book-entry form in accordance with any procedures reasonably requested by the Holders or any managing underwriter(s).

(x) If an underwritten offering is requested pursuant to Section 4.5(b)(ii), enter into an underwriting agreement in customary form, scope and substance and take all such other actions reasonably requested by the Holders of a majority of the Registrable Securities being sold in connection therewith or by the managing underwriter(s), if any, to expedite or facilitate the underwritten disposition of such Registrable Securities, and in connection therewith in any underwritten offering (including making members of management and executives of the Company available to participate in "road shows", similar sales events and other marketing activities), (A) make such representations and warranties to the Holders that are selling stockholders and the managing underwriter(s), if any, with respect to the business of the Company and its subsidiaries, and the Shelf Registration Statement, prospectus and documents, if any, incorporated or deemed to be incorporated by reference therein, in each case, in customary form, substance and scope, and, if true, confirm the same if and when requested, (B) use its reasonable best efforts to furnish the underwriters with opinions of counsel to the Company, addressed to the managing underwriter(s), if any, covering the matters customarily covered in such opinions requested in underwritten offerings, (C) use its reasonable best efforts to obtain "cold comfort" letters from the independent certified public accountants of the Company (and, if necessary, any other independent certified public accountants of any business acquired by the Company for which financial statements and financial data are included in the Shelf Registration Statement) who have certified the financial statements included in such Shelf Registration Statement, addressed to each of the managing underwriter(s), if any, such letters to be in customary form and covering matters of the type customarily covered in "cold comfort" letters, (D) if an underwriting agreement is entered into, the same shall contain indemnification provisions and procedures customary in underwritten offerings (provided that the Investor shall not be obligated to provide any indemnity), and (E) deliver such documents and certificates as may be reasonably requested by the Holders of a majority of the Registrable Securities being sold in connection therewith, their counsel and the managing underwriter(s), if any, to evidence the continued validity of the representations and warranties made pursuant to clause (i) above and to evidence compliance with any customary conditions contained in the underwriting agreement or other agreement entered into by the Company.

(xi) Make available for inspection by a representative of Holders that are selling stockholders, the managing underwriter(s), if any, and any attorneys or accountants retained by such Holders or managing underwriter(s), at the offices where normally kept, during reasonable business hours, financial and other records, pertinent corporate documents and properties of the Company, and cause the officers, directors and employees of the Company to supply all information in each case reasonably requested (and of the type customarily provided in connection with due diligence conducted in connection with a registered public offering of securities) by any such representative, managing underwriter(s), attorney or accountant in connection with such Shelf Registration Statement.

(xii) Use reasonable best efforts to cause all such Registrable Securities to be listed on each national securities exchange on which similar securities issued by the Company are then listed or, if no similar securities issued by the Company are then listed on any national securities exchange, use its reasonable best efforts to cause all such

Registrable Securities to be listed on such securities exchange as the Investor may designate.

(xiii) If requested by Holders of a majority of the Registrable Securities being registered and/or sold in connection therewith, or the managing underwriter(s), if any, promptly include in a prospectus supplement or amendment such information as the Holders of a majority of the Registrable Securities being registered and/or sold in connection therewith or managing underwriter(s), if any, may reasonably request in order to permit the intended method of distribution of such securities and make all required filings of such prospectus supplement or such amendment as soon as practicable after the Company has received such request.

(xiv) Timely provide to its security holders earning statements satisfying the provisions of Section 11(a) of the Securities Act and Rule 158 thereunder.

(e) Suspension of Sales. Upon receipt of written notice from the Company that a registration statement, prospectus or prospectus supplement contains or may contain an untrue statement of a material fact or omits or may omit to state a material fact required to be stated therein or necessary to make the statements therein not misleading or that circumstances exist that make inadvisable use of such registration statement, prospectus or prospectus supplement, the Investor and each Holder of Registrable Securities shall forthwith discontinue disposition of Registrable Securities until the Investor and/or Holder has received copies of a supplemented or amended prospectus or prospectus supplement, or until the Investor and/or such Holder is advised in writing by the Company that the use of the prospectus and, if applicable, prospectus supplement may be resumed, and, if so directed by the Company, the Investor and/or such Holder shall deliver to the Company (at the Company's expense) all copies, other than permanent file copies then in the Investor and/or such Holder's possession, of the prospectus and, if applicable, prospectus supplement covering such Registrable Securities current at the time of receipt of such notice. The total number of days that any such suspension may be in effect in any 12-month period shall not exceed 90 days.

(f) Termination of Registration Rights. A Holder's registration rights as to any securities held by such Holder (and its Affiliates, partners, members and former members) shall not be available unless such securities are Registrable Securities.

(g) Furnishing Information.

(i) Neither the Investor nor any Holder shall use any free writing prospectus (as defined in Rule 405) in connection with the sale of Registrable Securities without the prior written consent of the Company.

(ii) It shall be a condition precedent to the obligations of the Company to take any action pursuant to Section 4.5(d) that Investor and/or the selling Holders and the underwriters, if any, shall furnish to the Company such information regarding themselves, the Registrable Securities held by them and the intended method of disposition of such securities as shall be required to effect the registered offering of their Registrable Securities.

(h) Indemnification.

(i) The Company agrees to indemnify each Holder and, if a Holder is a person other than an individual, such Holder's officers, directors, employees, agents, representatives and Affiliates, and each Person, if any, that controls a Holder within the meaning of the Securities Act (each, an "*Indemnitee*"), against any and all losses, claims, damages, actions, liabilities, costs and expenses (including reasonable fees, expenses and disbursements of attorneys and other professionals incurred in connection with investigating, defending, settling, compromising or paying any such losses, claims, damages, actions, liabilities, costs and expenses), joint or several, arising out of or based upon any untrue statement or alleged untrue statement of material fact contained in any registration statement, including any preliminary prospectus or final prospectus contained therein or any amendments or supplements thereto or any documents incorporated therein by reference or contained in any free writing prospectus (as such term is defined in Rule 405) prepared by the Company or authorized by it in writing for use by such Holder (or any amendment or supplement thereto); or any omission to state therein a material fact required to be stated therein or necessary to make the statements therein, in light of the circumstances under which they were made, not misleading; *provided*, that the Company shall not be liable to such Indemnitee in any such case to the extent that any such loss, claim, damage, liability (or action or proceeding in respect thereof) or expense arises out of or is based upon (A) an untrue statement or omission made in such registration statement, including any such preliminary prospectus or final prospectus contained therein or any such amendments or supplements thereto or contained in any free writing prospectus (as such term is defined in Rule 405) prepared by the Company or authorized by it in writing for use by such Holder (or any amendment or supplement thereto), in reliance upon and in conformity with information regarding such Indemnitee or its plan of distribution or ownership interests which was furnished in writing to the Company by such Indemnitee for use in connection with such registration statement, including any such preliminary prospectus or final prospectus contained therein or any such amendments or supplements thereto, or (B) offers or sales effected by or on behalf of such Indemnitee "by means of" (as defined in Rule 159A) a "free writing prospectus" (as defined in Rule 405) that was not authorized in writing by the Company.

(ii) If the indemnification provided for in Section 4.5(h)(i) is unavailable to an Indemnitee with respect to any losses, claims, damages, actions, liabilities, costs or expenses referred to therein or is insufficient to hold the Indemnitee harmless as contemplated therein, then the Company, in lieu of indemnifying such Indemnitee, shall contribute to the amount paid or payable by such Indemnitee as a result of such losses, claims, damages, actions, liabilities, costs or expenses in such proportion as is appropriate to reflect the relative fault of the Indemnitee, on the one hand, and the Company, on the other hand, in connection with the statements or omissions which resulted in such losses, claims, damages, actions, liabilities, costs or expenses as well as any other relevant equitable considerations. The relative fault of the Company, on the one hand, and of the Indemnitee, on the other hand, shall be determined by reference to, among other factors, whether the untrue statement of a material fact or omission to state a material fact relates to information supplied by the Company or by the Indemnitee and the parties' relative intent, knowledge, access to information and opportunity to correct or prevent such statement or omission; the Company and each Holder agree that it would not be just and equitable if contribution pursuant to this Section 4.5(h)(ii) were determined by *pro rata* allocation or by any other method of allocation that does not take account of the equitable considerations referred to in Section 4.5(h)(i). No Indemnitee guilty of fraudulent misrepresentation (within the meaning of Section 11(f) of the Securities Act) shall be entitled to contribution from the Company if the Company was not guilty of such fraudulent misrepresentation.

(i) Assignment of Registration Rights. The rights of the Investor to registration of Registrable Securities pursuant to Section 4.5(b) may be assigned by the Investor to a transferee or assignee of Registrable Securities with a liquidation preference or, in the case of the Warrant, the liquidation preference of the underlying shares of Warrant Preferred Stock, no less than an amount equal to (i) 2% of the initial aggregate liquidation preference of the Preferred Shares if such initial aggregate liquidation preference is less than $2 billion and (ii) $200 million if the initial aggregate liquidation preference of the Preferred Shares is equal to or greater than $2 billion; *provided*, *however*, the transferor shall, within ten days after such transfer, furnish to the Company written notice of the name and address of such transferee or assignee and the number and type of Registrable Securities that are being assigned.

(j) Clear Market. With respect to any underwritten offering of Registrable Securities by the Investor or other Holders pursuant to this Section 4.5, the Company agrees not to effect (other than pursuant to such registration or pursuant to a Special Registration) any public sale or distribution, or to file any Shelf Registration Statement (other than such registration or a Special Registration) covering any preferred stock of the Company or any securities convertible into or exchangeable or exercisable for preferred stock of the Company, during the period not to exceed ten days prior and 60 days following the effective date of such offering or such longer period up to 90 days as may be requested by the managing underwriter for such underwritten offering. The Company also agrees to cause such of its directors and senior executive officers to execute and deliver customary lock-up agreements in such form and for such time period up to 90 days as may be requested by the managing underwriter. "*Special Registration*" means the registration of (A) equity securities and/or options or other rights in respect thereof solely registered on Form S-4 or Form S-8 (or successor form) or (B) shares of equity securities and/or options or other rights in respect thereof to be offered to directors, members of management, employees, consultants, customers, lenders or vendors of the Company or Company Subsidiaries or in connection with dividend reinvestment plans.

(k) Rule 144; Rule 144A. With a view to making available to the Investor and Holders the benefits of certain rules and regulations of the SEC which may permit the sale of the Registrable Securities to the public without registration, the Company agrees to use its reasonable best efforts to:

(i) make and keep public information available, as those terms are understood and defined in Rule 144(c)(1) or any similar or analogous rule promulgated under the Securities Act, at all times after the Signing Date;

(ii) (A) file with the SEC, in a timely manner, all reports and other documents required of the Company under the Exchange Act, and (B) if at any time the Company is not required to file such reports, make available, upon the request of any Holder, such information necessary to permit sales pursuant to Rule 144A (including the information required by Rule 144A(d)(4) under the Securities Act);

(iii) so long as the Investor or a Holder owns any Registrable Securities, furnish to the Investor or such Holder forthwith upon request: a written statement by the Company as to its compliance with the reporting requirements of Rule 144 under the Securities Act, and of the Exchange Act; a copy of the most recent annual or quarterly report of the Company; and such other reports and documents as the Investor or Holder may reasonably request in availing itself of any rule or regulation of the SEC allowing it to sell any such securities to the public without registration; and

(iv) take such further action as any Holder may reasonably request, all to the extent required from time to time to enable such Holder to sell Registrable Securities without registration under the Securities Act.

(l) As used in this Section 4.5, the following terms shall have the following respective meanings:

(i) "*Holder*" means the Investor and any other holder of Registrable Securities to whom the registration rights conferred by this Agreement have been transferred in compliance with Section 4.5(h) hereof.

(ii) "*Holders' Counsel*" means one counsel for the selling Holders chosen by Holders holding a majority interest in the Registrable Securities being registered.

(iii) "*Register*," "*registered*," and "*registration*" shall refer to a registration effected by preparing and (A) filing a registration statement or amendment thereto in compliance with the Securities Act and applicable rules and regulations thereunder, and the declaration or ordering of effectiveness of such registration statement or amendment thereto or (B) filing a prospectus and/or prospectus supplement in respect of an appropriate effective registration statement on Form S-3.

(iv) "*Registrable Securities*" means (A) all Preferred Shares, (B) the Warrant (subject to Section 4.5(q)) and (C) any equity securities issued or issuable directly or indirectly with respect to the securities referred to in the foregoing clauses (A) or (B) by way of conversion, exercise or exchange thereof, including the Warrant Shares, or share dividend or share split or in connection with a combination of shares, recapitalization, reclassification, merger, amalgamation, arrangement, consolidation or other reorganization, *provided* that, once issued, such securities will not be Registrable Securities when (1) they are sold pursuant to an effective registration statement under the Securities Act, (2) except as provided below in Section 4.5(p), they may be sold pursuant to Rule 144 without limitation thereunder on volume or manner of sale, (3) they shall have ceased to be outstanding or (4) they have been sold in a private transaction in which the transferor's rights under this Agreement are not assigned to the transferee of the securities. No Registrable Securities may be registered under more than one registration statement at any one time.

(v) "*Registration Expenses*" mean all expenses incurred by the Company in effecting any registration pursuant to this Agreement (whether or not any registration or prospectus becomes effective or final) or otherwise complying with its obligations under this Section 4.5, including all registration, filing and listing fees, printing expenses, fees and disbursements of counsel for the Company, blue sky fees and expenses, expenses incurred in connection with any "road show", the reasonable fees and disbursements of Holders' Counsel, and expenses of the Company's independent accountants in connection with any regular or special reviews or audits incident to or required by any such registration, but shall not include Selling Expenses.

(vi) "*Rule 144*", "*Rule 144A*", "*Rule 159A*", "*Rule 405*" and "*Rule 415*" mean, in each case, such rule promulgated under the Securities Act (or any successor provision), as the same shall be amended from time to time.

(vii) "*Selling Expenses*" mean all discounts, selling commissions and stock transfer taxes applicable to the sale of Registrable Securities and fees and disbursements of counsel for any Holder (other than the fees and disbursements of Holders' Counsel included in Registration Expenses).

(m) At any time, any holder of Securities (including any Holder) may elect to forfeit its rights set forth in this Section 4.5 from that date forward; *provided*, that a Holder forfeiting such rights shall nonetheless be entitled to participate under Section 4.5(b)(iv) – (vi) in any Pending Underwritten Offering to the same extent that such Holder would have been entitled to if the holder had not withdrawn; and *provided*, *further*, that no such forfeiture shall terminate a Holder's rights or obligations under Section 4.5(g) with respect to any prior registration or Pending Underwritten Offering. "*Pending Underwritten Offering*" means, with respect to any Holder forfeiting its rights pursuant to this Section 4.5(m), any underwritten offering of Registrable Securities in which such Holder has advised the Company of its intent to register its Registrable Securities either pursuant to Section 4.5(b)(ii) or 4.5(b)(iv) prior to the date of such Holder's forfeiture.

(n) Specific Performance. The parties hereto acknowledge that there would be no adequate remedy at law if the Company fails to perform any of its obligations under this Section 4.5 and that the Investor and the Holders from time to time may be irreparably harmed by any such failure, and accordingly agree that the Investor and such Holders, in addition to any other remedy to which they may be entitled at law or in equity, to the fullest extent permitted and enforceable under applicable law shall be entitled to compel specific performance of the obligations of the Company under this Section 4.5 in accordance with the terms and conditions of this Section 4.5.

(o) No Inconsistent Agreements. The Company shall not, on or after the Signing Date, enter into any agreement with respect to its securities that may impair the rights granted to the Investor and the Holders under this Section 4.5 or that otherwise conflicts with the provisions hereof in any manner that may impair the rights granted to the Investor and the Holders under this Section 4.5. In the event the Company has, prior to the Signing Date, entered into any agreement with respect to its securities that is inconsistent with the rights granted to the Investor and the Holders under this Section 4.5 (including agreements that are inconsistent with the order of priority contemplated by Section 4.5(b)(vi)) or that may otherwise conflict with the provisions hereof, the Company shall use its reasonable best efforts to amend such agreements to ensure they are consistent with the provisions of this Section 4.5.

(p) Certain Offerings by the Investor. In the case of any securities held by the Investor that cease to be Registrable Securities solely by reason of clause (2) in the definition of "Registrable Securities," the provisions of Sections 4.5(b)(ii), clauses (iv), (ix) and (x)-(xii) of Section 4.5(d), Section 4.5(h) and Section 4.5(j) shall continue to apply until such securities otherwise cease to be Registrable Securities. In any such case, an "underwritten" offering or other disposition shall include any distribution of such securities on behalf of the Investor by one or more broker-dealers, an "underwriting agreement" shall include any purchase agreement entered into by such broker-dealers, and any "registration statement" or "prospectus" shall include any offering document approved by the Company and used in connection with such distribution.

(q) Registered Sales of the Warrant. The Holders agree to sell the Warrant or any portion thereof under the Shelf Registration Statement only beginning 30 days after notifying the Company of any such sale, during which 30-day period the Investor and all Holders of the Warrant shall take reasonable steps to agree to revisions to the Warrant to permit a public distribution of the Warrant, including entering into a warrant agreement and appointing a warrant agent.

4.6 Depositary Shares. Upon request by the Investor at any time following the Closing Date, the Company shall promptly enter into a depositary arrangement, pursuant to customary agreements reasonably satisfactory to the Investor and with a depositary reasonably acceptable to the Investor, pursuant to which the Preferred Shares or the Warrant Shares may be deposited and depositary shares, each representing a fraction of a Preferred Share or Warrant Share, as applicable, as specified by the Investor, may be issued. From and after the execution of any such depositary arrangement, and the deposit of any Preferred Shares or Warrant Shares, as applicable, pursuant thereto, the depositary shares issued pursuant thereto shall be deemed "Preferred Shares", "Warrant Shares" and, as applicable, "Registrable Securities" for purposes of this Agreement.

4.7 Restriction on Dividends and Repurchases.

(a) Prior to the earlier of (x) the third anniversary of the Closing Date and (y) the date on which all of the Preferred Shares and Warrant Shares have been redeemed in whole or the Investor has transferred all of the Preferred Shares and Warrant Shares to third parties which are not Affiliates of the Investor, neither the Company nor any Company Subsidiary shall, without the consent of the Investor, declare or pay any dividend or make any distribution on capital stock or other equity securities of any kind of the Company or any Company Subsidiary (other than (i) regular quarterly cash dividends of not more than the amount of the last quarterly cash dividend per share declared or, if lower, announced to its holders of Common Stock an intention to declare, on the Common Stock prior to November 17, 2008, as adjusted for any stock split, stock dividend, reverse stock split, reclassification or similar transaction, (ii) dividends payable solely in shares of Common Stock, (iii) regular dividends on shares of preferred stock in accordance with the terms thereof and which are permitted under the terms of the Preferred Shares and the Warrant Shares, (iv) dividends or distributions by any wholly-owned Company Subsidiary or (v) dividends or distributions by any Company Subsidiary required pursuant to binding contractual agreements entered into prior to November 17, 2008).

(b) During the period beginning on the third anniversary of the Closing Date and ending on the earlier of (i) the tenth anniversary of the Closing Date and (ii) the date on which all of the Preferred Shares and Warrant Shares have been redeemed in whole or the Investor has transferred all of the Preferred Shares and Warrant Shares to third parties which are not Affiliates of the Investor, neither the Company nor any Company Subsidiary shall, without the consent of the Investor, (A) pay any per share dividend or distribution on capital stock or other equity securities of any kind of the Company at a per annum rate that is in excess of 103% of the aggregate per share dividends and distributions for the immediately prior fiscal year (other than regular dividends on shares of preferred stock in accordance with the terms thereof and which are permitted under the terms of the Preferred Shares and the Warrant Shares); *provided* that no increase in the aggregate amount of dividends or distributions on Common Stock shall be permitted as a result of any dividends or distributions paid in shares of Common Stock, any stock split or any similar transaction or (B) pay aggregate dividends or distributions on capital stock or other equity securities of any kind of any Company Subsidiary that is in excess of 103% of the aggregate dividends and distributions paid for the immediately prior fiscal year (other than in the case of this clause (B), (1) regular dividends on shares of preferred stock in accordance with the terms thereof and which are permitted under the terms of the Preferred Shares and the Warrant Shares, (2) dividends or distributions by any wholly-owned Company Subsidiary, (3) dividends or distributions by any Company Subsidiary required pursuant to binding contractual agreements entered into prior to November 17, 2008) or (4) dividends or distributions on newly issued shares of capital stock for cash or other property.

(c) Prior to the earlier of (x) the tenth anniversary of the Closing Date and (y) the date on which all of the Preferred Shares and Warrant Shares have been redeemed in whole or the Investor has transferred all of the Preferred Shares and Warrant Shares to third parties which are not Affiliates of the Investor, neither the Company nor any Company Subsidiary shall, without the consent of the Investor, redeem, purchase or acquire any shares of Common Stock or other capital stock or other equity securities of any kind of the Company or any Company Subsidiary, or any trust preferred securities issued by the Company or any Affiliate of the Company, other than (i) redemptions, purchases or other acquisitions of the Preferred Shares and Warrant Shares, (ii) in connection with the administration of any employee benefit plan in the ordinary course of business and consistent with past practice, (iii) the acquisition by the Company or any of the Company Subsidiaries of record ownership in Junior Stock or Parity Stock for the beneficial ownership of any other persons (other than the Company or any other Company Subsidiary), including as trustees or custodians, (iv) the exchange or conversion of Junior Stock for or into other Junior Stock or of Parity Stock or trust preferred securities for or into other Parity Stock (with the same or lesser aggregate liquidation amount) or Junior Stock, in each case set forth in this clause (iv), solely to the extent required pursuant to binding contractual agreements entered into prior to the Signing Date or any subsequent agreement for the accelerated exercise, settlement or exchange thereof for Common Stock (clauses (ii) and (iii), collectively, the "*Permitted Repurchases*"), (v) redemptions of securities held by the Company or any wholly-owned Company Subsidiary or (vi) redemptions, purchases or other acquisitions of capital stock or other equity securities of any kind of any Company Subsidiary required pursuant to binding contractual agreements entered into prior to November 17, 2008.

(d) Until such time as the Investor ceases to own any Preferred Shares or Warrant Shares, the Company shall not repurchase any Preferred Shares or Warrant Shares from any holder thereof, whether by means of open market purchase, negotiated transaction, or otherwise, other than Permitted Repurchases, unless it offers to repurchase a ratable portion of the Preferred Shares or Warrant Shares, as the case may be, then held by the Investor on the same terms and conditions.

(e) During the period beginning on the tenth anniversary of the Closing and ending on the date on which all of the Preferred Shares and Warrant Shares have been redeemed in whole or the Investor has transferred all of the Preferred Shares and Warrant Shares to third parties which are not Affiliates of the Investor, neither the Company nor any Company Subsidiary shall, without the consent of the Investor, (i) declare or pay any dividend or make any distribution on capital stock or other equity securities of any kind of the Company or any Company Subsidiary; or (ii) redeem, purchase or acquire any shares of Common Stock or other capital stock or other equity securities of any kind of the Company or any Company Subsidiary, or any trust preferred securities issued by the Company or any Affiliate of the Company, other than (A) redemptions, purchases or other acquisitions of the Preferred Shares and Warrant Shares, (B) regular dividends on shares of preferred stock in accordance with the terms thereof and which are permitted under the terms of the Preferred Shares and the Warrant Shares, or (C) dividends or distributions by any wholly-owned Company Subsidiary.

(f) "*Junior Stock*" means Common Stock and any other class or series of stock of the Company the terms of which expressly provide that it ranks junior to the Preferred Shares as to dividend rights and/or as to rights on liquidation, dissolution or winding up of the Company. "*Parity Stock*" means any class or series of stock of the Company the terms of which do not expressly provide that such class or series will rank senior or junior to the Preferred Shares as to dividend rights and/or as to rights on liquidation, dissolution or winding up of the Company (in each case without regard to whether dividends accrue cumulatively or non-cumulatively).

4.8 Executive Compensation. Until such time as the Investor ceases to own any debt or equity securities of the Company acquired pursuant to this Agreement or the Warrant, the Company shall take all necessary action to ensure that its Benefit Plans with respect to its Senior Executive Officers comply in all respects with Section 111(b) of the EESA as implemented by any guidance or regulation thereunder that has been issued and is in effect as of the Closing Date, and shall not adopt any new Benefit Plan with respect to its Senior Executive Officers that does not comply therewith. "*Senior Executive Officers*" means the Company's "senior executive officers" as defined in subsection 111(b)(3) of the EESA and regulations issued thereunder, including the rules set forth in 31 C.F.R. Part 30.

4.9 Related Party Transactions. Until such time as the Investor ceases to own any Purchased Securities or Warrant Shares, the Company and the Company Subsidiaries shall not enter into transactions with Affiliates or related persons (within the meaning of Item 404 under the SEC's Regulation S-K) unless (i) such transactions are on terms no less favorable to the Company and the Company Subsidiaries than could be obtained from an unaffiliated third party, and (ii) have been approved by the audit committee of the Board of Directors or comparable body of independent directors of the Company.

4.10 Bank and Thrift Holding Company Status. If the Company is a Bank Holding Company or a Savings and Loan Holding Company on the Signing Date, then the Company shall maintain its status as a Bank Holding Company or Savings and Loan Holding Company, as the case may be, for as long as the Investor owns any Purchased Securities or Warrant Shares. The Company shall redeem all Purchased Securities and Warrant Shares held by the Investor prior to terminating its status as a Bank Holding Company or Savings and Loan Holding Company, as applicable. "*Bank Holding Company*" means a company registered as such with the Board of Governors of the Federal Reserve System (the "*Federal Reserve*") pursuant to 12 U.S.C. §1842 and the regulations of the Federal Reserve promulgated thereunder. "*Savings and Loan Holding Company*" means a company registered as such with the Office of Thrift Supervision pursuant to 12 U.S.C. §1467(a) and the regulations of the Office of Thrift Supervision promulgated thereunder.

4.11 Predominantly Financial. For as long as the Investor owns any Purchased Securities or Warrant Shares, the Company, to the extent it is not itself an insured depository institution, agrees to remain predominantly engaged in financial activities. A company is predominantly engaged in financial activities if the annual gross revenues derived by the company and all subsidiaries of the company (excluding revenues derived from subsidiary depository institutions), on a consolidated basis, from engaging in activities that are financial in nature or are incidental to a financial activity under subsection (k) of Section 4 of the Bank Holding Company Act of 1956 (12 U.S.C. 1843(k)) represent at least 85 percent of the consolidated annual gross revenues of the company.

Article V
Miscellaneous

5.1 Termination. This Agreement may be terminated at any time prior to the Closing:

(a) by either the Investor or the Company if the Closing shall not have occurred by the 30th calendar day following the Signing Date; *provided*, *however*, that in the event the Closing has not occurred by such 30th calendar day, the parties will consult in good faith to determine whether to extend the term of this Agreement, it being understood that the parties shall be required to consult only until the fifth day after such 30th calendar day and not be under any obligation to extend the term of this Agreement thereafter; *provided*, *further*, that the right to terminate this Agreement under this Section 5.1(a) shall not be available to any party whose breach of any representation or warranty or failure to perform any obligation under this Agreement shall have caused or resulted in the failure of the Closing to occur on or prior to such date; or

(b) by either the Investor or the Company in the event that any Governmental Entity shall have issued an order, decree or ruling or taken any other action restraining, enjoining or otherwise prohibiting the transactions contemplated by this Agreement and such order, decree, ruling or other action shall have become final and nonappealable; or

(c) by the mutual written consent of the Investor and the Company.

In the event of termination of this Agreement as provided in this Section 5.1, this Agreement shall forthwith become void and there shall be no liability on the part of either party hereto except that nothing herein shall relieve either party from liability for any breach of this Agreement.

5.2 Survival of Representations and Warranties. All covenants and agreements, other than those which by their terms apply in whole or in part after the Closing, shall terminate as of the Closing. The representations and warranties of the Company made herein or in any certificates delivered in connection with the Closing shall survive the Closing without limitation.

5.3 Amendment. No amendment of any provision of this Agreement will be effective unless made in writing and signed by an officer or a duly authorized representative of each party; *provided* that the Investor may unilaterally amend any provision of this Agreement to the extent required to comply with any changes after the Signing Date in applicable federal statutes. No failure or delay by any party in exercising any right, power or privilege hereunder shall operate as a waiver thereof nor shall any single or partial exercise thereof preclude any other or further exercise of any other right, power or privilege. The rights and remedies herein provided shall be cumulative of any rights or remedies provided by law.

5.4 Waiver of Conditions. The conditions to each party's obligation to consummate the Purchase are for the sole benefit of such party and may be waived by such party in whole or in part to the extent permitted by applicable law. No waiver will be effective unless it is in a writing signed by a duly authorized officer of the waiving party that makes express reference to the provision or provisions subject to such waiver.

5.5 **Governing Law: Submission to Jurisdiction, Etc. This Agreement will be governed by and construed in accordance with the federal law of the United States if and to**

the extent such law is applicable, and otherwise in accordance with the laws of the State of New York applicable to contracts made and to be performed entirely within such State. Each of the parties hereto agrees (a) to submit to the exclusive jurisdiction and venue of the United States District Court for the District of Columbia and the United States Court of Federal Claims for any and all civil actions, suits or proceedings arising out of or relating to this Agreement or the Warrant or the transactions contemplated hereby or thereby, and (b) that notice may be served upon (i) the Company at the address and in the manner set forth for notices to the Company in Section 5.6 and (ii) the Investor in accordance with federal law. To the extent permitted by applicable law, each of the parties hereto hereby unconditionally waives trial by jury in any civil legal action or proceeding relating to this Agreement or the Warrant or the transactions contemplated hereby or thereby.

5.6 Notices. Any notice, request, instruction or other document to be given hereunder by any party to the other will be in writing and will be deemed to have been duly given (a) on the date of delivery if delivered personally, or by facsimile, upon confirmation of receipt, or (b) on the second business day following the date of dispatch if delivered by a recognized next day courier service. All notices to the Company shall be delivered as set forth in Schedule A, or pursuant to such other instruction as may be designated in writing by the Company to the Investor. All notices to the Investor shall be delivered as set forth below, or pursuant to such other instructions as may be designated in writing by the Investor to the Company.

If to the Investor:

United States Department of the Treasury
1500 Pennsylvania Avenue, NW, Room 2312
Washington, D.C. 20220
Attention: Assistant General Counsel (Banking and Finance)
Facsimile: (202) 622-1974

5.7 Definitions

(a) When a reference is made in this Agreement to a subsidiary of a person, the term "*subsidiary*" means any corporation, partnership, joint venture, limited liability company or other entity (x) of which such person or a subsidiary of such person is a general partner or (y) of which a majority of the voting securities or other voting interests, or a majority of the securities or other interests of which having by their terms ordinary voting power to elect a majority of the board of directors or persons performing similar functions with respect to such entity, is directly or indirectly owned by such person and/or one or more subsidiaries thereof.

(b) The term "*Affiliate*" means, with respect to any person, any person directly or indirectly controlling, controlled by or under common control with, such other person. For purposes of this definition, "*control*" (including, with correlative meanings, the terms "*controlled by*" and "*under common control with*") when used with respect to any person, means the possession, directly or indirectly, of the power to cause the direction of management and/or policies of such person, whether through the ownership of voting securities by contract or otherwise.

(c) The terms "*knowledge of the Company*" or "*Company's knowledge*" mean the actual knowledge after reasonable and due inquiry of the "*officers*" (as such term is defined in Rule 3b-2 under the Exchange Act, but excluding any Vice President or Secretary) of the Company.

5.8 Assignment. Neither this Agreement nor any right, remedy, obligation nor liability arising hereunder or by reason hereof shall be assignable by any party hereto without the prior written consent of the other party, and any attempt to assign any right, remedy, obligation or liability hereunder without such consent shall be void, except (a) an assignment, in the case of a merger, consolidation, statutory share exchange or similar transaction that requires the approval of the Company's stockholders (a "*Business Combination*") where such party is not the surviving entity, or a sale of substantially all of its assets, to the entity which is the survivor of such Business Combination or the purchaser in such sale and (b) as provided in Sections 3.5 and 4.5.

5.9 Severability. If any provision of this Agreement or the Warrant, or the application thereof to any person or circumstance, is determined by a court of competent jurisdiction to be invalid, void or unenforceable, the remaining provisions hereof, or the application of such provision to persons or circumstances other than those as to which it has been held invalid or unenforceable, will remain in full force and effect and shall in no way be affected, impaired or invalidated thereby, so long as the economic or legal substance of the transactions contemplated hereby is not affected in any manner materially adverse to any party. Upon such determination, the parties shall negotiate in good faith in an effort to agree upon a suitable and equitable substitute provision to effect the original intent of the parties.

5.10 No Third Party Beneficiaries. Nothing contained in this Agreement, expressed or implied, is intended to confer upon any person or entity other than the Company and the Investor any benefit, right or remedies, except that the provisions of Section 4.5 shall inure to the benefit of the persons referred to in that Section.

* * *

ANNEX A

FORM OF CERTIFICATE OF DESIGNATIONS FOR PREFERRED STOCK

[SEE ATTACHED]

ANNEX A

FORM OF [CERTIFICATE OF DESIGNATIONS]

OF

FIXED RATE CUMULATIVE PERPETUAL PREFERRED STOCK, SERIES [●]

OF

[●]

[*Insert name of Issuer*], a **[**corporation/bank/banking association**]** organized and existing under the laws of the **[*Insert jurisdiction of organization*]** (the "Issuer"), in accordance with the provisions of Section[s] **[●]** of the **[*Insert applicable statute*]** thereof, does hereby certify:

The board of directors of the Issuer (the "Board of Directors") or an applicable committee of the Board of Directors, in accordance with the **[[**certificate of incorporation/articles of association**]** and bylaws**]** of the Issuer and applicable law, adopted the following resolution on **[●]** creating a series of **[●]** shares of Preferred Stock of the Issuer designated as "Fixed Rate Cumulative Perpetual Preferred Stock, Series **[●]**".

RESOLVED, that pursuant to the provisions of the **[[**certificate of incorporation/articles of association**]** and the bylaws**]** of the Issuer and applicable law, a series of Preferred Stock, par value $**[●]** per share, of the Issuer be and hereby is created, and that the designation and number of shares of such series, and the voting and other powers, preferences and relative, participating, optional or other rights, and the qualifications, limitations and restrictions thereof, of the shares of such series, are as follows:

Part 1. Designation and Number of Shares. There is hereby created out of the authorized and unissued shares of preferred stock of the Issuer a series of preferred stock designated as the "Fixed Rate Cumulative Perpetual Preferred Stock, Series **[●]**" (the "Designated Preferred Stock"). The authorized number of shares of Designated Preferred Stock shall be **[●]**.

Part 2. Standard Provisions. The Standard Provisions contained in Schedule A attached hereto are incorporated herein by reference in their entirety and shall be deemed to be a part of this **[**Certificate of Designations**]** to the same extent as if such provisions had been set forth in full herein.

Part. 3. Definitions. The following terms are used in this **[**Certificate of Designations**]** (including the Standard Provisions in Schedule A hereto) as defined below:

(a) "Common Stock" means the common stock, par value $**[●]** per share, of the Issuer.

(b) "Dividend Payment Date" means February 15, May 15, August 15 and November 15 of each year.

(c) "Junior Stock" means the Common Stock, **[*Insert titles of any existing Junior Stock*]** and any other class or series of stock of the Issuer the terms of which expressly provide that it ranks junior to Designated Preferred Stock as to dividend rights and/or as to rights on liquidation, dissolution or winding up of the Issuer.

(d) "Liquidation Amount" means $**[**1,000**]**[1] per share of Designated Preferred Stock.

(e) "Minimum Amount" means $**[*Insert $ amount equal to 25% of the aggregate value of the Designated Preferred Stock issued on the Original Issue Date*]**.

(f) "Parity Stock" means any class or series of stock of the Issuer (other than Designated Preferred Stock) the terms of which do not expressly provide that such class or series will rank senior or junior to Designated Preferred Stock as to dividend rights and/or as to rights on liquidation, dissolution or winding up of the Issuer (in each case without regard to whether dividends accrue cumulatively or non-cumulatively). Without limiting the foregoing, Parity Stock shall include the Issuer's **[*Insert title(s) of existing classes or series of Parity Stock*]**.

(g) "Signing Date" means **[*Insert date of applicable securities purchase agreement*]**.

Part. 4. Certain Voting Matters. **[*To be inserted if the Charter provides for voting in proportion to liquidation preferences*:** Whether the vote or consent of the holders of a plurality, majority or other portion of the shares of Designated Preferred Stock and any Voting Parity Stock has been cast or given on any matter on which the holders of shares of Designated Preferred Stock are entitled to vote shall be determined by the Issuer by reference to the specified liquidation amount of the shares voted or covered by the consent as if the Issuer were liquidated on the record date for such vote or consent, if any, or, in the absence of a record date, on the date for such vote or consent. For purposes of determining the voting rights of the holders of Designated Preferred Stock under Section 7 of the Standard Provisions forming part of this **[**Certificate of Designations**]**, each holder will be entitled to one vote for each $1,000 of liquidation preference to which such holder's shares are entitled.**]** **[*To be inserted if the Charter does not provide for voting in proportion to liquidation preferences:*** Holders of shares of Designated Preferred Stock will be entitled to one vote for each such share on any matter on which holders of Designated Preferred Stock are entitled to vote, including any action by written consent.**]**

[*Remainder of Page Intentionally Left Blank*]

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[1] If Issuer desires to issue shares with a higher dollar amount liquidation preference, liquidation preference references will be modified accordingly. In such case (in accordance with Section 4.6 of the Securities Purchase Agreement), the issuer will be required to enter into a deposit agreement.

IN WITNESS WHEREOF, **[*Insert name of Issuer*]** has caused this **[**Certificate of Designations**]** to be signed by **[●]**, its **[●]**, this **[●]** day of **[●]**.

[*Insert name of Issuer*]

By: ______________________
Name:
Title:

Schedule A

STANDARD PROVISIONS

Section 1. General Matters. Each share of Designated Preferred Stock shall be identical in all respects to every other share of Designated Preferred Stock. The Designated Preferred Stock shall be perpetual, subject to the provisions of Section 5 of these Standard Provisions that form a part of the Certificate of Designations. The Designated Preferred Stock shall rank equally with Parity Stock and shall rank senior to Junior Stock with respect to the payment of dividends and the distribution of assets in the event of any dissolution, liquidation or winding up of the Issuer.

Section 2. Standard Definitions. As used herein with respect to Designated Preferred Stock:

(a) "Applicable Dividend Rate" means (i) during the period from the Original Issue Date to, but excluding, the first day of the first Dividend Period commencing on or after the fifth anniversary of the Original Issue Date, 5% per annum and (ii) from and after the first day of the first Dividend Period commencing on or after the fifth anniversary of the Original Issue Date, 9% per annum.

(b) "Appropriate Federal Banking Agency" means the "appropriate Federal banking agency" with respect to the Issuer as defined in Section 3(q) of the Federal Deposit Insurance Act (12 U.S.C. Section 1813(q)), or any successor provision.

(c) "Business Combination" means a merger, consolidation, statutory share exchange or similar transaction that requires the approval of the Issuer's stockholders.

(d) "Business Day" means any day except Saturday, Sunday and any day on which banking institutions in the State of New York generally are authorized or required by law or other governmental actions to close.

(e) "Bylaws" means the bylaws of the Issuer, as they may be amended from time to time.

(f) "Certificate of Designations" means the Certificate of Designations or comparable instrument relating to the Designated Preferred Stock, of which these Standard Provisions form a part, as it may be amended from time to time.

(g) "Charter" means the Issuer's certificate or articles of incorporation, articles of association, or similar organizational document.

(h) "Dividend Period" has the meaning set forth in Section 3(a).

(i) "Dividend Record Date" has the meaning set forth in Section 3(a).

(j) "Liquidation Preference" has the meaning set forth in Section 4(a).

(k) "Original Issue Date" means the date on which shares of Designated Preferred Stock are first issued.

(l) "Preferred Director" has the meaning set forth in Section 7(b).

(m) "Preferred Stock" means any and all series of preferred stock of the Issuer, including the Designated Preferred Stock.

(n) "Qualified Equity Offering" means the sale and issuance for cash by the Issuer to persons other than the Issuer or any of its subsidiaries after the Original Issue Date of shares of perpetual Preferred Stock, Common Stock or any combination of such stock, that, in each case, qualify as and may be included in Tier 1 capital of the Issuer at the time of issuance under the applicable risk-based capital guidelines of the Issuer's Appropriate Federal Banking Agency (other than any such sales and issuances made pursuant to agreements or arrangements entered into, or pursuant to financing plans which were publicly announced, on or prior to November 17, 2008).

(o) "Standard Provisions" mean these Standard Provisions that form a part of the Certificate of Designations relating to the Designated Preferred Stock.

(p) "Successor Preferred Stock" has the meaning set forth in Section 5(a).

(q) "Voting Parity Stock" means, with regard to any matter as to which the holders of Designated Preferred Stock are entitled to vote as specified in Sections 7(a) and 7(b) of these Standard Provisions that form a part of the Certificate of Designations, any and all series of Parity Stock upon which like voting rights have been conferred and are exercisable with respect to such matter.

Section 3. Dividends.

(a) Rate. Holders of Designated Preferred Stock shall be entitled to receive, on each share of Designated Preferred Stock if, as and when declared by the Board of Directors or any duly authorized committee of the Board of Directors, but only out of assets legally available therefor, cumulative cash dividends with respect to each Dividend Period (as defined below) at a rate per annum equal to the Applicable Dividend Rate on (i) the Liquidation Amount per share of Designated Preferred Stock and (ii) the amount of accrued and unpaid dividends for any prior Dividend Period on such share of Designated Preferred Stock, if any. Such dividends shall begin to accrue and be cumulative from the Original Issue Date, shall compound on each subsequent Dividend Payment Date (*i.e.*, no dividends shall accrue on other dividends unless and until the first Dividend Payment Date for such other dividends has passed without such other dividends having been paid on such date) and shall be payable quarterly in arrears on each Dividend Payment Date, commencing with the first such Dividend Payment Date to occur at least 20 calendar days after the Original Issue Date. In the event that any Dividend Payment Date would otherwise fall on a day that is not a Business Day, the dividend payment due on that date will be postponed to the next day that is a Business Day and no additional dividends will accrue as a result of that postponement. The period from and including any Dividend Payment Date to, but excluding, the next Dividend Payment Date is a "Dividend Period", provided that the initial

Dividend Period shall be the period from and including the Original Issue Date to, but excluding, the next Dividend Payment Date.

Dividends that are payable on Designated Preferred Stock in respect of any Dividend Period shall be computed on the basis of a 360-day year consisting of twelve 30-day months. The amount of dividends payable on Designated Preferred Stock on any date prior to the end of a Dividend Period, and for the initial Dividend Period, shall be computed on the basis of a 360-day year consisting of twelve 30-day months, and actual days elapsed over a 30-day month.

Dividends that are payable on Designated Preferred Stock on any Dividend Payment Date will be payable to holders of record of Designated Preferred Stock as they appear on the stock register of the Issuer on the applicable record date, which shall be the 15th calendar day immediately preceding such Dividend Payment Date or such other record date fixed by the Board of Directors or any duly authorized committee of the Board of Directors that is not more than 60 nor less than 10 days prior to such Dividend Payment Date (each, a "Dividend Record Date"). Any such day that is a Dividend Record Date shall be a Dividend Record Date whether or not such day is a Business Day.

Holders of Designated Preferred Stock shall not be entitled to any dividends, whether payable in cash, securities or other property, other than dividends (if any) declared and payable on Designated Preferred Stock as specified in this Section 3 (subject to the other provisions of the Certificate of Designations).

(b) Priority of Dividends. So long as any share of Designated Preferred Stock remains outstanding, no dividend or distribution shall be declared or paid on the Common Stock or any other shares of Junior Stock (other than dividends payable solely in shares of Common Stock) or Parity Stock, subject to the immediately following paragraph in the case of Parity Stock, and no Common Stock, Junior Stock or Parity Stock shall be, directly or indirectly, purchased, redeemed or otherwise acquired for consideration by the Issuer or any of its subsidiaries unless all accrued and unpaid dividends for all past Dividend Periods, including the latest completed Dividend Period (including, if applicable as provided in Section 3(a) above, dividends on such amount), on all outstanding shares of Designated Preferred Stock have been or are contemporaneously declared and paid in full (or have been declared and a sum sufficient for the payment thereof has been set aside for the benefit of the holders of shares of Designated Preferred Stock on the applicable record date). The foregoing limitation shall not apply to (i) redemptions, purchases or other acquisitions of shares of Common Stock or other Junior Stock in connection with the administration of any employee benefit plan in the ordinary course of business and consistent with past practice; (ii) the acquisition by the Issuer or any of its subsidiaries of record ownership in Junior Stock or Parity Stock for the beneficial ownership of any other persons (other than the Issuer or any of its subsidiaries), including as trustees or custodians; and (iii) the exchange or conversion of Junior Stock for or into other Junior Stock or of Parity Stock for or into other Parity Stock (with the same or lesser aggregate liquidation amount) or Junior Stock, in each case, solely to the extent required pursuant to binding contractual agreements entered into prior to the Signing Date or any subsequent agreement for the accelerated exercise, settlement or exchange thereof for Common Stock.

When dividends are not paid (or declared and a sum sufficient for payment thereof set aside for the benefit of the holders thereof on the applicable record date) on any Dividend Payment Date (or, in the case of Parity Stock having dividend payment dates different from the Dividend Payment Dates, on a dividend payment date falling within a Dividend Period related to such Dividend Payment Date) in full upon Designated Preferred Stock and any shares of Parity Stock, all dividends declared on Designated Preferred Stock and all such Parity Stock and payable on such Dividend Payment Date (or, in the case of Parity Stock having dividend payment dates different from the Dividend Payment Dates, on a dividend payment date falling within the Dividend Period related to such Dividend Payment Date) shall be declared *pro rata* so that the respective amounts of such dividends declared shall bear the same ratio to each other as all accrued and unpaid dividends per share on the shares of Designated Preferred Stock (including, if applicable as provided in Section 3(a) above, dividends on such amount) and all Parity Stock payable on such Dividend Payment Date (or, in the case of Parity Stock having dividend payment dates different from the Dividend Payment Dates, on a dividend payment date falling within the Dividend Period related to such Dividend Payment Date) (subject to their having been declared by the Board of Directors or a duly authorized committee of the Board of Directors out of legally available funds and including, in the case of Parity Stock that bears cumulative dividends, all accrued but unpaid dividends) bear to each other. If the Board of Directors or a duly authorized committee of the Board of Directors determines not to pay any dividend or a full dividend on a Dividend Payment Date, the Issuer will provide written notice to the holders of Designated Preferred Stock prior to such Dividend Payment Date.

Subject to the foregoing, and not otherwise, such dividends (payable in cash, securities or other property) as may be determined by the Board of Directors or any duly authorized committee of the Board of Directors may be declared and paid on any securities, including Common Stock and other Junior Stock, from time to time out of any funds legally available for such payment, and holders of Designated Preferred Stock shall not be entitled to participate in any such dividends.

Section 4. Liquidation Rights.

(a) Voluntary or Involuntary Liquidation. In the event of any liquidation, dissolution or winding up of the affairs of the Issuer, whether voluntary or involuntary, holders of Designated Preferred Stock shall be entitled to receive for each share of Designated Preferred Stock, out of the assets of the Issuer or proceeds thereof (whether capital or surplus) available for distribution to stockholders of the Issuer, subject to the rights of any creditors of the Issuer, before any distribution of such assets or proceeds is made to or set aside for the holders of Common Stock and any other stock of the Issuer ranking junior to Designated Preferred Stock as to such distribution, payment in full in an amount equal to the sum of (i) the Liquidation Amount per share and (ii) the amount of any accrued and unpaid dividends (including, if applicable as provided in Section 3(a) above, dividends on such amount), whether or not declared, to the date of payment (such amounts collectively, the "Liquidation Preference").

(b) Partial Payment. If in any distribution described in Section 4(a) above the assets of the Issuer or proceeds thereof are not sufficient to pay in full the amounts payable with respect to all outstanding shares of Designated Preferred Stock and the corresponding amounts payable with respect of any other stock of the Issuer ranking equally with Designated Preferred Stock as to such distribution, holders of Designated Preferred Stock and the holders of such other stock shall share ratably in any such distribution in proportion to the full respective distributions to which they are entitled.

(c) Residual Distributions. If the Liquidation Preference has been paid in full to all holders of Designated Preferred Stock and the corresponding amounts payable with respect of any other stock of the Issuer ranking equally with Designated Preferred Stock as to such distribution has been paid in full, the holders of other stock of the Issuer shall be entitled to receive all remaining assets of the Issuer (or proceeds thereof) according to their respective rights and preferences.

(d) Merger, Consolidation and Sale of Assets Not Liquidation. For purposes of this Section 4, the merger or consolidation of the Issuer with any other corporation or other entity, including a merger or consolidation in which the holders of Designated Preferred Stock receive cash, securities or other property for their shares, or the sale, lease or exchange (for cash, securities or other property) of all or substantially all of the assets of the Issuer, shall not constitute a liquidation, dissolution or winding up of the Issuer.

Section 5. Redemption.

(a) Optional Redemption. Except as provided below, the Designated Preferred Stock may not be redeemed prior to the first Dividend Payment Date falling on or after the third anniversary of the Original Issue Date. On or after the first Dividend Payment Date falling on or after the third anniversary of the Original Issue Date, the Issuer, at its option, subject to the approval of the Appropriate Federal Banking Agency, may redeem, in whole or in part, at any time and from time to time, out of funds legally available therefor, the shares of Designated Preferred Stock at the time outstanding, upon notice given as provided in Section 5(c) below, at a redemption price equal to the sum of (i) the Liquidation Amount per share and (ii) except as otherwise provided below, any accrued and unpaid dividends (including, if applicable as provided in Section 3(a) above, dividends on such amount) (regardless of whether any dividends are actually declared) to, but excluding, the date fixed for redemption.

Notwithstanding the foregoing, prior to the first Dividend Payment Date falling on or after the third anniversary of the Original Issue Date, the Issuer, at its option, subject to the approval of the Appropriate Federal Banking Agency, may redeem, in whole or in part, at any time and from time to time, the shares of Designated Preferred Stock at the time outstanding, upon notice given as provided in Section 5(c) below, at a redemption price equal to the sum of (i) the Liquidation Amount per share and (ii) except as otherwise provided below, any accrued and unpaid dividends (including, if applicable as provided in Section 3(a) above, dividends on such amount) (regardless of whether any dividends are actually declared) to, but excluding, the date fixed for redemption; *provided* that (x) the Issuer (or any successor by Business Combination) has received aggregate gross proceeds of not less than the Minimum Amount (plus the "Minimum Amount" as defined in the relevant certificate of designations for each other outstanding series of preferred stock of such successor that was originally issued to the United States Department of the Treasury (the "Successor Preferred Stock") in connection with the Troubled Asset Relief Program Capital Purchase Program) from one or more Qualified Equity Offerings (including Qualified Equity Offerings of such successor), and (y) the aggregate redemption price of the Designated Preferred Stock (and any Successor Preferred Stock) redeemed pursuant to this paragraph may not exceed the aggregate net cash proceeds received by the Issuer (or any successor by Business Combination) from such Qualified Equity Offerings (including Qualified Equity Offerings of such successor).

The redemption price for any shares of Designated Preferred Stock shall be payable on the redemption date to the holder of such shares against surrender of the certificate(s) evidencing such shares to the Issuer or its agent. Any declared but unpaid dividends payable on a redemption date that occurs subsequent to the Dividend Record Date for a Dividend Period shall not be paid to the holder entitled to receive the redemption price on the redemption date, but rather shall be paid to the holder of record of the redeemed shares on such Dividend Record Date relating to the Dividend Payment Date as provided in Section 3 above.

(b) No Sinking Fund. The Designated Preferred Stock will not be subject to any mandatory redemption, sinking fund or other similar provisions. Holders of Designated Preferred Stock will have no right to require redemption or repurchase of any shares of Designated Preferred Stock.

(c) Notice of Redemption. Notice of every redemption of shares of Designated Preferred Stock shall be given by first class mail, postage prepaid, addressed to the holders of record of the shares to be redeemed at their respective last addresses appearing on the books of the Issuer. Such mailing shall be at least 30 days and not more than 60 days before the date fixed for redemption. Any notice mailed as provided in this Subsection shall be conclusively presumed to have been duly given, whether or not the holder receives such notice, but failure duly to give such notice by mail, or any defect in such notice or in the mailing thereof, to any holder of shares of Designated Preferred Stock designated for redemption shall not affect the validity of the proceedings for the redemption of any other shares of Designated Preferred Stock. Notwithstanding the foregoing, if shares of Designated Preferred Stock are issued in book-entry form through The Depository Trust Issuer or any other similar facility, notice of redemption may be given to the holders of Designated Preferred Stock at such time and in any manner permitted by such facility. Each notice of redemption given to a holder shall state: (1) the redemption date; (2) the number of shares of Designated Preferred Stock to be redeemed and, if less than all the shares held by such holder are to be redeemed, the number of such shares to be redeemed from such holder; (3) the redemption price; and (4) the place or places where certificates for such shares are to be surrendered for payment of the redemption price.

(d) Partial Redemption. In case of any redemption of part of the shares of Designated Preferred Stock at the time outstanding, the shares to be redeemed shall be selected either *pro rata* or in such other manner as the Board of Directors or a duly authorized committee thereof may determine to be fair and equitable. Subject to the provisions hereof, the Board of Directors or a duly authorized committee thereof shall have full power and authority to prescribe the terms and conditions upon which shares of Designated Preferred Stock shall be redeemed from time to time. If fewer than all the shares represented by any certificate are redeemed, a new certificate shall be issued representing the unredeemed shares without charge to the holder thereof.

(e) Effectiveness of Redemption. If notice of redemption has been duly given and if on or before the redemption date specified in the notice all funds necessary for the redemption have been deposited by the Issuer, in trust for the *pro rata* benefit of the holders of the shares called for redemption, with a bank or trust company doing business in the Borough of Manhattan, The City of New York, and having a capital and surplus of at least $500 million and selected by the Board of Directors, so as to be and continue to be available solely therefor, then, notwithstanding that any certificate for any share so called for redemption has not been surrendered for cancellation, on and after the redemption date dividends shall cease to accrue on all shares so called for redemption, all shares so called for redemption shall no longer be deemed outstanding and all rights with respect to such shares shall forthwith on such redemption date cease and terminate, except only the right of the holders thereof to receive the amount payable on such redemption from such bank or trust company, without interest. Any funds unclaimed at the end of three years from the redemption date shall, to the extent permitted by law, be released to the Issuer, after which time the holders of the shares so called for redemption shall look only to the Issuer for payment of the redemption price of such shares.

(f) Status of Redeemed Shares. Shares of Designated Preferred Stock that are redeemed, repurchased or otherwise acquired by the Issuer shall revert to authorized but unissued shares of Preferred Stock (*provided* that any such cancelled shares of Designated Preferred Stock may be reissued only as shares of any series of Preferred Stock other than Designated Preferred Stock).

Section 6. Conversion. Holders of Designated Preferred Stock shares shall have no right to exchange or convert such shares into any other securities.

Section 7. Voting Rights.

(a) General. The holders of Designated Preferred Stock shall not have any voting rights except as set forth below or as otherwise from time to time required by law.

(b) Preferred Stock Directors. Whenever, at any time or times, dividends payable on the shares of Designated Preferred Stock have not been paid for an aggregate of six quarterly Dividend Periods or more, whether or not consecutive, the authorized number of directors of the Issuer shall automatically be increased by two and the holders of the Designated Preferred Stock shall have the right, with holders of shares of any one or more other classes or series of Voting Parity Stock outstanding at the time, voting together as a class, to elect two directors (hereinafter the "Preferred Directors" and each a "Preferred Director") to fill such newly created directorships at the Issuer's next annual meeting of stockholders (or at a special meeting called for that purpose prior to such next annual meeting) and at each subsequent annual meeting of stockholders until all accrued and unpaid dividends for all past Dividend Periods, including the latest completed Dividend Period (including, if applicable as provided in Section 3(a) above, dividends on such amount), on all outstanding shares of Designated Preferred Stock have been declared and paid in full at which time such right shall terminate with respect to the Designated Preferred Stock, except as herein or by law expressly provided, subject to revesting in the event of each and every subsequent default of the character above mentioned; *provided* that it shall be a qualification for election for any Preferred Director that the election of such Preferred Director shall not cause the Issuer to violate any corporate governance requirements of any securities exchange or other trading facility on which securities of the Issuer may then be listed or traded that listed or traded companies must have a majority of independent directors. Upon any termination of the right of the holders of shares of Designated Preferred Stock and Voting Parity Stock as a class to vote for directors as provided above, the Preferred Directors shall cease to be qualified as directors, the term of office of all Preferred Directors then in office shall terminate immediately and the authorized number of directors shall be reduced by the number of Preferred Directors elected pursuant hereto. Any Preferred Director may be removed at any time, with or without cause, and any vacancy created thereby may be filled, only by the affirmative vote of the holders a majority of the shares of Designated Preferred Stock at the time outstanding voting separately as a class together with the holders of shares of Voting Parity Stock, to the extent the voting rights of such holders described above are then exercisable. If the office of any Preferred Director becomes vacant for any reason other than removal from office as aforesaid, the remaining Preferred Director may choose a successor who shall hold office for the unexpired term in respect of which such vacancy occurred.

(c) Class Voting Rights as to Particular Matters. So long as any shares of Designated Preferred Stock are outstanding, in addition to any other vote or consent of stockholders required by law or by the Charter, the vote or consent of the holders of at least 66 2/3% of the shares of Designated Preferred Stock at the time outstanding, voting as a separate class, given in person or by proxy, either in writing without a meeting or by vote at any meeting called for the purpose, shall be necessary for effecting or validating:

(i) Authorization of Senior Stock. Any amendment or alteration of the Certificate of Designations for the Designated Preferred Stock or the Charter to authorize or create or increase the authorized amount of, or any issuance of, any shares of, or any securities convertible into or exchangeable or exercisable for shares of, any class or series of capital stock of the Issuer ranking senior to Designated Preferred Stock with respect to either or both the payment of dividends and/or the distribution of assets on any liquidation, dissolution or winding up of the Issuer;

(ii) Amendment of Designated Preferred Stock. Any amendment, alteration or repeal of any provision of the Certificate of Designations for the Designated Preferred Stock or the Charter (including, unless no vote on such merger or consolidation is required by Section 7(c)(iii) below, any amendment, alteration or repeal by means of a merger, consolidation or otherwise) so as to adversely affect the rights, preferences, privileges or voting powers of the Designated Preferred Stock; or

(iii) Share Exchanges, Reclassifications, Mergers and Consolidations. Any consummation of a binding share exchange or reclassification involving the Designated Preferred Stock, or of a merger or consolidation of the Issuer with another corporation or other entity, unless in each case (x) the shares of Designated Preferred Stock remain outstanding or, in the case of any such merger or consolidation with respect to which the Issuer is not the surviving or resulting entity, are converted into or exchanged for preference securities of the surviving or resulting entity or its ultimate parent, and (y) such shares remaining outstanding or such preference securities, as the case may be, have such rights, preferences, privileges and voting powers, and limitations and restrictions thereof, taken as a whole, as are not materially less favorable to the holders thereof than the rights, preferences, privileges and voting powers, and limitations and restrictions thereof, of Designated Preferred Stock immediately prior to such consummation, taken as a whole;

provided, *however*, that for all purposes of this Section 7(c), any increase in the amount of the authorized Preferred Stock, including any increase in the authorized amount of Designated Preferred Stock necessary to satisfy preemptive or similar rights granted by the Issuer to other persons prior to the Signing Date, or the creation and issuance, or an increase in the authorized or issued amount, whether pursuant to preemptive or similar rights or otherwise, of any other series of Preferred Stock, or any securities convertible into or exchangeable or exercisable for any other series of Preferred Stock, ranking equally with and/or junior to Designated Preferred Stock with respect to the payment of dividends (whether such dividends are cumulative or non-cumulative) and the distribution of assets upon liquidation, dissolution or winding up of the Issuer will not be deemed to adversely affect the rights, preferences, privileges or voting powers, and shall not require the affirmative vote or consent of, the holders of outstanding shares of the Designated Preferred Stock.

(d) Changes after Provision for Redemption. No vote or consent of the holders of Designated Preferred Stock shall be required pursuant to Section 7(c) above if, at or prior to the time when any such vote or consent would otherwise be required pursuant to such Section, all outstanding shares of the Designated Preferred Stock shall have been redeemed, or shall have been called for redemption upon proper notice and sufficient funds shall have been deposited in trust for such redemption, in each case pursuant to Section 5 above.

(e) Procedures for Voting and Consents. The rules and procedures for calling and conducting any meeting of the holders of Designated Preferred Stock (including, without limitation, the fixing of a record date in connection therewith), the solicitation and use of proxies at such a meeting, the obtaining of written consents and any other aspect or matter with regard to such a meeting or such consents shall be governed by any rules of the Board of Directors or any duly authorized committee of the Board of Directors, in its discretion, may adopt from time to time, which rules and procedures shall conform to the requirements of the Charter, the Bylaws, and applicable law and the rules of any national securities exchange or other trading facility on which Designated Preferred Stock is listed or traded at the time.

Section 8. Record Holders. To the fullest extent permitted by applicable law, the Issuer and the transfer agent for Designated Preferred Stock may deem and treat the record holder of any share of Designated Preferred Stock as the true and lawful owner thereof for all purposes, and neither the Issuer nor such transfer agent shall be affected by any notice to the contrary.

Section 9. Notices. All notices or communications in respect of Designated Preferred Stock shall be sufficiently given if given in writing and delivered in person or by first class mail, postage prepaid, or if given in such other manner as may be permitted in this Certificate of Designations, in the Charter or Bylaws or by applicable law. Notwithstanding the foregoing, if shares of Designated Preferred Stock are issued in book-entry form through The Depository Trust Issuer or any similar facility, such notices may be given to the holders of Designated Preferred Stock in any manner permitted by such facility.

Section 10. No Preemptive Rights. No share of Designated Preferred Stock shall have any rights of preemption whatsoever as to any securities of the Issuer, or any warrants, rights or options issued or granted with respect thereto, regardless of how such securities, or such warrants, rights or options, may be designated, issued or granted.

Section 11. Replacement Certificates. The Issuer shall replace any mutilated certificate at the holder's expense upon surrender of that certificate to the Issuer. The Issuer shall replace certificates that become destroyed, stolen or lost at the holder's expense upon delivery to the Issuer of reasonably satisfactory evidence that the certificate has been destroyed, stolen or lost, together with any indemnity that may be reasonably required by the Issuer.

Section 12. Other Rights. The shares of Designated Preferred Stock shall not have any rights, preferences, privileges or voting powers or relative, participating, optional or other special rights, or qualifications, limitations or restrictions thereof, other than as set forth herein or in the Charter or as provided by applicable law.

ANNEX B

FORM OF CERTIFICATE OF DESIGNATIONS
FOR WARRANT PREFERRED STOCK

[SEE ATTACHED]

ANNEX B

FORM OF [CERTIFICATE OF DESIGNATIONS]

OF

FIXED RATE CUMULATIVE PERPETUAL PREFERRED STOCK, SERIES [●]

OF

[●]

[*Insert name of Issuer*], a **[**corporation/bank/banking association**]** organized and existing under the laws of the **[*Insert jurisdiction of organization*]** (the "Issuer"), in accordance with the provisions of Section[s] **[●]** of the **[*Insert applicable statute*]** thereof, does hereby certify:

The board of directors of the Issuer (the "Board of Directors") or an applicable committee of the Board of Directors, in accordance with the **[[**certificate of incorporation/articles of association**]** and bylaws**]** of the Issuer and applicable law, adopted the following resolution on **[●]** creating a series of **[●]** shares of Preferred Stock of the Issuer designated as "Fixed Rate Cumulative Perpetual Preferred Stock, Series **[●]**".

RESOLVED, that pursuant to the provisions of the **[[**certificate of incorporation/articles of association**]** and the bylaws**]** of the Issuer and applicable law, a series of Preferred Stock, par value $**[●]** per share, of the Issuer be and hereby is created, and that the designation and number of shares of such series, and the voting and other powers, preferences and relative, participating, optional or other rights, and the qualifications, limitations and restrictions thereof, of the shares of such series, are as follows:

Part 1. Designation and Number of Shares. There is hereby created out of the authorized and unissued shares of preferred stock of the Issuer a series of preferred stock designated as the "Fixed Rate Cumulative Perpetual Preferred Stock, Series **[●]**" (the "Designated Preferred Stock"). The authorized number of shares of Designated Preferred Stock shall be **[●]**.

Part 2. Standard Provisions. The Standard Provisions contained in Schedule A attached hereto are incorporated herein by reference in their entirety and shall be deemed to be a part of this **[**Certificate of Designations**]** to the same extent as if such provisions had been set forth in full herein.

Part. 3. Definitions. The following terms are used in this **[**Certificate of Designations**]** (including the Standard Provisions in Schedule A hereto) as defined below:

(a) "Common Stock" means the common stock, par value $**[●]** per share, of the Issuer.

(b) "Dividend Payment Date" means February 15, May 15, August 15 and November 15 of each year.

(c) "Junior Stock" means the Common Stock, **[*Insert titles of any existing Junior Stock*]** and any other class or series of stock of the Issuer the terms of which expressly provide that it ranks junior to Designated Preferred Stock as to dividend rights and/or as to rights on liquidation, dissolution or winding up of the Issuer.

(d) "Liquidation Amount" means $**[**1,000**]**[1] per share of Designated Preferred Stock.

(e) "Minimum Amount" means $**[*Insert $ amount equal to 25% of the aggregate value of the Designated Preferred Stock issued on the Original Issue Date*]**.

(f) "Parity Stock" means any class or series of stock of the Issuer (other than Designated Preferred Stock) the terms of which do not expressly provide that such class or series will rank senior or junior to Designated Preferred Stock as to dividend rights and/or as to rights on liquidation, dissolution or winding up of the Issuer (in each case without regard to whether dividends accrue cumulatively or non-cumulatively). Without limiting the foregoing, Parity Stock shall include the Issuer's UST Preferred Stock **[**and**]** **[*Insert title(s) of any other classes or series of Parity Stock*]**.

(g) "Signing Date" means **[*Insert date of applicable securities purchase agreement*]**.

(h) "UST Preferred Stock" means the Issuer's Fixed Rate Cumulative Perpetual Preferred Stock, Series **[●]**.

Part. 4. Certain Voting Matters. **[*To be inserted if the Charter provides for voting in proportion to liquidation preferences*:** Whether the vote or consent of the holders of a plurality, majority or other portion of the shares of Designated Preferred Stock and any Voting Parity Stock has been cast or given on any matter on which the holders of shares of Designated Preferred Stock are entitled to vote shall be determined by the Issuer by reference to the specified liquidation amount of the shares voted or covered by the consent as if the Issuer were liquidated on the record date for such vote or consent, if any, or, in the absence of a record date, on the date for such vote or consent. For purposes of determining the voting rights of the holders of Designated Preferred Stock under Section 7 of the Standard Provisions forming part of this **[**Certificate of Designations**]**, each holder will be entitled to one vote for each $1,000 of liquidation preference to which such holder's shares are entitled.**]** **[*To be inserted if the Charter does not provide for voting in proportion to liquidation preferences:*** Holders of shares of Designated Preferred Stock will be entitled to one vote for each such share on any matter on which holders of Designated Preferred Stock are entitled to vote, including any action by written consent.**]**

[*Remainder of Page Intentionally Left Blank*]

[1] If Issuer desires to issue shares with a higher dollar amount liquidation preference, liquidation preference references will be modified accordingly. In such case (in accordance with Section 4.6 of the Securities Purchase Agreement), the issuer will be required to enter into a deposit agreement.

IN WITNESS WHEREOF, **[*Insert name of Issuer*]** has caused this **[**Certificate of Designations**]** to be signed by **[●]**, its **[●]**, this **[●]** day of **[●]**.

[*Insert name of Issuer*]

By: ______________________
Name:
Title:

Schedule A

STANDARD PROVISIONS

Section 1. General Matters. Each share of Designated Preferred Stock shall be identical in all respects to every other share of Designated Preferred Stock. The Designated Preferred Stock shall be perpetual, subject to the provisions of Section 5 of these Standard Provisions that form a part of the Certificate of Designations. The Designated Preferred Stock shall rank equally with Parity Stock and shall rank senior to Junior Stock with respect to the payment of dividends and the distribution of assets in the event of any dissolution, liquidation or winding up of the Issuer.

Section 2. Standard Definitions. As used herein with respect to Designated Preferred Stock:

(a) "Appropriate Federal Banking Agency" means the "appropriate Federal banking agency" with respect to the Issuer as defined in Section 3(q) of the Federal Deposit Insurance Act (12 U.S.C. Section 1813(q)), or any successor provision.

(b) "Business Combination" means a merger, consolidation, statutory share exchange or similar transaction that requires the approval of the Issuer's stockholders.

(c) "Business Day" means any day except Saturday, Sunday and any day on which banking institutions in the State of New York generally are authorized or required by law or other governmental actions to close.

(d) "Bylaws" means the bylaws of the Issuer, as they may be amended from time to time.

(e) "Certificate of Designations" means the Certificate of Designations or comparable instrument relating to the Designated Preferred Stock, of which these Standard Provisions form a part, as it may be amended from time to time.

(f) "Charter" means the Issuer's certificate or articles of incorporation, articles of association, or similar organizational document.

(g) "Dividend Period" has the meaning set forth in Section 3(a).

(h) "Dividend Record Date" has the meaning set forth in Section 3(a).

(i) "Liquidation Preference" has the meaning set forth in Section 4(a).

(j) "Original Issue Date" means the date on which shares of Designated Preferred Stock are first issued.

(k) "Preferred Director" has the meaning set forth in Section 7(b).

(l) "<u>Preferred Stock</u>" means any and all series of preferred stock of the Issuer, including the Designated Preferred Stock.

(m) "<u>Qualified Equity Offering</u>" means the sale and issuance for cash by the Issuer to persons other than the Issuer or any of its subsidiaries after the Original Issue Date of shares of perpetual Preferred Stock, Common Stock or any combination of such stock, that, in each case, qualify as and may be included in Tier 1 capital of the Issuer at the time of issuance under the applicable risk-based capital guidelines of the Issuer's Appropriate Federal Banking Agency (other than any such sales and issuances made pursuant to agreements or arrangements entered into, or pursuant to financing plans which were publicly announced, on or prior to November 17, 2008).

(n) "<u>Standard Provisions</u>" mean these Standard Provisions that form a part of the Certificate of Designations relating to the Designated Preferred Stock.

(o) "<u>Successor Preferred Stock</u>" has the meaning set forth in Section 5(a).

(p) "<u>Voting Parity Stock</u>" means, with regard to any matter as to which the holders of Designated Preferred Stock are entitled to vote as specified in Sections 7(a) and 7(b) of these Standard Provisions that form a part of the Certificate of Designations, any and all series of Parity Stock upon which like voting rights have been conferred and are exercisable with respect to such matter.

Section 3. <u>Dividends</u>.

(a) <u>Rate</u>. Holders of Designated Preferred Stock shall be entitled to receive, on each share of Designated Preferred Stock if, as and when declared by the Board of Directors or any duly authorized committee of the Board of Directors, but only out of assets legally available therefor, cumulative cash dividends with respect to each Dividend Period (as defined below) at a per annum rate of 9.0% on (i) the Liquidation Amount per share of Designated Preferred Stock and (ii) the amount of accrued and unpaid dividends for any prior Dividend Period on such share of Designated Preferred Stock, if any. Such dividends shall begin to accrue and be cumulative from the Original Issue Date, shall compound on each subsequent Dividend Payment Date (*i.e.*, no dividends shall accrue on other dividends unless and until the first Dividend Payment Date for such other dividends has passed without such other dividends having been paid on such date) and shall be payable quarterly in arrears on each Dividend Payment Date, commencing with the first such Dividend Payment Date to occur at least 20 calendar days after the Original Issue Date. In the event that any Dividend Payment Date would otherwise fall on a day that is not a Business Day, the dividend payment due on that date will be postponed to the next day that is a Business Day and no additional dividends will accrue as a result of that postponement. The period from and including any Dividend Payment Date to, but excluding, the next Dividend Payment Date is a "<u>Dividend Period</u>", provided that the initial Dividend Period shall be the period from and including the Original Issue Date to, but excluding, the next Dividend Payment Date.

Dividends that are payable on Designated Preferred Stock in respect of any Dividend Period shall be computed on the basis of a 360-day year consisting of twelve 30-day months. The amount of dividends payable on Designated Preferred Stock on any date prior to the end of a

Dividend Period, and for the initial Dividend Period, shall be computed on the basis of a 360-day year consisting of twelve 30-day months, and actual days elapsed over a 30-day month.

Dividends that are payable on Designated Preferred Stock on any Dividend Payment Date will be payable to holders of record of Designated Preferred Stock as they appear on the stock register of the Issuer on the applicable record date, which shall be the 15th calendar day immediately preceding such Dividend Payment Date or such other record date fixed by the Board of Directors or any duly authorized committee of the Board of Directors that is not more than 60 nor less than 10 days prior to such Dividend Payment Date (each, a "Dividend Record Date"). Any such day that is a Dividend Record Date shall be a Dividend Record Date whether or not such day is a Business Day.

Holders of Designated Preferred Stock shall not be entitled to any dividends, whether payable in cash, securities or other property, other than dividends (if any) declared and payable on Designated Preferred Stock as specified in this Section 3 (subject to the other provisions of the Certificate of Designations).

(b) Priority of Dividends. So long as any share of Designated Preferred Stock remains outstanding, no dividend or distribution shall be declared or paid on the Common Stock or any other shares of Junior Stock (other than dividends payable solely in shares of Common Stock) or Parity Stock, subject to the immediately following paragraph in the case of Parity Stock, and no Common Stock, Junior Stock or Parity Stock shall be, directly or indirectly, purchased, redeemed or otherwise acquired for consideration by the Issuer or any of its subsidiaries unless all accrued and unpaid dividends for all past Dividend Periods, including the latest completed Dividend Period (including, if applicable as provided in Section 3(a) above, dividends on such amount), on all outstanding shares of Designated Preferred Stock have been or are contemporaneously declared and paid in full (or have been declared and a sum sufficient for the payment thereof has been set aside for the benefit of the holders of shares of Designated Preferred Stock on the applicable record date). The foregoing limitation shall not apply to (i) redemptions, purchases or other acquisitions of shares of Common Stock or other Junior Stock in connection with the administration of any employee benefit plan in the ordinary course of business and consistent with past practice; (ii) the acquisition by the Issuer or any of its subsidiaries of record ownership in Junior Stock or Parity Stock for the beneficial ownership of any other persons (other than the Issuer or any of its subsidiaries), including as trustees or custodians; and (iii) the exchange or conversion of Junior Stock for or into other Junior Stock or of Parity Stock for or into other Parity Stock (with the same or lesser aggregate liquidation amount) or Junior Stock, in each case, solely to the extent required pursuant to binding contractual agreements entered into prior to the Signing Date or any subsequent agreement for the accelerated exercise, settlement or exchange thereof for Common Stock.

When dividends are not paid (or declared and a sum sufficient for payment thereof set aside for the benefit of the holders thereof on the applicable record date) on any Dividend Payment Date (or, in the case of Parity Stock having dividend payment dates different from the Dividend Payment Dates, on a dividend payment date falling within a Dividend Period related to such Dividend Payment Date) in full upon Designated Preferred Stock and any shares of Parity Stock, all dividends declared on Designated Preferred Stock and all such Parity Stock and payable on such Dividend Payment Date (or, in the case of Parity Stock having dividend payment dates different from the Dividend Payment Dates, on a dividend payment date falling within the Dividend Period related to such Dividend Payment Date) shall be declared *pro rata* so that the respective amounts of such dividends declared shall bear the same ratio to each other as all accrued and unpaid dividends per share on the shares of Designated Preferred Stock (including, if applicable as provided in Section 3(a) above, dividends on such amount) and all Parity Stock payable on such Dividend Payment Date (or, in the case of Parity Stock having dividend payment dates different from the Dividend Payment Dates, on a dividend payment date falling within the Dividend Period related to such Dividend Payment Date) (subject to their having been declared by the Board of Directors or a duly authorized committee of the Board of Directors out of legally available funds and including, in the case of Parity Stock that bears cumulative dividends, all accrued but unpaid dividends) bear to each other. If the Board of Directors or a duly authorized committee of the Board of Directors determines not to pay any dividend or a full dividend on a Dividend Payment Date, the Issuer will provide written notice to the holders of Designated Preferred Stock prior to such Dividend Payment Date.

Subject to the foregoing, and not otherwise, such dividends (payable in cash, securities or other property) as may be determined by the Board of Directors or any duly authorized committee of the Board of Directors may be declared and paid on any securities, including Common Stock and other Junior Stock, from time to time out of any funds legally available for such payment, and holders of Designated Preferred Stock shall not be entitled to participate in any such dividends.

Section 4. Liquidation Rights.

(a) Voluntary or Involuntary Liquidation. In the event of any liquidation, dissolution or winding up of the affairs of the Issuer, whether voluntary or involuntary, holders of Designated Preferred Stock shall be entitled to receive for each share of Designated Preferred Stock, out of the assets of the Issuer or proceeds thereof (whether capital or surplus) available for distribution to stockholders of the Issuer, subject to the rights of any creditors of the Issuer, before any distribution of such assets or proceeds is made to or set aside for the holders of Common Stock and any other stock of the Issuer ranking junior to Designated Preferred Stock as to such distribution, payment in full in an amount equal to the sum of (i) the Liquidation Amount per share and (ii) the amount of any accrued and unpaid dividends (including, if applicable as provided in Section 3(a) above, dividends on such amount), whether or not declared, to the date of payment (such amounts collectively, the "Liquidation Preference").

(b) Partial Payment. If in any distribution described in Section 4(a) above the assets of the Issuer or proceeds thereof are not sufficient to pay in full the amounts payable with respect to all outstanding shares of Designated Preferred Stock and the corresponding amounts payable with respect of any other stock of the Issuer ranking equally with Designated Preferred Stock as to such distribution, holders of Designated Preferred Stock and the holders of such other stock shall share ratably in any such distribution in proportion to the full respective distributions to which they are entitled.

(c) Residual Distributions. If the Liquidation Preference has been paid in full to all holders of Designated Preferred Stock and the corresponding amounts payable with respect of any other stock of the Issuer ranking equally with Designated Preferred Stock as to such distribution has been paid in full, the holders of other stock of the Issuer shall be entitled to receive all remaining assets of the Issuer (or proceeds thereof) according to their respective rights and preferences.

(d) Merger, Consolidation and Sale of Assets Not Liquidation. For purposes of this Section 4, the merger or consolidation of the Issuer with any other corporation or other entity, including a merger or consolidation in which the holders of Designated Preferred Stock receive cash, securities or other property for their shares, or the sale, lease or exchange (for cash, securities or other property) of all or substantially all of the assets of the Issuer, shall not constitute a liquidation, dissolution or winding up of the Issuer.

Section 5. Redemption.

(a) Optional Redemption. Except as provided below, the Designated Preferred Stock may not be redeemed prior to the later of (i) first Dividend Payment Date falling on or after the third anniversary of the Original Issue Date; and (ii) the date on which all outstanding shares of UST Preferred Stock have been redeemed, repurchased or otherwise acquired by the Issuer. On or after the first Dividend Payment Date falling on or after the third anniversary of the Original Issue Date, the Issuer, at its option, subject to the approval of the Appropriate Federal Banking Agency, may redeem, in whole or in part, at any time and from time to time, out of funds legally available therefor, the shares of Designated Preferred Stock at the time outstanding, upon notice given as provided in Section 5(c) below, at a redemption price equal to the sum of (i) the Liquidation Amount per share and (ii) except as otherwise provided below, any accrued and unpaid dividends (including, if applicable as provided in Section 3(a) above, dividends on such amount) (regardless of whether any dividends are actually declared) to, but excluding, the date fixed for redemption.

Notwithstanding the foregoing, prior to the first Dividend Payment Date falling on or after the third anniversary of the Original Issue Date, the Issuer, at its option, subject to the approval of the Appropriate Federal Banking Agency and subject to the requirement that all outstanding shares of UST Preferred Stock shall previously have been redeemed, repurchased or otherwise acquired by the Issuer, may redeem, in whole or in part, at any time and from time to time, the shares of Designated Preferred Stock at the time outstanding, upon notice given as provided in Section 5(c) below, at a redemption price equal to the sum of (i) the Liquidation Amount per share and (ii) except as otherwise provided below, any accrued and unpaid dividends (including, if applicable as provided in Section 3(a) above, dividends on such amount) (regardless of whether any dividends are actually declared) to, but excluding, the date fixed for redemption; *provided* that (x) the Issuer (or any successor by Business Combination) has received aggregate gross proceeds of not less than the Minimum Amount (plus the "Minimum Amount" as defined in the relevant certificate of designations for each other outstanding series of preferred stock of such successor that was originally issued to the United States Department of the Treasury (the "Successor Preferred Stock") in connection with the Troubled Asset Relief Program Capital Purchase Program) from one or more Qualified Equity Offerings (including Qualified Equity Offerings of such successor), and (y) the aggregate redemption price of the Designated Preferred Stock (and any Successor Preferred Stock) redeemed pursuant to this paragraph may not exceed the aggregate net cash proceeds received by the Issuer (or any successor by Business Combination) from such Qualified Equity Offerings (including Qualified Equity Offerings of such successor).

The redemption price for any shares of Designated Preferred Stock shall be payable on the redemption date to the holder of such shares against surrender of the certificate(s) evidencing such shares to the Issuer or its agent. Any declared but unpaid dividends payable on a redemption date that occurs subsequent to the Dividend Record Date for a Dividend Period shall not be paid to the holder entitled to receive the redemption price on the redemption date, but rather shall be paid to the holder of record of the redeemed shares on such Dividend Record Date relating to the Dividend Payment Date as provided in Section 3 above.

(b) No Sinking Fund. The Designated Preferred Stock will not be subject to any mandatory redemption, sinking fund or other similar provisions. Holders of Designated Preferred Stock will have no right to require redemption or repurchase of any shares of Designated Preferred Stock.

(c) Notice of Redemption. Notice of every redemption of shares of Designated Preferred Stock shall be given by first class mail, postage prepaid, addressed to the holders of record of the shares to be redeemed at their respective last addresses appearing on the books of the Issuer. Such mailing shall be at least 30 days and not more than 60 days before the date fixed for redemption. Any notice mailed as provided in this Subsection shall be conclusively presumed to have been duly given, whether or not the holder receives such notice, but failure duly to give such notice by mail, or any defect in such notice or in the mailing thereof, to any holder of shares of Designated Preferred Stock designated for redemption shall not affect the validity of the proceedings for the redemption of any other shares of Designated Preferred Stock. Notwithstanding the foregoing, if shares of Designated Preferred Stock are issued in book-entry form through The Depository Trust Issuer or any other similar facility, notice of redemption may be given to the holders of Designated Preferred Stock at such time and in any manner permitted by such facility. Each notice of redemption given to a holder shall state: (1) the redemption date; (2) the number of shares of Designated Preferred Stock to be redeemed and, if less than all the shares held by such holder are to be redeemed, the number of such shares to be redeemed from such holder; (3) the redemption price; and (4) the place or places where certificates for such shares are to be surrendered for payment of the redemption price.

(d) Partial Redemption. In case of any redemption of part of the shares of Designated Preferred Stock at the time outstanding, the shares to be redeemed shall be selected either *pro rata* or in such other manner as the Board of Directors or a duly authorized committee thereof may determine to be fair and equitable. Subject to the provisions hereof, the Board of Directors or a duly authorized committee thereof shall have full power and authority to prescribe the terms and conditions upon which shares of Designated Preferred Stock shall be redeemed from time to time. If fewer than all the shares represented by any certificate are redeemed, a new certificate shall be issued representing the unredeemed shares without charge to the holder thereof.

(e) Effectiveness of Redemption. If notice of redemption has been duly given and if on or before the redemption date specified in the notice all funds necessary for the redemption have been deposited by the Issuer, in trust for the *pro rata* benefit of the holders of the shares called for redemption, with a bank or trust company doing business in the Borough of

Manhattan, The City of New York, and having a capital and surplus of at least $500 million and selected by the Board of Directors, so as to be and continue to be available solely therefor, then, notwithstanding that any certificate for any share so called for redemption has not been surrendered for cancellation, on and after the redemption date dividends shall cease to accrue on all shares so called for redemption, all shares so called for redemption shall no longer be deemed outstanding and all rights with respect to such shares shall forthwith on such redemption date cease and terminate, except only the right of the holders thereof to receive the amount payable on such redemption from such bank or trust company, without interest. Any funds unclaimed at the end of three years from the redemption date shall, to the extent permitted by law, be released to the Issuer, after which time the holders of the shares so called for redemption shall look only to the Issuer for payment of the redemption price of such shares.

(f) Status of Redeemed Shares. Shares of Designated Preferred Stock that are redeemed, repurchased or otherwise acquired by the Issuer shall revert to authorized but unissued shares of Preferred Stock (*provided* that any such cancelled shares of Designated Preferred Stock may be reissued only as shares of any series of Preferred Stock other than Designated Preferred Stock).

Section 6. Conversion. Holders of Designated Preferred Stock shares shall have no right to exchange or convert such shares into any other securities.

Section 7. Voting Rights.

(a) General. The holders of Designated Preferred Stock shall not have any voting rights except as set forth below or as otherwise from time to time required by law.

(b) Preferred Stock Directors. Whenever, at any time or times, dividends payable on the shares of Designated Preferred Stock have not been paid for an aggregate of six quarterly Dividend Periods or more, whether or not consecutive, the authorized number of directors of the Issuer shall automatically be increased by two and the holders of the Designated Preferred Stock shall have the right, with holders of shares of any one or more other classes or series of Voting Parity Stock outstanding at the time, voting together as a class, to elect two directors (hereinafter the "Preferred Directors" and each a "Preferred Director") to fill such newly created directorships at the Issuer's next annual meeting of stockholders (or at a special meeting called for that purpose prior to such next annual meeting) and at each subsequent annual meeting of stockholders until all accrued and unpaid dividends for all past Dividend Periods, including the latest completed Dividend Period (including, if applicable as provided in Section 3(a) above, dividends on such amount), on all outstanding shares of Designated Preferred Stock have been declared and paid in full at which time such right shall terminate with respect to the Designated Preferred Stock, except as herein or by law expressly provided, subject to revesting in the event of each and every subsequent default of the character above mentioned; *provided* that it shall be a qualification for election for any Preferred Director that the election of such Preferred Director shall not cause the Issuer to violate any corporate governance requirements of any securities exchange or other trading facility on which securities of the Issuer may then be listed or traded that listed or traded companies must have a majority of independent directors. Upon any termination of the right of the holders of shares of Designated Preferred Stock and Voting Parity Stock as a class to vote for directors as provided above, the Preferred Directors shall cease to be qualified as directors, the term of office of all Preferred Directors then in office shall terminate immediately and the authorized number of directors shall be reduced by the number of Preferred Directors elected pursuant hereto. Any Preferred Director may be removed at any time, with or without cause, and any vacancy created thereby may be filled, only by the affirmative vote of the holders a majority of the shares of Designated Preferred Stock at the time outstanding voting separately as a class together with the holders of shares of Voting Parity Stock, to the extent the voting rights of such holders described above are then exercisable. If the office of any Preferred Director becomes vacant for any reason other than removal from office as aforesaid, the remaining Preferred Director may choose a successor who shall hold office for the unexpired term in respect of which such vacancy occurred.

(c) Class Voting Rights as to Particular Matters. So long as any shares of Designated Preferred Stock are outstanding, in addition to any other vote or consent of stockholders required by law or by the Charter, the vote or consent of the holders of at least 66 2/3% of the shares of Designated Preferred Stock at the time outstanding, voting as a separate class, given in person or by proxy, either in writing without a meeting or by vote at any meeting called for the purpose, shall be necessary for effecting or validating:

(i) Authorization of Senior Stock. Any amendment or alteration of the Certificate of Designations for the Designated Preferred Stock or the Charter to authorize or create or increase the authorized amount of, or any issuance of, any shares of, or any securities convertible into or exchangeable or exercisable for shares of, any class or series of capital stock of the Issuer ranking senior to Designated Preferred Stock with respect to either or both the payment of dividends and/or the distribution of assets on any liquidation, dissolution or winding up of the Issuer;

(ii) Amendment of Designated Preferred Stock. Any amendment, alteration or repeal of any provision of the Certificate of Designations for the Designated Preferred Stock or the Charter (including, unless no vote on such merger or consolidation is required by Section 7(c)(iii) below, any amendment, alteration or repeal by means of a merger, consolidation or otherwise) so as to adversely affect the rights, preferences, privileges or voting powers of the Designated Preferred Stock; or

(iii) Share Exchanges, Reclassifications, Mergers and Consolidations. Any consummation of a binding share exchange or reclassification involving the Designated Preferred Stock, or of a merger or consolidation of the Issuer with another corporation or other entity, unless in each case (x) the shares of Designated Preferred Stock remain outstanding or, in the case of any such merger or consolidation with respect to which the Issuer is not the surviving or resulting entity, are converted into or exchanged for preference securities of the surviving or resulting entity or its ultimate parent, and (y) such shares remaining outstanding or such preference securities, as the case may be, have such rights, preferences, privileges and voting powers, and limitations and restrictions thereof, taken as a whole, as are not materially less favorable to the holders thereof than the rights, preferences, privileges and voting powers, and limitations and restrictions thereof, of Designated Preferred Stock immediately prior to such consummation, taken as a whole;

provided, *however*, that for all purposes of this Section 7(c), any increase in the amount of the authorized Preferred Stock, including any increase in the authorized amount of Designated Preferred Stock necessary to satisfy preemptive or similar rights granted by the Issuer to other persons prior to the Signing Date, or the creation and issuance, or an increase in the authorized or issued amount, whether pursuant to preemptive or similar rights or otherwise, of any other series of Preferred Stock, or any securities convertible into or exchangeable or exercisable for any other series of Preferred Stock, ranking equally with and/or junior to Designated Preferred Stock with respect to the payment of dividends (whether such dividends are cumulative or non-cumulative) and the distribution of assets upon liquidation, dissolution or winding up of the Issuer will not be deemed to adversely affect the rights, preferences, privileges or voting powers, and shall not require the affirmative vote or consent of, the holders of outstanding shares of the Designated Preferred Stock.

(d) Changes after Provision for Redemption. No vote or consent of the holders of Designated Preferred Stock shall be required pursuant to Section 7(c) above if, at or prior to the time when any such vote or consent would otherwise be required pursuant to such Section, all outstanding shares of the Designated Preferred Stock shall have been redeemed, or shall have been called for redemption upon proper notice and sufficient funds shall have been deposited in trust for such redemption, in each case pursuant to Section 5 above.

(e) Procedures for Voting and Consents. The rules and procedures for calling and conducting any meeting of the holders of Designated Preferred Stock (including, without limitation, the fixing of a record date in connection therewith), the solicitation and use of proxies at such a meeting, the obtaining of written consents and any other aspect or matter with regard to such a meeting or such consents shall be governed by any rules of the Board of Directors or any duly authorized committee of the Board of Directors, in its discretion, may adopt from time to time, which rules and procedures shall conform to the requirements of the Charter, the Bylaws, and applicable law and the rules of any national securities exchange or other trading facility on which Designated Preferred Stock is listed or traded at the time.

Section 8. Record Holders. To the fullest extent permitted by applicable law, the Issuer and the transfer agent for Designated Preferred Stock may deem and treat the record holder of any share of Designated Preferred Stock as the true and lawful owner thereof for all purposes, and neither the Issuer nor such transfer agent shall be affected by any notice to the contrary.

Section 9. Notices. All notices or communications in respect of Designated Preferred Stock shall be sufficiently given if given in writing and delivered in person or by first class mail, postage prepaid, or if given in such other manner as may be permitted in this Certificate of Designations, in the Charter or Bylaws or by applicable law. Notwithstanding the foregoing, if shares of Designated Preferred Stock are issued in book-entry form through The Depository Trust Issuer or any similar facility, such notices may be given to the holders of Designated Preferred Stock in any manner permitted by such facility.

Section 10. No Preemptive Rights. No share of Designated Preferred Stock shall have any rights of preemption whatsoever as to any securities of the Issuer, or any warrants, rights or options issued or granted with respect thereto, regardless of how such securities, or such warrants, rights or options, may be designated, issued or granted.

Section 11. <u>Replacement Certificates</u>. The Issuer shall replace any mutilated certificate at the holder's expense upon surrender of that certificate to the Issuer. The Issuer shall replace certificates that become destroyed, stolen or lost at the holder's expense upon delivery to the Issuer of reasonably satisfactory evidence that the certificate has been destroyed, stolen or lost, together with any indemnity that may be reasonably required by the Issuer.

Section 12. <u>Other Rights</u>. The shares of Designated Preferred Stock shall not have any rights, preferences, privileges or voting powers or relative, participating, optional or other special rights, or qualifications, limitations or restrictions thereof, other than as set forth herein or in the Charter or as provided by applicable law.

ANNEX C

FORM OF WAIVER

In consideration for the benefits I will receive as a result of my employer's participation in the United States Department of the Treasury's TARP Capital Purchase Program, I hereby voluntarily waive any claim against the United States or my employer for any changes to my compensation or benefits that are required to comply with the regulation issued by the Department of the Treasury as published in the Federal Register on October 20, 2008.

I acknowledge that this regulation may require modification of the compensation, bonus, incentive and other benefit plans, arrangements, policies and agreements (including so-called "golden parachute" agreements) that I have with my employer or in which I participate as they relate to the period the United States holds any equity or debt securities of my employer acquired through the TARP Capital Purchase Program.

This waiver includes all claims I may have under the laws of the United States or any state related to the requirements imposed by the aforementioned regulation, including without limitation a claim for any compensation or other payments I would otherwise receive, any challenge to the process by which this regulation was adopted and any tort or constitutional claim about the effect of these regulations on my employment relationship.

ANNEX D

FORM OF OPINION

(a) The Company has been duly incorporated and is validly existing as a corporation in good standing under the laws of the state of its incorporation.

(b) The Preferred Shares have been duly and validly authorized, and, when issued and delivered pursuant to the Agreement, the Preferred Shares will be duly and validly issued and fully paid and non-assessable, will not be issued in violation of any preemptive rights, and will rank *pari passu* with or senior to all other series or classes of Preferred Stock issued on the Closing Date with respect to the payment of dividends and the distribution of assets in the event of any dissolution, liquidation or winding up of the Company.

(c) The Warrant has been duly authorized and, when executed and delivered as contemplated by the Agreement, will constitute a valid and legally binding obligation of the Company enforceable against the Company in accordance with its terms, except as the same may be limited by applicable bankruptcy, insolvency, reorganization, moratorium or similar laws affecting the enforcement of creditors' rights generally and general equitable principles, regardless of whether such enforceability is considered in a proceeding at law or in equity.

(d) The shares of Warrant Preferred Stock issuable upon exercise of the Warrant have been duly authorized and reserved for issuance upon exercise of the Warrant and when so issued in accordance with the terms of the Warrant will be validly issued, fully paid and non-assessable, and will rank *pari passu* with or senior to all other series or classes of Preferred Stock, whether or not issued or outstanding, with respect to the payment of dividends and the distribution of assets in the event of any dissolution, liquidation or winding up of the Company.

(e) The Company has the corporate power and authority to execute and deliver the Agreement and the Warrant and to carry out its obligations thereunder (which includes the issuance of the Preferred Shares, Warrant and Warrant Shares).

(f) The execution, delivery and performance by the Company of the Agreement and the Warrant and the consummation of the transactions contemplated thereby have been duly authorized by all necessary corporate action on the part of the Company and its stockholders, and no further approval or authorization is required on the part of the Company.

(g) The Agreement is a valid and binding obligation of the Company enforceable against the Company in accordance with its terms, except as the same may be limited by applicable bankruptcy, insolvency, reorganization, moratorium or similar laws affecting the enforcement of creditors' rights generally and general equitable principles, regardless of whether such enforceability is considered in a proceeding at law or in equity; *provided*, *however*, such counsel need express no opinion with respect to Section 4.5(h) or the severability provisions of the Agreement insofar as Section 4.5(h) is concerned.

ANNEX E

FORM OF WARRANT

[SEE ATTACHED]

ANNEX E

FORM OF WARRANT TO PURCHASE PREFERRED STOCK

THE SECURITIES REPRESENTED BY THIS INSTRUMENT HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, OR THE SECURITIES LAWS OF ANY STATE AND MAY NOT BE TRANSFERRED, SOLD OR OTHERWISE DISPOSED OF EXCEPT WHILE A REGISTRATION STATEMENT RELATING THERETO IS IN EFFECT UNDER SUCH ACT AND APPLICABLE STATE SECURITIES LAWS OR PURSUANT TO AN EXEMPTION FROM REGISTRATION UNDER SUCH ACT OR SUCH LAWS. THIS INSTRUMENT IS ISSUED SUBJECT TO THE RESTRICTIONS ON TRANSFER AND OTHER PROVISIONS OF A SECURITIES PURCHASE AGREEMENT BETWEEN THE ISSUER OF THESE SECURITIES AND THE INVESTOR REFERRED TO THEREIN, A COPY OF WHICH IS ON FILE WITH THE ISSUER. THE SECURITIES REPRESENTED BY THIS INSTRUMENT MAY NOT BE SOLD OR OTHERWISE TRANSFERRED EXCEPT IN COMPLIANCE WITH SAID AGREEMENT. ANY SALE OR OTHER TRANSFER NOT IN COMPLIANCE WITH SAID AGREEMENT WILL BE VOID.

WARRANT
to purchase
____
Shares of Preferred Stock

of ______________________

Issue Date: _________________________

1. Definitions. Unless the context otherwise requires, when used herein the following terms shall have the meanings indicated.

"*Board of Directors*" means the board of directors of the Company, including any duly authorized committee thereof.

"*business day*" means any day except Saturday, Sunday and any day on which banking institutions in the State of New York generally are authorized or required by law or other governmental actions to close.

"*Charter*" means, with respect to any Person, its certificate or articles of incorporation, articles of association, or similar organizational document.

"*Company*" means the Person whose name, corporate or other organizational form and jurisdiction of organization is set forth in Item 1 of Schedule A hereto.

"*Exchange Act*" means the Securities Exchange Act of 1934, as amended, or any successor statute, and the rules and regulations promulgated thereunder.

"*Exercise Price*" means the amount set forth in Item 2 of Schedule A hereto.

"*Expiration Time*" has the meaning set forth in Section 3.

"*Issue Date*" means the date set forth in Item 3 of Schedule A hereto.

"*Liquidation Amount*" means the amount set forth in Item 4 of Schedule A hereto.

"*Original Warrantholder*" means the United States Department of the Treasury. Any actions specified to be taken by the Original Warrantholder hereunder may only be taken by such Person and not by any other Warrantholder.

"*Person*" has the meaning given to it in Section 3(a)(9) of the Exchange Act and as used in Sections 13(d)(3) and 14(d)(2) of the Exchange Act.

"*Preferred Stock*" means the series of perpetual preferred stock set forth in Item 5 of Schedule A hereto.

"*Purchase Agreement*" means the Securities Purchase Agreement – Standard Terms incorporated into the Letter Agreement, dated as of the date set forth in Item 6 of Schedule A hereto, as amended from time to time, between the Company and the United States Department of the Treasury (the "*Letter Agreement*"), including all annexes and schedules thereto.

"*Regulatory Approvals*" with respect to the Warrantholder, means, to the extent applicable and required to permit the Warrantholder to exercise this Warrant for shares of Preferred Stock and to own such Preferred Stock without the Warrantholder being in violation of applicable law, rule or regulation, the receipt of any necessary approvals and authorizations of, filings and registrations with, notifications to, or expiration or termination of any applicable waiting period under, the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended, and the rules and regulations thereunder.

"*SEC*" means the U.S. Securities and Exchange Commission.

"*Securities Act*" means the Securities Act of 1933, as amended, or any successor statute, and the rules and regulations promulgated thereunder.

"*Shares*" has the meaning set forth in Section 2.

"*Warrantholder*" has the meaning set forth in Section 2.

"*Warrant*" means this Warrant, issued pursuant to the Purchase Agreement.

2. Number of Shares; Exercise Price. This certifies that, for value received, the United States Department of the Treasury or its permitted assigns (the "*Warrantholder*") is entitled, upon the terms and subject to the conditions hereinafter set forth, to acquire from the

Company, in whole or in part, after the receipt of all applicable Regulatory Approvals, if any, up to an aggregate of the number of fully paid and nonassessable shares of Preferred Stock set forth in Item 7 of Schedule A hereto (the "*Shares*"), at a purchase price per share of Preferred Stock equal to the Exercise Price.

3. Exercise of Warrant; Term. Subject to Section 2, to the extent permitted by applicable laws and regulations, the right to purchase the Shares represented by this Warrant is exercisable, in whole or in part by the Warrantholder, at any time or from time to time after the execution and delivery of this Warrant by the Company on the date hereof, but in no event later than 5:00 p.m., New York City time on the tenth anniversary of the Issue Date (the "*Expiration Time*"), by (A) the surrender of this Warrant and Notice of Exercise annexed hereto, duly completed and executed on behalf of the Warrantholder, at the principal executive office of the Company located at the address set forth in Item 8 of Schedule A hereto (or such other office or agency of the Company in the United States as it may designate by notice in writing to the Warrantholder at the address of the Warrantholder appearing on the books of the Company), and (B) payment of the Exercise Price for the Shares thereby purchased, by having the Company withhold, from the shares of Preferred Stock that would otherwise be delivered to the Warrantholder upon such exercise, shares of Preferred Stock issuable upon exercise of the Warrant with an aggregate Liquidation Amount equal in value to the aggregate Exercise Price as to which this Warrant is so exercised.

If the Warrantholder does not exercise this Warrant in its entirety, the Warrantholder will be entitled to receive from the Company within a reasonable time, and in any event not exceeding three business days, a new warrant in substantially identical form for the purchase of that number of Shares equal to the difference between the number of Shares subject to this Warrant and the number of Shares as to which this Warrant is so exercised. Notwithstanding anything in this Warrant to the contrary, the Warrantholder hereby acknowledges and agrees that its exercise of this Warrant for Shares is subject to the condition that the Warrantholder will have first received any applicable Regulatory Approvals.

4. Issuance of Shares; Authorization. Certificates for Shares issued upon exercise of this Warrant will be issued in such name or names as the Warrantholder may designate and will be delivered to such named Person or Persons within a reasonable time, not to exceed three business days after the date on which this Warrant has been duly exercised in accordance with the terms of this Warrant. The Company hereby represents and warrants that any Shares issued upon the exercise of this Warrant in accordance with the provisions of Section 3 will be duly and validly authorized and issued, fully paid and nonassessable and free from all taxes, liens and charges (other than liens or charges created by the Warrantholder, income and franchise taxes incurred in connection with the exercise of the Warrant or taxes in respect of any transfer occurring contemporaneously therewith). The Company agrees that the Shares so issued will be deemed to have been issued to the Warrantholder as of the close of business on the date on which this Warrant and payment of the Exercise Price are delivered to the Company in accordance with the terms of this Warrant, notwithstanding that the stock transfer books of the Company may then be closed or certificates representing such Shares may not be actually delivered on such date. The Company will at all times reserve and keep available, out of its authorized but unissued preferred stock, solely for the purpose of providing for the exercise of this Warrant, the aggregate number of shares of Preferred Stock then issuable upon exercise of this Warrant at any

time. The Company will use reasonable best efforts to ensure that the Shares may be issued without violation of any applicable law or regulation or of any requirement of any securities exchange on which the Shares are listed or traded.

5. No Rights as Stockholders; Transfer Books. This Warrant does not entitle the Warrantholder to any voting rights or other rights as a stockholder of the Company prior to the date of exercise hereof. The Company will at no time close its transfer books against transfer of this Warrant in any manner which interferes with the timely exercise of this Warrant.

6. Charges, Taxes and Expenses. Issuance of certificates for Shares to the Warrantholder upon the exercise of this Warrant shall be made without charge to the Warrantholder for any issue or transfer tax or other incidental expense in respect of the issuance of such certificates, all of which taxes and expenses shall be paid by the Company.

7. Transfer/Assignment.

(A) Subject to compliance with clause (B) of this Section 7, this Warrant and all rights hereunder are transferable, in whole or in part, upon the books of the Company by the registered holder hereof in person or by duly authorized attorney, and a new warrant shall be made and delivered by the Company, of the same tenor and date as this Warrant but registered in the name of one or more transferees, upon surrender of this Warrant, duly endorsed, to the office or agency of the Company described in Section 3. All expenses (other than stock transfer taxes) and other charges payable in connection with the preparation, execution and delivery of the new warrants pursuant to this Section 7 shall be paid by the Company.

(B) The transfer of the Warrant and the Shares issued upon exercise of the Warrant are subject to the restrictions set forth in Section 4.4 of the Purchase Agreement. If and for so long as required by the Purchase Agreement, this Warrant shall contain the legends as set forth in Section 4.2(a) of the Purchase Agreement.

8. Exchange and Registry of Warrant. This Warrant is exchangeable, upon the surrender hereof by the Warrantholder to the Company, for a new warrant or warrants of like tenor and representing the right to purchase the same aggregate number of Shares. The Company shall maintain a registry showing the name and address of the Warrantholder as the registered holder of this Warrant. This Warrant may be surrendered for exchange or exercise in accordance with its terms, at the office of the Company, and the Company shall be entitled to rely in all respects, prior to written notice to the contrary, upon such registry.

9. Loss, Theft, Destruction or Mutilation of Warrant. Upon receipt by the Company of evidence reasonably satisfactory to it of the loss, theft, destruction or mutilation of this Warrant, and in the case of any such loss, theft or destruction, upon receipt of a bond, indemnity or security reasonably satisfactory to the Company, or, in the case of any such mutilation, upon surrender and cancellation of this Warrant, the Company shall make and deliver, in lieu of such lost, stolen, destroyed or mutilated Warrant, a new Warrant of like tenor and representing the right to purchase the same aggregate number of Shares as provided for in such lost, stolen, destroyed or mutilated Warrant.

10. Saturdays, Sundays, Holidays, etc. If the last or appointed day for the taking of any action or the expiration of any right required or granted herein shall not be a business day, then such action may be taken or such right may be exercised on the next succeeding day that is a business day.

11. Rule 144 Information. The Company covenants that it will use its reasonable best efforts to timely file all reports and other documents required to be filed by it under the Securities Act and the Exchange Act and the rules and regulations promulgated by the SEC thereunder (or, if the Company is not required to file such reports, it will, upon the request of any Warrantholder, make publicly available such information as necessary to permit sales pursuant to Rule 144 under the Securities Act), and it will use reasonable best efforts to take such further action as any Warrantholder may reasonably request, in each case to the extent required from time to time to enable such holder to, if permitted by the terms of this Warrant and the Purchase Agreement, sell this Warrant without registration under the Securities Act within the limitation of the exemptions provided by (A) Rule 144 under the Securities Act, as such rule may be amended from time to time, or (B) any successor rule or regulation hereafter adopted by the SEC. Upon the written request of any Warrantholder, the Company will deliver to such Warrantholder a written statement that it has complied with such requirements.

12. Adjustments and Other Rights. For so long as the Original Warrantholder holds this Warrant or any portion thereof, if any event occurs that, in the good faith judgment of the Board of Directors of the Company, would require adjustment of the Exercise Price or number of Shares into which this Warrant is exercisable in order to fairly and adequately protect the purchase rights of the Warrants in accordance with the essential intent and principles of the Purchase Agreement and this Warrant, then the Board of Directors shall make such adjustments in the application of such provisions, in accordance with such essential intent and principles, as shall be reasonably necessary, in the good faith opinion of the Board of Directors, to protect such purchase rights as aforesaid.

Whenever the Exercise Price or the number of Shares into which this Warrant is exercisable shall be adjusted as provided in this Section 12, the Company shall forthwith file at the principal office of the Company a statement showing in reasonable detail the facts requiring such adjustment and the Exercise Price that shall be in effect and the number of Shares into which this Warrant shall be exercisable after such adjustment, and the Company shall also cause a copy of such statement to be sent by mail, first class postage prepaid, to each Warrantholder at the address appearing in the Company's records.

13. No Impairment. The Company will not, by amendment of its Charter or through any reorganization, transfer of assets, consolidation, merger, dissolution, issue or sale of securities or any other voluntary action, avoid or seek to avoid the observance or performance of any of the terms to be observed or performed hereunder by the Company, but will at all times in good faith assist in the carrying out of all the provisions of this Warrant and in taking of all such action as may be necessary or appropriate in order to protect the rights of the Warrantholder.

14. Governing Law. This Warrant will be governed by and construed in accordance with the federal law of the United States if and to the extent such law is applicable, and otherwise in accordance with the laws of the State of New York applicable to contracts made and

to be performed entirely within such State. Each of the Company and the Warrantholder agrees (a) to submit to the exclusive jurisdiction and venue of the United States District Court for the District of Columbia for any civil action, suit or proceeding arising out of or relating to this Warrant or the transactions contemplated hereby, and (b) that notice may be served upon the Company at the address in Section 17 below and upon the Warrantholder at the address for the Warrantholder set forth in the registry maintained by the Company pursuant to Section 8 hereof. To the extent permitted by applicable law, each of the Company and the Warrantholder hereby unconditionally waives trial by jury in any civil legal action or proceeding relating to the Warrant or the transactions contemplated hereby or thereby.

15. Binding Effect. This Warrant shall be binding upon any successors or assigns of the Company.

16. Amendments. This Warrant may be amended and the observance of any term of this Warrant may be waived only with the written consent of the Company and the Warrantholder.

17. Notices. Any notice, request, instruction or other document to be given hereunder by any party to the other will be in writing and will be deemed to have been duly given (a) on the date of delivery if delivered personally, or by facsimile, upon confirmation of receipt, or (b) on the second business day following the date of dispatch if delivered by a recognized next day courier service. All notices hereunder shall be delivered as set forth in Item 9 of Schedule A hereto, or pursuant to such other instructions as may be designated in writing by the party to receive such notice.

18. Entire Agreement. This Warrant, the forms attached hereto and Schedule A hereto (the terms of which are incorporated by reference herein), and the Letter Agreement (including all documents incorporated therein), contain the entire agreement between the parties with respect to the subject matter hereof and supersede all prior and contemporaneous arrangements or undertakings with respect thereto.

[Remainder of page intentionally left blank]

[Form of Notice of Exercise]

Date: _________

TO: **[Company]**

RE: Election to Purchase Preferred Stock

The undersigned, pursuant to the provisions set forth in the attached Warrant, hereby agrees to subscribe for and purchase the number of shares of the Preferred Stock set forth below covered by such Warrant. The undersigned, in accordance with Section 3 of the Warrant, hereby agrees to pay the aggregate Exercise Price for such shares of Preferred Stock in the manner set forth in Section 3(B) of the Warrant. A new warrant evidencing the remaining shares of Preferred Stock covered by such Warrant, but not yet subscribed for and purchased, if any, should be issued in the name set forth below.

Number of Shares of Preferred Stock ________________________

Aggregate Exercise Price: ________________________

Holder: _____________________________
By: ________________________
Name: ________________________
Title: ________________________

IN WITNESS WHEREOF, the Company has caused this Warrant to be duly executed by a duly authorized officer.

Dated: ________________

COMPANY: ________________

By: ________________________
Name:
Title:

Attest:

By: ________________________________
Name:
Title:

[Signature Page to Warrant]

SCHEDULE A

Item 1
Name:
Corporate or other organizational form:
Jurisdiction of organization:

Item 2
Exercise Price:[1]

Item 3
Issue Date:

Item 4
Liquidation Amount:

Item 5
Series of Perpetual Preferred Stock:

Item 6
Date of Letter Agreement between the Company and the United States Department of the Treasury:

Item 7
Number of shares of Preferred Stock:[2]

Item 8
Company's address:

Item 9
Notice information:

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[1] $0.01 per share or such greater amount as the Charter may require as the par value of the Preferred Stock.

[2] The initial number of shares of Preferred Stock for which this Warrant is exercisable shall include the number of shares required to effect the cashless exercise pursuant to Section 3(B) of this Warrant (e.g., such number of shares of Preferred Stock having an aggregate Liquidation Amount equal in value to the aggregate Exercise Price) such that, following exercise of this Warrant and payment of the Exercise Price in accordance with such Section 3(B), the net number of shares of Preferred Stock delivered to the Warrantholder (and rounded to the nearest whole share) would have an aggregate Liquidation Amount equal to 5% of the aggregate amount invested by the United States Department of the Treasury on the investment date.

SCHEDULE A

ADDITIONAL TERMS AND CONDITIONS

Company Information:

Name of Company	Uwharrie Capital Corp
Corporate or other organizational form:	Corporation
Jurisdiction of Organization:	North Carolina
Appropriate Federal Banking Agency:	Federal Reserve
Notice Information:	Robert Bratton Uwharrie Capital Corp P.O. Box 338 Albemarle, NC 28002-0338 Office: (704) 982-4415 Fax: (704) 982-4355 [redacted]

Terms of the Purchase:

Series of Preferred Stock Purchased:	Series A
Per Share Liquidation Preference of Preferred Stock:	$1,000
Number of Shares of Preferred Stock Purchased:	10,000
Dividend Payment Dates on Preferred Stock:	2/15, 5/15, 8/15, 11/15
Series of Warrant Preferred Stock:	Series B
Number of Warrant Shares:	500.005
Number of Net Warrant Shares (after net settlement):	500
Exercise Price of the Warrant:	$0.01
Purchase Price:	$10,000,000

Closing:

Location of Closing:	Telephonic
Time of Closing:	9:00 a.m. EST
Date of Closing:	December 23, 2008

UST No. 129

Wire Information for Closing:

ABA Number: [redacted]
Bank: BK STANLY ALBEMARL
Account Name: Uwharrie Capital Corp
Account Number: [redacted]
Beneficiary: Uwharrie Capital Corp

Contact for Confirmation of Wire Information:

David Beaver
Uwharrie Capital Corp
704-983-6181 ext. 1488
[redacted]

SCHEDULE B

CAPITALIZATION

Capitalization Date:	November 30, 2008
Common Stock	
Par Value:	$1.25
Total Authorized:	20,000,000
Outstanding:	7,407,851
Subject to warrants, options, convertible securities, etc.:	446,465
Reserved for benefit plans and other issuances:	250,685
Remaining authorized but unissued:	11,894,999
Shares issued after Capitalization Date (other than pursuant to warrants, options, convertible securities, etc. as set forth above):	7,407,851
Preferred Stock	
Par Value:	No par
Total Authorized:	10,000,000
Outstanding (by series):	-0-
Reserved for issuance:	Series A – 10,000 Series B – 501
Remaining authorized but unissued:	9,989,499
Holders of 5% or more of any class of capital stock	Primary Address
Uwharrie Capital Corp Employee Stock Ownership Plan (5.12%)	132 North First Street Albemarle, NC 28001

UST No. 129

SCHEDULE C

LITIGATION

List any exceptions to the representation and warranty in Section 2.2(l) of the Securities Purchase Agreement – Standard Terms.

If none, please so indicate by checking the box: ☒.

UST No. 129

SCHEDULE D

COMPLIANCE WITH LAWS

List any exceptions to the representation and warranty in the second sentence of Section 2.2(m) of the Securities Purchase Agreement – Standard Terms.

If none, please so indicate by checking the box: ☒.

List any exceptions to the representation and warranty in the last sentence of Section 2.2(m) of the Securities Purchase Agreement – Standard Terms.

If none, please so indicate by checking the box: ☒.

SCHEDULE E

REGULATORY AGREEMENTS

List any exceptions to the representation and warranty in Section 2.2(s) of the Securities Purchase Agreement – Standard Terms.

If none, please so indicate by checking the box: ☒.

UWHARRIE CAPITAL CORP
DISCLOSURE SCHEDULE
Delivered Pursuant to Section 2.1(a) of that Certain Stock Purchase Agreement with the United States Department of the Treasury

The following schedule is intended to serve as the "Disclosure Schedule" of Uwharrie Capital Corp (the "Company"), as defined in Section 2.1(a) of that certain Letter Agreement including the Stock Purchase Agreement – Standard Terms attached thereto as Exhibit A (the "Agreement") between the Company and the United States Department of the Treasury. The section numbers contained in the schedule below correspond to those contained in the Agreement. Capitalized terms not otherwise defined herein have the same meaning as provided in the Agreement.

Section 2.2(e)(iii)

The Company is required to file a Current Report on Form 8-K within four (4) business days of the Signing Date

Section 2.2(h)

Attached hereto are the Company's Quarterly Reports on Form 10-Q for the fiscal quarters ended September 30, 2008, June 30, 2008 and March 31, 2008 and the Company's annual reports to shareholders for the fiscal years ended December 31, 2007, 2006 and 2005, which reports contain the consolidated financial statements required to be "previously disclosed" pursuant to Section 2.2(h) of the Agreement.

Section 2.2(i)(ii)

The Company's subsidiary banks outsource their core data processing function to Fidelity Information Systems.

Section 2.2(k)

In 2008, the Company offered and sold subordinated debt securities pursuant to Regulation D promulgated under the Securities Act of 1933, as amended. The circumstances of that offering would not require integration with the offering of the Purchased Securities under the Securities Act and relevant regulations and guidance promulgated thereunder.

EX-13 2 dex13.htm 2005 ANNUAL REPORT TO SHAREHOLDERS

Exhibit 13

Uwharrie Capital Corp

2005

ANNUAL REPORT TO SHAREHOLDERS

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UWHARRIE CAPITAL CORP AND SUBSIDIARIES

Description of Business

Uwharrie Capital Corp (the “Company”) is a North Carolina bank holding company. The Company was organized on July 1, 1993 to become the bank holding company for the Bank of Stanly (“Stanly”), a North Carolina commercial bank chartered on September 28, 1983, and its three wholly-owned subsidiaries, The Strategic Alliance Corporation, BOS Agency, Inc., and Gateway Mortgage, Inc., a mortgage brokerage company. The Company also owns three non-bank subsidiaries, Strategic Investment Advisors, Inc., Uwharrie Mortgage, Inc. and Uwharrie Statutory Trust 1.

Stanly engages in retail and commercial banking, with five banking offices in Stanly County. Stanly provides a wide range of banking services including deposit accounts, commercial, consumer, home equity and residential mortgage loans, safe deposit boxes, and electronic banking services.

On January 19, 2000, the Company completed its acquisition of Anson BanCorp, Inc. and its subsidiary, Anson Savings Bank. The savings bank retained its North Carolina savings bank charter and became a wholly-owned subsidiary of Uwharrie Capital Corp as Anson Bank & Trust Co. (“Anson”) and provides financial services to customers through one banking office in Anson County.

On April 10, 2003, the Company capitalized a new wholly-owned subsidiary bank, Cabarrus Bank & Trust Company (“Cabarrus”), located in Concord, North Carolina. As of that date, Cabarrus purchased two branch offices located in Cabarrus County from Stanly to begin its operation. Cabarrus operates as a commercial bank and provides a full range of banking services.

The Company and its subsidiaries are located in Stanly County, Anson County and Cabarrus County. However, the Company intends to prudently expand its service area to include the entire Uwharrie Lakes Region of North Carolina.

Depository services offered by the subsidiary banks include personal and commercial checking, savings, money market, certificates of deposit accounts and individual retirement accounts, all tailored to meet customers’ needs. The banks provide fixed and variable rate loans, which include mortgage, home equity, lines of credit, consumer and commercial loans. The banks also offer Internet Banking and 24-Hour Telephone Banking, providing customers the convenience of access to account information, rate information and accessibility of funds transfers between accounts. Other services include MasterCard® credit cards and a Visa® Check Card which functions as a point-of-sale (POS) and automated teller machine (ATM) card. Customers can use the Check Card for purchases at any merchant accepting Visa and at any ATM displaying the STAR® or CIRRUS® networks regionally and worldwide, respectively.

Strategic Investment Advisors Inc. provides portfolio management services to its customers. The Strategic Alliance Corporation (Strategic Alliance®) is a registered broker-dealer with the National Association of Securities Dealers, Inc. (“NASD”). BOS Agency provides insurance products and is licensed in the state of North Carolina. Through Strategic Investment Group, a DBA for a partnership with UVEST Financial Services, Inc., securities and insurance products are offered including fixed annuities, long-term care, and life products. Group insurance products are offered through an arrangement with Benchmark Life Strategies as well as Medicare supplement products.

The Strategic Alliance Corporation. Member NASD/SIPC.

Securities and insurance products are offered by, and Financial Consultants are registered with UVEST Financial Services, member NASD/SIPC. UVEST, Strategic Investment Group and Uwharrie Capital Corp affiliates are independent entities. Securities and/or insurance products are not FDIC insured, are not deposits or other obligations of any depository institution, are not guaranteed by any depository institution and are subject to investment risks, including possible loss of the principal amount invested.

Bank of Stanly. Member FDIC. Equal Housing Lender.
Anson Bank & Trust Co. Member FDIC. Equal Housing Lender.
Cabarrus Bank & Trust Company, Member FDIC, Equal Housing Lender.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES

Financial Highlights

(Dollars in thousands except per share amounts)	2005	2004	Percent Increase (Decrease)
For the year:			
Net Income	$ 1,517	$ 253	499.60%
Basic net income per common share (1)	$ .22	$ .04	450.00%
Diluted net income per common share	$ .21	$ .03	600.00%
Weighted average common shares outstanding (diluted)	7,202,692	7,314,407	(1.52)%
At year-end:			
Total assets	$ 350,190	$ 329,262	6.36%
Total earning assets	323,286	302,836	6.75%
Loans, net of unearned income	276,196	263,738	4.72%
Total interest-bearing liabilities	273,703	263,714	3.79%
Shareholders' equity	27,453	27,156	1.09%
Book value per share (1)	$ 3.85	$ 3.74	2.94%
Averages for the year:			
Total assets	$ 334,193	$ 321,093	4.08%
Total earning assets	307,229	293,232	4.77%
Loans, net of unearned income	267,164	256,525	4.15%
Total interest-bearing liabilities	260,711	254,986	2.25%
Shareholders' equity	27,187	27,741	(2.00)%
Financial Ratios (in percentage):			
Return on average assts	0.45%	0.08%	
Return on average shareholders' equity	5.58%	0.91%	
Average equity to average assets	8.14%	8.64%	
Net interest margin (fully tax equivalent basis)	4.16%	3.96%	
Allowance as % of loans at year-end	1.62%	1.89%	
Allowance as % of nonperforming loans	239.09%	147.59%	
Nonperforming loans to total loans	.68%	1.29%	
Nonperforming assets to total assets	.58%	1.17%	
Net loan charge-offs to average loans	0.47%	0.13%	

(1) Net income per share, book value per share, and shares outstanding at year-end have been adjusted to reflect the 3% stock dividends in 2005 and in 2004.

Market for the Company's Common Stock and Related Security Holder Matters

It is the philosophy of Uwharrie Capital Corp to promote a broad base of local shareholders. Therefore, management makes every reasonable effort to match willing buyers with willing sellers as they become known for the purpose of private negotiations for the purchase and sale of the Company's common stock. The Company on a quarterly basis has an independent valuation of the Company stock performed to assist with fairness and market efficiencies regarding these private negotiations and makes the most current valuation available to interested shareholders. Trades of the Company's stock also occur in the Over-the-Counter marketplace that involve a "spread" between the bid and ask prices to compensate the brokerage firms involved in the Over-the-Counter market. In addition, Uwharrie Capital Corp has adopted a program of on-going open market purchases of shares of the Company's stock. The combination of public and private trades as well as the holding company purchases provides good liquidity for the investors of Uwharrie Capital Corp stock. The Board of Directors has historically adopted a dividend policy on an annual basis. For 2005, Uwharrie Capital Corp declared a 3% stock dividend. The Board of Directors determines, on an annual basis, the dividend policy that is consistent with the capital needs of the Company.

Shareholders needing information about purchasing or selling shares of Uwharrie Capital Corp should contact Tamara M. Singletary or Lisa E. Hartsell, Investor Relations at Uwharrie Capital Corp, 132 N. First Street, Post Office Box 338, Albemarle, NC 28002.

DIXON HUGHES PLLC

Certified Public Accountants and Advisors

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and Board of Directors
Uwharrie Capital Corp
Albemarle, North Carolina

We have audited the accompanying consolidated balance sheets of Uwharrie Capital Corp and Subsidiaries (the "Company") as of December 31, 2005 and 2004, and the related consolidated statements of income, comprehensive income, changes in shareholders' equity and cash flows for each of the years in the three-year period ended December 31, 2005. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Uwharrie Capital Corp and Subsidiaries as of December 31, 2005 and 2004, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2005 in conformity with accounting principles generally accepted in the United States of America.

Dixon Hughes PLLC

Raleigh, North Carolina
March 10, 2006

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
December 31, 2005 and 2004

	2005	2004
ASSETS		
Cash and due from banks	$ 11,438,743	$ 11,449,899
Interest-earning deposits with banks	3,729,940	4,024,870
Federal funds sold	6,200,000	4,100,000
Securities available for sale, at fair value	35,015,878	28,523,869
Loans	276,195,875	263,738,272
Less allowance for loan losses	(4,482,304)	(4,982,891)
Net loans	271,713,571	258,755,381
Premises and equipment, net	8,432,296	8,317,497
Interest receivable	1,525,366	1,273,777
Federal Home Loan Bank stock	2,072,200	2,385,300
Bank owned life insurance	4,948,772	4,794,098
Goodwill	987,436	987,436
Other assets	4,125,663	4,649,868
Total assets	$350,189,865	$329,261,995
LIABILITIES		
Deposits:		
Demand noninterest-bearing	$ 47,279,515	$ 36,866,146
Interest checking and money market accounts	83,679,745	80,393,133
Savings deposits	36,689,516	39,852,601
Time deposits, $100,000 and over	38,881,451	36,966,834
Other time deposits	67,445,605	52,860,046
Total deposits	273,975,832	246,938,760
Short-term borrowed funds	7,903,628	11,062,392
Long-term debt	39,103,025	42,734,057
Interest payable	368,850	301,930
Other liabilities	1,385,754	1,069,057
Total liabilities	322,737,089	302,106,196
Off balance sheet items, commitments and contingencies (Note 11)		
SHAREHOLDERS' EQUITY		
Common stock, $1.25 par value: 20,000,000 shares authorized; shares issued and outstanding 7,138,686 and 7,057,755 shares, respectively	8,923,357	8,822,194
Additional paid-in capital	12,409,663	12,043,348
Unearned ESOP compensation	(914,088)	(964,935)
Undivided profits	6,705,568	6,469,142
Accumulated other comprehensive income	328,276	786,050
Total shareholders' equity	27,452,776	27,155,799
Total liabilities and shareholders' equity	$350,189,865	$329,261,995

The accompanying notes are an integral part of the consolidated financial statements

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
Years Ended December 31, 2005, 2004 and 2003

	2005	2004	2003
Interest Income			
Loans, including fees	$17,445,375	$14,468,077	$13,293,773
Investment securities:			
US Treasury	97,997	101,947	50,104
US Government agencies and corporations	537,184	438,589	412,570
State and political subdivisions	652,828	717,382	729,703
Other	125,127	80,943	84,362
Interest-earning deposits with banks and federal funds sold	302,088	98,985	26,380
Total interest income	19,160,599	15,905,923	14,596,892
Interest Expense			
Time deposits, $100,000 and over	1,168,441	787,945	648,149
Other interest-bearing deposits	3,304,493	1,888,256	1,849,393
Short-term borrowed funds	238,533	83,764	147,417
Long-term debt	1,918,200	1,974,131	1,960,997
Total interest expense	6,629,667	4,734,096	4,605,956
Net interest income	12,530,932	11,171,827	9,990,936
Provision for loan losses	755,000	2,091,500	593,000
Net interest income after provision for loan losses	11,775,932	9,080,327	9,397,936
Noninterest Income			
Service charges on deposit accounts	1,706,784	1,435,827	1,347,538
Other service fees and commissions	1,727,955	1,426,481	1,052,354
Gain(loss) on sale of securities	(16,272)	2,373	128,845
Income from mortgage loan sales	554,414	844,882	2,072,433
Other income	378,220	560,961	558,412
Total noninterest income	4,351,101	4,270,524	5,159,582
Noninterest Expense			
Salaries and employee benefits	8,001,849	7,154,708	6,853,200
Net occupancy expense	642,537	640,546	530,726
Equipment expense	639,332	665,458	638,391
Data processing costs	843,514	809,938	805,118
Other noninterest expense	3,959,640	4,026,370	3,638,784
Total noninterest expense	14,086,872	13,297,020	12,466,219
Income before taxes	2,040,161	53,831	2,091,299
Income taxes (benefit)	523,570	(199,500)	531,480
Net income	$ 1,516,591	$ 253,331	$ 1,559,819
Net income per common share			
Basic	$ 0.22	$ 0.04	$ 0.22
Diluted	$ 0.21	$ 0.03	$ 0.21
Weighted average shares outstanding			
Basic	7,031,322	7,147,074	7,158,342
Diluted	7,202,692	7,314,407	7,292,338

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

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
Years Ended December 31, 2005, 2004 and 2003

	2005	2004	2003
Net Income	$1,516,591	$ 253,331	$1,559,819
Other comprehensive income (loss):			
Unrealized gains (losses) on available for sale securities	(761,273)	(251,972)	(204,209)
Related tax effect	293,500	97,145	60,407
Reclassification of losses(gains) recognized in net income	16,272	(2,373)	(128,845)
Related tax effect	(6,273)	915	38,113
Total other comprehensive loss	(457,774)	(156,285)	(234,534)
Comprehensive income	$1,058,817	$ 97,046	$1,325,285

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

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
Years Ended December 31, 2005, 2004 and 2003

	Common Stock		Additional Paid-in Capital	Unearned ESOP Compensation	Undivided Profits	Accumulated Other Comprehensive Income	Total
	Shares	Amount					
Balance, January 1, 2003	6,494,101	$8,117,626	$ 9,817,177	$(1,055,610)	$ 7,066,142	$ 1,176,869	$25,122,204
Net income	—	—	—	—	1,559,819	—	1,559,819
Other comprehensive income	—	—	—	—	—	(234,534)	(234,534)
Release of ESOP shares	—	—	27,922	43,593	—	—	71,515
Common stock issued pursuant to:							
3% stock dividend	202,409	253,011	900,720	—	(1,153,731)	—	—
Stock options exercised	39,095	48,869	81,460	—	—	—	130,329
Stock offering:							
Shares issued	361,730	452,163	1,433,685	—	—	—	1,885,848
Repurchase of common stock	(119,951)	(149,939)	(525,723)	—	—	—	(675,662)
Cash paid - fractional shares	—	—	—	—	(7,845)	—	(7,845)
Balance, December. 31, 2003	6,977,384	8,721,730	11,735,241	(1,012,017)	7,464,385	942,335	27,851,674
Net income	—	—	—	—	253,331	—	253,331
Other comprehensive income	—	—	—	—	—	(156,285)	(156,285)
Release of ESOP shares	—	—	40,817	47,082	—	—	87,899
Common stock issued pursuant to:							
3% stock dividend	206,657	255,763	982,128	—	(1,237,891)	—	—
Stock options exercised	119,372	151,774	419,473	—	—	—	571,247
Tax benefit of stock options exercised	—	—	50,492	—	—	—	50,492
Repurchase of common stock	(245,658)	(307,073)	(1,184,803)	—	—	—	(1,491,876)
Cash paid - fractional shares	—	—	—	—	(10,683)	—	(10,683)
Balance, December 31, 2004	7,057,755	8,822,194	12,043,348	(964,935)	6,469,142	786,050	27,155,799
Net income	—	—	—	—	1,516,591	—	1,516,591
Other comprehensive income	—	—	—	—	—	(457,774)	(457,774)
Release of ESOP shares	—	—	33,395	50,847	—	—	84,242
Common stock issued pursuant to:							
3% stock dividend	206,730	258,412	1,012,977	—	(1,271,389)	—	—
Stock options issued	71,227	89,034	258,193	—	—	—	347,227
Tax benefit of stock options exercised	—	—	29,928	—	—	—	29,928
Repurchase of common stock	(197,026)	(246,283)	(968,178)	—	—	—	(1,214,461)
Cash paid - fractional shares	—	—	—	—	(8,776)	—	(8,776)
Balance, December 31, 2005	7,138,686	$8,923,357	$12,409,663	$ (914,088)	$ 6,705,568	$ 328,276	$27,452,776

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

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
Years Ended December 31, 2005, 2004 and 2003

	2005	2004	2003
Cash flows from operating activities			
Net income	$ 1,516,591	$ 253,331	$ 1,559,819
Adjustments to reconcile net income to net cash Provided (used) by operating activities:			
Depreciation	645,758	610,089	602,597
Net amortization of security premiums/discounts	36,707	73,926	129,463
Provision for loan losses	755,000	2,091,500	593,000
Deferred income taxes	52,000	(472,000)	(223,481)
Net realized loss (gain) on available for sale securities	16,272	(2,373)	(128,845)
Income from mortgage loan sales	(554,414)	(844,882)	(2,072,433)
Proceeds from sales of loans held for sale	29,162,011	44,089,905	93,843,832
Origination of loans held for sale	(29,057,631)	(42,959,955)	(91,771,399)
Gain on sale of premises, equipment and other assets	(76,463)	(15,796)	(113,418)
Increase in cash surrender value of life insurance	(154,674)	(190,013)	(171,019)
Loss (gain) on sales of other real estate	(11,690)	2,330	27,808
Release of ESOP Shares	84,242	87,898	71,515
Net change in interest receivable	(251,589)	(117,534)	(24,033)
Net change in other assets	652,434	244,445	(124,095)
Net change in interest payable	66,920	19,447	5,083
Net change in other liabilities	316,697	161,780	175,388
Net cash provided by operating activities	3,198,171	3,032,098	2,379,782
Cash flows from investing activities			
Proceeds from sales, maturities and calls of securities available for sale	1,487,264	3,534,537	7,976,008
Purchase of securities available for sale	(8,777,253)	(4,677,766)	(8,742,785)
Net increase in loans	(14,332,476)	(24,076,492)	(46,234,604)
Proceeds from sale of premises, equipment and other assets	229,986	404,442	478,694
Purchase of premises and equipment	(775,588)	(856,987)	(3,154,927)
Investment in life insurance	—	—	(401,000)
Proceeds from sales of other real estate	1,392,544	162,212	649,943
Net cash used by investing activities	(20,775,523)	(25,510,054)	(49,428,671)
Cash flows from financing activities			
Net increase in deposit accounts	27,037,072	34,376,000	39,006,347
Net increase (decrease) in short-term borrowed funds	(3,158,764)	(1,752,077)	1,905,886
Net increase (decrease) in long-term borrowed funds	(3,631,032)	(3,530,805)	6,469,511
Repurchases of common stock	(1,214,461)	(1,491,875)	(675,662)
Net proceeds from issuance of common stock	347,227	571,247	2,016,177
Cash paid for fractional shares	(8,776)	(10,683)	(7,845)
Net cash provided by financing activities	19,371,266	28,161,807	48,714,414
Increase in cash and cash equivalents	1,793,914	5,683,851	1,665,525
Cash and cash equivalents, beginning of period	19,574,769	13,890,918	12,225,393
Cash and cash equivalents, end of period	$ 21,368,683	$ 19,574,769	$ 13,890,918
Supplemental Disclosures of Cash Flow Information			
Interest paid	$ 6,562,747	$ 4,714,649	$ 4,600,873
Income taxes paid	240,610	434,000	793,338
Supplemental Schedule of Non-Cash Investing and Financing Activities			
Decrease in fair value of securities available for sale, net of tax	(457,774)	(156,285)	(234,534)
Loans securitized into investment securities	—	—	1,327,500
Loans transferred to foreclosed real estate	1,069,320	537,000	72,165
Tax benefit of stock options exercised	29,928	50,492	—

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

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1 - Significant Accounting Policies

Nature of Business

Uwharrie Capital Corp (the "Company") was incorporated under North Carolina law for the purpose of becoming the holding company for Bank of Stanly ("Stanly"). On July 1, 1993, Stanly became a wholly-owned subsidiary of the Company through a one-for-one exchange of the common stock of Stanly for common stock of the Company.

Stanly was incorporated on September 28, 1983, under the laws of the State of North Carolina and began operations on January 26, 1984 in Albemarle, North Carolina. Deposits with Stanly are insured by the Federal Deposit Insurance Corporation ("FDIC"). Stanly is under regulation of both the FDIC and the North Carolina State Banking Commission. Through its five branch locations in Stanly County, Stanly provides a wide range of deposit accounts, commercial, consumer, home equity and residential mortgage loans, safe deposit boxes and automated banking.

In 1987, Stanly established a wholly-owned subsidiary, BOS Agency, Inc. ("BOS Agency"), which engages in investment and insurance product sales. In 1989, Stanly established a second wholly-owned subsidiary, BOS Financial Corporation, for the purpose of conducting business as a broker/dealer in securities. During 1993, BOS Financial Corporation changed its name to The Strategic Alliance Corporation ("Strategic Alliance") and was licensed as a broker/dealer by the National Association of Securities Dealers.

The Company formed a new subsidiary, Strategic Investment Advisors, Inc. ("SIA"), during 1999 to provide investment advisory and asset management services. This subsidiary is registered as an investment advisor with the Securities and Exchange Commission.

On January 19, 2000, the Company completed its acquisition of Anson BanCorp, Inc. and its subsidiary, Anson Savings Bank. The savings bank retained its North Carolina savings bank charter and became a wholly-owned subsidiary of Uwharrie Capital Corp as Anson Bank & Trust Co ("Anson"), operating out of its main office branch in Wadesboro.

On August 4, 2000, Stanly acquired another subsidiary, Gateway Mortgage, Inc. ("Gateway"), a mortgage origination company.

On April 10, 2003, the Company capitalized a new wholly-owned subsidiary bank, Cabarrus ("Cabarrus") Bank & Trust Company, located in Concord, North Carolina. As of that date, Cabarrus purchased two branch offices located in Cabarrus County from Stanly to begin its operation. Cabarrus operates as a commercial bank and provides a full range of banking services.

On April 7, 2004 Uwharrie Mortgage, Inc. was established as a subsidiary of the Company to serve in the capacity of trustee and substitute trustee under deeds of trust.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company, Stanly, Anson, Cabarrus, SIA and its indirectly-owned subsidiaries, BOS Agency, Strategic Alliance and Gateway. All significant intercompany transactions and balances have been eliminated in consolidation.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1 - Significant Accounting Policies (Continued)

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses.

Cash and Cash Equivalents

For the purpose of presentation in the consolidated statements of cash flows, cash and cash equivalents are defined as those amounts included in the balance sheet captions “Cash and due from banks,” “Interest-earning deposits with banks”, and “Federal funds sold”.

Investment Securities Held To Maturity

Investment securities classified as held to maturity are debt securities the Company has both the intent and ability to hold to maturity regardless of changes in market conditions, liquidity needs or changes in general economic conditions. These securities are carried at cost adjusted for amortization of premium and accretion of discount, computed by the interest method over their contractual lives. Declines in the fair value of individual held to maturity securities below their cost that are other than temporary would result in write-downs of the individual securities to their fair value. Such write-downs would be included in earnings as realized losses. The Company had no securities held to maturity at December 31, 2005 and 2004.

Investment Securities Available for Sale

Investment securities available for sale consist of bonds and notes not classified as trading securities nor as held to maturity securities. Unrealized holding gains and losses on available for sale securities are reported as a net amount in other comprehensive income, net of income taxes. Gains and losses on the sale of available for sale securities are determined using the specific identification method. Declines in the fair value of individual available for sale securities below their cost that are other than temporary would result in write-downs of the individual securities to their fair value. Such write-downs would be included in earnings as realized losses. Premiums and discounts are recognized in interest income using the interest method over the period to maturity.

Loans Held for Sale

Loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated fair value in the aggregate. Net unrealized losses, if any, are recognized through a valuation allowance by charges to income.

Loans

The Company grants mortgage, commercial and consumer loans to customers. The ability of the Company’s borrowers to honor their contracts is largely dependent upon the real estate and general economic conditions in the Company’s market area. Loans that management has the

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1 - Significant Accounting Policies (Continued)

intent and ability to hold for the foreseeable future or until maturity or pay-off are reported at their outstanding unpaid principal balances adjusted for charge-offs, the allowance for loan losses, and any deferred fees or costs. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the related loan yield using the interest method.

The accrual of interest on mortgage and commercial loans is discontinued at the time the loan is 90 days delinquent unless the credit is well-secured and in process of collection. Credit card loans and other personal loans are typically charged off no later than 180 days past due. In all cases, loans are placed on nonaccrual or charged-off at an earlier date if collection of principal or interest is considered doubtful.

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

Allowance for Loan Losses

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management’s periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower’s ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available. In addition, regulatory examiners may require the Company to recognize adjustments to the allowance for loan loss based on their judgment about information available to them at the time of their assessment.

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

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1 - Significant Accounting Policies (Continued)

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Company does not separately identify individual consumer, residential and other loans for impairment disclosures.

Servicing Assets

Servicing assets are recognized as separate assets when rights are acquired through purchase or through sale of financial assets. Capitalized servicing rights are reported in other assets and are amortized into other income in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets which ranged from five to twelve years as of December 31, 2005. Servicing assets are evaluated for impairment based upon the fair value. Fair value is determined using prices for similar assets with similar characteristics, when available, or based upon discounted cash flows using market-based assumptions. Impairment is recognized through a valuation allowance.

Transfers of Financial Assets

Transfers of financial assets are accounted for as sales when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Foreclosed Real Estate

Real estate properties acquired through foreclosure or other proceedings are initially recorded at fair value upon foreclosure, establishing a new cost basis. After foreclosure, valuations are performed and the foreclosed property is adjusted to the lower of cost or fair market value of the properties, less costs to sell. Any write-down at the time of transfer to foreclosed properties is charged to the allowance for loan losses. Subsequent write-downs are charged to other expenses. Property is evaluated regularly to ensure that the recorded amount is supported by its current fair market value.

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation. Land is carried at cost. Additions and major replacements or betterments which extend the useful lives of premises and equipment are capitalized. Maintenance, repairs and minor improvements are expensed as incurred. Depreciation is computed principally by the straight-line method over estimated useful lives, except in the case of leasehold improvements, which are amortized over the term of the leases, if shorter. Useful lives range from five years for furniture and fixtures to ten to thirty years for leasehold improvements and buildings, respectively. Upon retirement or other disposition of the assets, the cost and the related accumulated depreciation are removed from the accounts and any gains or losses are reflected in income.

Federal Home Loan Bank Stock

As a requirement for membership, the banks invest in stock of the Federal Home Loan Bank of Atlanta (“FHLB”). This investment is carried at cost. Due to the redemption provisions of the

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1 - Significant Accounting Policies (Continued)

FHLB, the Company estimated that fair value equals cost and that this investment was not impaired.

Stock-Based Compensation

Statement of Financial Accounting Standards ("SFAS") No. 123, *Accounting for Stock-Based Compensation*, encourages all entities to adopt a fair value based method of accounting for employee stock compensation plans, whereby compensation cost is measured at the grant date based on the value of the award and is recognized over the service period, which is usually the vesting period. However, it also allows an entity to continue to measure compensation cost for those plans using the intrinsic value based method of accounting prescribed by Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees*, whereby compensation cost is the excess, if any, of the quoted market price of the stock at the grant date (or other measurement date) over the amount an employee must pay to acquire the stock. Stock options issued under the Company's stock option plans have no intrinsic value at the grant date and, under Opinion No. 25, no compensation cost is recognized for them. The Company uses the Black-Scholes option pricing model with the following assumptions to evaluate it's options: a risk-free interest rate of 3.5%, a dividend yield of 0%, an expected life equal to 70% of the term of the option, and a volatility rate of 14%. The Company has elected to continue with the accounting methodology in Opinion No. 25, and as a result, the following pro forma disclosures of net income and earnings per share and other disclosures as if the fair value based method of accounting had been applied are as follows:

(Dollars in thousands, except per share data)	2005	2004	2003
Net income as reported	$1,517	$ 253	$1,560
Deduct: Total stock-based employee compensation expense determined under fair value method for all awards, net of related tax effect	(136)	(77)	(90)
Net income pro forma	$1,381	$ 176	$1,470
Basic net income per common share			
As reported	$ 0.22	$0.04	0.22
Pro forma	0.20	0.02	0.21
Diluted net income per share			
As reported	0.21	0.03	0.21
Pro forma	0.19	0.02	0.20

Income Taxes

The Company and its subsidiaries file a consolidated Federal income tax return and separate North Carolina income tax returns. The provision for income taxes in the accompanying consolidated financial statements is provided on a liability method whereby deferred tax assets are recognized for deductible temporary differences and operating loss and tax credit carryforwards and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1 - Significant Accounting Policies (Continued)

Fair Value of Financial Instruments

SFAS No. 107, Disclosures About Fair Value of Financial Instruments, requires disclosure of fair value information about financial instruments, whether or not recognized in the consolidated balance sheets, for which it is practicable to estimate that value. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. In that regard, the derived fair value estimates cannot be substantiated by comparison to independent markets and, in many cases, could not be realized in immediate settlement of the instrument. Statement No. 107 excludes certain financial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented do not represent the underlying market value or liquidation value of the Company.

The following methods and assumptions were used by the Company in estimating the fair value of its financial instruments:

Carrying amounts approximate fair values for cash and due from banks; interest-bearing deposits with banks; federal funds sold; interest receivable and payable; variable rate loans that reprice frequently where no significant change in credit risk has occurred; bank owned life insurance; Federal Home Loan Bank stock; variable rate money market, demand, interest checking and savings accounts; variable rate time deposits; federal funds purchased and securities sold under repurchase agreements and short-term borrowed funds.

Quoted market prices, where available, or if not available, quoted market prices of comparable instruments are used for investment securities.

Discounted cash flows using interest rates currently being offered on instruments with similar terms and with similar credit quality are used for long-term debt; all loans (except variable rate loans described above) and fixed rate time deposits.

Comprehensive Income

The Company reports as comprehensive income all changes in shareholders' equity during the year from sources other than shareholders. Other comprehensive income refers to all components (revenues, expenses, gains, and losses) of comprehensive income that are excluded from net income. The Company's only component of other comprehensive income is unrealized gains and losses, net of income tax, on investment securities available for sale.

Earnings per Common Share

The Company issued 3% stock dividends in 2005, 2004 and 2003. All references in these consolidated financial statements to earnings per common share and weighted average common and common equivalent shares outstanding have been adjusted for the effect of these stock dividends. There were no anti-dilutive stock options outstanding during 2005, 2004 or 2003.

Basic earnings per share ("EPS") excludes dilution and is computed by dividing income available to common shareholders by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1 - Significant Accounting Policies (Continued)

stock or resulted in the issuance of common stock that then shared in the earnings of the entity. The computation of basic and dilutive earnings per share is summarized below:

	2005	2004	2003
Weighted average number of common shares used in computing basic net income per common share	7,031,322	7,147,074	7,158,342
Effect of dilutive stock options	171,370	167,333	133,996
Weighted average number of common shares and dilutive potential common shares used in computing diluted net income per common share	7,202,692	7,314,407	7,292,338

Recent Accounting Pronouncements

EITF 03-01

In November 2003, the Emerging Issues Task Force (“EITF”) issued EITF Issue No. 03-01, “The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments (“EITF 03- 01”). EITF 03-01 provided guidance for evaluating whether an investment is other-than-temporarily impaired and requires certain disclosures with respect to these investments. In September 2004, the Financial Accounting Standards Board (“FASB”) issued a FASB Staff Position (“FSP EITF 03-1-b”) to delay the requirement to record impairment losses under EITF 03-1. The guidance also included accounting considerations subsequent to the recognition of an other-than-temporary impairment and requirements for disclosures about unrealized losses that have not been recognized as other-than-temporary impairments. In November 2005, the FASB issued FSP FAS 115-1 and FAS 124-1, which addresses the determination as to when an investment is considered impaired. This FSP nullifies certain requirements of EITF 03-01 and supersedes EITF Topic No. D-44, “Recognition of Other-Than-Temporary Impairment upon the Planned Sale of a Security Whose Cost Exceeds Fair Value.” This FSP is to be applied to reporting periods beginning after December 15, 2005. The adoption of the FSP did not result in any other-than-temporary impairment.

FAS 123(R)

In December 2004, the FASB issued Statement of Financial Accounting Standards No. 123(R) (“SFAS No. 123(R)”), “Share-Based Payment”, which is a revision of FASB Statement No. 123 “Accounting for Stock-Based Compensation” and supersedes APB Opinion No. 25 “Accounting for Stock Issued to Employees”. SFAS No. 123(R) requires companies to recognize in the income statement the grant-date fair value of stock options and other equity-based compensation issued to employees over the period during which an employee is required to provide service in exchange for the award, which may be the shorter of the vesting period or the period the employee will be retirement eligible. SFAS No. 123(R) sets accounting requirements for “share-based” compensation to employees, including employee-stock purchase plans (“ESPPs”). Awards to most nonemployee directors will be accounted for as employee awards. Registrants must adopt SFAS No. 123(R) as of the beginning of their first annual period beginning after June 15, 2005. Accordingly, the Company will adopt SFAS No. 123(R) on January 1, 2006. If the cost of employee stock option compensation had been included in the

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1 - Significant Accounting Policies (Continued)

Company's consolidated financial statements, net income for the fiscal years ended December 31, 2005, 2004, and 2003 would have decreased by approximately $136,000, $77,000 and $90,000, respectively.

In March 2005, the SEC issued Staff Accounting Bulletin 107 ("SAB 107"), which contains guidance on applying the requirements in SFAS No. 123(R). SAB 107 provides guidance on valuation techniques, development of assumptions used in valuing employee share options and related MD&A disclosures. SAB 107 is effective for the period in which SFAS No. 123 (R) is adopted. The Corporation will adopt SAB 107 on January 1, 2006.

SFAS No. 123(R) and SAB 107 are expected to have a material effect on the Company's consolidated financial statements.

FAS 154

In May 2005, the FASB issued "SFAS No. 154", "Accounting Changes and Error Corrections", which replaces APB Opinion No. 20 "Accounting Changes" and FASB Statement No. 3 "Reporting Accounting Changes in Interim Financial Statements". SFAS No. 154 changes the requirements for the accounting and reporting of a change in an accounting principle. SFAS No. 154 requires retrospective application for voluntary changes in an accounting principle unless it is impracticable to do so. SFAS No. 154 is effective for accounting changes made in fiscal years beginning after December 15, 2005. The Company will adopt SFAS No. 154 on January 1, 2006 with no expected material effect on its consolidated financial statements.

Reclassification

Certain amounts in the 2004 and 2003 financial statements have been reclassified to conform to the 2005 presentation. The reclassifications had no effect on net income or shareholders' equity as previously reported.

Note 2 - Investment Securities

Carrying amounts and fair values of securities available for sale are summarized below:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2005				
U.S. Treasury	$ 2,988,145	$ —	$ 86,583	$ 2,901,562
U.S. Government agencies	9,850,306	72,244	184,462	9,738,088
Mortgage-backed securities and CMO's	5,772,431	38,111	26,321	5,784,221
State and political subdivisions	12,855,765	734,560	33,973	13,556,352
Commercial paper	2,479,513	—	—	2,479,513
Corporate bonds	527,340	9,278	—	536,618
Total debt securities	34,473,500	854,193	331,339	34,996,354
Equity securities	8,125	11,399	—	19,524
Total securities available for sale	$34,481,625	$865,592	$331,339	$35,015,878

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 2 - Investment Securities (Continued)

December 31,2004	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury	$ 2,983,899	$ —	$ 17,649	$ 2,966,250
U.S. Government agencies	8,926,220	160,825	50,354	9,036,691
Mortgage-backed securities and CMO's	2,884,438	94,775	—	2,979,213
State and political subdivisions	11,901,185	1,081,141	—	12,982,326
Corporate bonds	540,749	—	9,892	530,857
Total debt securities	27,236,491	1,336,741	77,895	28,495,337
Equity securities	8,125	20,407	—	28,532
Total securities available for sale	$27,244,616	$1,357,148	$ 77,895	$28,523,869

Results from sales of securities available for sale for the years ended December 31, 2005, 2004 and 2003 are as follows:

	2005	2004	2003
Gross proceeds from sales	$1,295,239	$262,625	$2,796,731
Realized gains from sales	$ 3,960	$ 2,373	$ 128,845
Realized losses from sales	(20,232)	—	—
Net realized gains (losses)	$ (16,272)	$ 2,373	$ 128,845

At December 31, 2005, 2004 and 2003 securities available for sale with a carrying amount of $13,052,369, $12,757,021 and $11,609,413, respectively, were pledged as collateral on public deposits and for other purposes as required or permitted by law.

The following tables show the gross unrealized losses and fair value of investments, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2005 and 2004. These unrealized losses on investment securities are a result of volatility in the market during 2005 and 2004. At December 31, 2005 the unrealized losses were related to three U.S. Treasuries, eight U.S. Government agencies, four mortgage backed securities and CMOs, and six state and political subdivisions. All unrealized losses on investment securities are considered by management to be temporary given the credit ratings on these investment securities.

	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
December 31, 2005						
Securities available for sale:						
U.S. Treasury	$ —	$ —	$2,901,562	86,583	$ 2,901,562	$ 86,583
U.S. Gov't agencies	2,496,562	35,975	4,841,250	148,487	7,337,812	184,462
Mortgage-backed securities and CMO's	4,034,069	26,321	—	—	4,034,069	26,321
State and political subdivisions	1,445,291	33,973	—	—	1,445,291	33,973
Corporate bonds	—	—	—	—	—	—
	$7,975,922	$ 96,269	$7,742,812	$235,070	$15,718,734	$331,339
December 31, 2004						
Securities available for sale:						
U.S. Treasury	$2,966,250	$ 17,649	$ —	—	$ 2,966,250	17,649
Mortgage-backed securities and CMO's	3,941,252	17,810	1,001,250	32,544	4,942,502	50,354
Corporate bonds	530,857	9,892	—	—	530,857	9,892
	$7,438,359	$ 45,351	$1,001,250	$ 32,544	$ 8,439,609	$ 77,895

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 3 - Loans

The composition of net loans as of December 31, 2005 and 2004 is as follows:

	2005	2004
Commercial	$ 37,298,798	$ 37,717,487
Real estate - construction	21,206,369	25,479,828
Real estate – residential	116,715,341	102,626,549
Real estate - commercial	83,860,836	81,283,050
Consumer	13,478,425	13,488,205
Loans held for sale	3,353,455	2,903,421
Other	72,438	90,347
	275,985,662	263,588,887
Less:		
Allowance for loan losses	(4,482,304)	(4,982,891)
Deferred loan fees, net	210,213	149,385
Loans, net	$271,713,571	$258,755,381

Although the subsidiary banks' loan portfolios are diversified, there is a concentration of mortgage real estate loans, primarily one to four family residential mortgage loans, which represent 42.96% of net loans. Additionally, there is concentration in commercial loans secured primarily by real estate, to finance manufacturing buildings, shopping center locations, commercial land development, commercial buildings and equipment that comprise 30.86% of net loans. There is not a concentration of a particular type of credit in this group of commercial loans.

An analysis of fixed-rate loan maturities and repricing frequencies of variable-rate loans as of December 31, 2005 and 2004 follows:

	2005	2004
Fixed-rate loans with a maturity of:		
Three months or less	$ 1,689,708	$ 2,004,205
Over three months through twelve months	4,947,178	1,988,301
Over one year through five years	45,391,368	31,238,637
Over five years	36,900,837	22,247,129
Total fixed-rate loans	88,929,091	57,478,272
Variable-rate loans with a repricing frequency of:		
Three months or less	$186,448,694	$205,397,621
Over three months through twelve months	818,090	862,379
Over one year through five years	—	—
Over five years	—	—
Total variable-rate loans	187,266,784	206,260,000
Total loans	$276,195,875	$263,738,272

Impaired loans, which consisted of nonaccrual loans and loans identified by management as impaired, totaled $3,605,085 and $3,376,270 at December 31, 2005 and 2004, respectively. The nonaccrual status of these loans had the effect of reducing net income by $106,670 in 2005 and $109,678 in 2004. Of the nonaccrual amount in 2005 and 2004, a total of $36,628 and $48,940, respectively, was government guaranteed as to principal. The allowance for impaired loans, amounted to $1.6 million and $1.9 million at December 31, 2005 and 2004, respectively. At December 31, 2005 and 2004, loans past due 90 days and still accruing interest totaled $338,724 and $1,150,188, respectively. Restructured loans, excluding those included in nonperforming loans, amounted to $3.3 million at December 31, 2005. The carrying value of

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 3 – Loans (Continued)

foreclosed properties held as other real estate was $169,466 and $481,000 at December 31, 2005 and 2004, respectively.

The Company's loan policies are written to address loan-to-value ratios and collateralization methods with respect to each lending category. Consideration is given to the economic and credit risk of lending areas and customers associated with each category.

Note 4 - Allowance for Loan Losses

Changes in the allowance for loan losses for the years ended December 31, 2005, 2004 and 2003 are presented below:

	2005	2004	2003
Balance, beginning of the year	$ 4,982,891	$3,223,952	$2,755,302
Charge-offs	(1,378,164)	(373,534)	(150,097)
Recoveries	122,577	40,973	25,747
Provision charged against income	755,000	2,091,500	593,000
Balance, end of year	$ 4,482,304	$4,982,891	$3,223,952

Note 5 - Servicing

Loans serviced for others are not included in the accompanying consolidated balance sheets. The unpaid principal balances of mortgage and other loans serviced for others were approximately $167,000,000 and $164,000,000 at December 31, 2005 and 2004, respectively. The carrying value of capitalized servicing rights, net of valuation allowances, is included in other assets. A summary of mortgage servicing rights follows:

	2005	2004	2003
Mortgage servicing rights, beginning of the year	$1,236,396	$1,233,469	$1,386,619
Amounts capitalized	291,619	374,226	742,515
Amortization expenses	389,548	371,299	695,665
Impairment change	—	—	200,000
End of year, net	$1,138,467	$1,236,396	$1,233,469

Amortization expense for each of the next five years is estimated to be as follows:

Year ending December 31,	
2006	$269,000
2007	233,000
2008	197,000
2009	161,000
2010	124,000
Total	$984,000

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 6 - Premises and Equipment

The major classes of premises and equipment and the total accumulated depreciation at December 31, 2005 and 2004 are listed below:

	2005	2004
Land	$ 2,280,199	$ 1,980,199
Building and improvements	6,220,068	6,040,611
Furniture and equipment	4,609,127	4,613,384
	13,109,394	12,634,194
Less accumulated depreciation	4,677,098	4,316,697
	$ 8,432,296	$ 8,317,497

Note 7 - Deposits

The composition of deposits at December 31, 2005 and 2004 is as follows:

	2005		2004	
	Amount	Percentage of Total	Amount	Percentage of Total
Demand deposits	$ 47,279,515	17%	$ 36,866,146	15%
Interest checking and money market	83,679,745	31%	80,393,133	33%
Savings	36,689,516	13%	39,852,601	16%
Time deposits $100,000 and over	38,881,451	14%	36,966,834	15%
Other time deposits	67,445,605	25%	52,860,046	21%
	$273,975,832	100%	$246,938,760	100%

The maturities of fixed-rate time deposits at December 31, 2005 are reflected in the table below.

Year ending December 31,	Time Deposits $100,000 and Over	Other Time Deposits
2006	$27,444,226	$43,001,699
2007	9,005,670	16,544,991
2008	2,272,369	5,886,713
2009	159,186	793,858
2010	—	1,164,517
Thereafter	—	53,827
Total	$38,881,451	$67,445,605

Note 8 - Short-Term Borrowed Funds

The following tables set forth certain information regarding the amounts, year-end weighted average rates, average balances, weighted average rate, and maximum month-end balances for short-term borrowed funds, at and during 2005 and 2004.

	2005		2004	
At year-end	Amount	Rate	Amount	Rate
Securities sold under repurchase agreements	$3,449,044	3.84%	$ 3,531,414	1.00%
Master notes	4,454,584	3.60%	5,030,978	1.03%
Short-term advances from FHLB	—	0.00%	2,500,000	2.51%
	$7,903,628	3.70%	$11,062,392	1.35%

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 8 – Short-Term Borrowed Funds (Continued)

	2005		2004	
	Amount	Rate	Amount	Rate
Average for the year				
Federal funds purchased	$ 231,370	3.33%	$ 593,219	1.42%
Securities sold under repurchase agreements	2,919,815	2.50%	2,951,542	1.18%
Master notes	5,008,272	2.92%	4,442,875	1.10%
Short-term advances from FHLB	405,479	2.84%	5,480,274	1.53%
	$8,564,936	2.78%	$13,467,910	1.30%

	2005	2004
Maximum month-end balance		
Federal Funds purchased	$2,500,000	$3,650,000
Securities sold under repurchase agreements	3,872,347	4,139,837
Master notes	8,135,263	6,080,604
Short-term advances from FHLB	2,000,000	8,500,000

Federal funds purchased represent unsecured overnight borrowings from other financial institutions. Securities sold under repurchase agreements represent short-term borrowings collateralized by securities of the United States government or its agencies.

The subsidiary banks have combined available lines of credit for federal funds in the amount of $20,150,000 at December 31, 2005.

Note 9 - Long-Term Debt

The Company has a line of credit with the Federal Home Loan Bank secured by qualifying first lien and second mortgage loans and commercial real estate loans with eligible collateral value of $71,017,000 at December 31, 2005. The long-term advances under this line amounted to $31,436,500 and $34,661,350 at December 31, 2005 and 2004, respectively. Interest rates ranged from 2.64% to 7.52% for both 2005 and 2004. One subsidiary bank also has standby letters of credit issued by the Federal Home Loan Bank to be used as collateral for public funds deposits. The amount of the letters of credit was $13,000,000 at December 31, 2005.

On April 30, 2001, the Company borrowed $4,000,000 from a bank at an interest rate of prime less one percent. The note is payable in annual installments of $400,000. The balance outstanding at December 31, 2005 and 2004 was $2,400,000 and $2,800,000, respectively.

The Company issued $5,155,000 of junior subordinated debentures to Uwharrie Statutory Trust 1 in exchange for the proceeds of the trust preferred securities issued by the Trust. The junior subordinated debentures are included in long term debt and the Company’s equity interest in the trust is included in other assets. The junior subordinated debentures pay interest quarterly at an annual rate, reset quarterly, equal to LIBOR plus 3.40%. The debentures are redeemable on September 26, 2007 or afterwards, in whole or in part, on March 26, June 26, September 26 or December 26 of each subsequent year through maturity at September 26, 2032. The Company fully and unconditionally guarantees the trust preferred securities through the combined operation of the junior subordinated debentures and other related documents. The Company’s obligation under the guarantee is unsecured and subordinate to senior and subordinated indebtedness of the Company.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 9 - Long-Term Debt (Continued)

The trust preferred securities presently qualify as Tier 1 regulatory capital and are reported in Federal Reserve regulatory reports as a minority interest in a consolidated subsidiary. The junior subordinated debentures do not qualify as Tier 1 regulatory capital. On March 1, 2005, the Board of Governors of the Federal Reserve adopted a final rule that allows the continued limited inclusion of trust preferred securities in Tier 1 capital. The final rule limits trust preferred securities to 25 percent of all core capital elements, net of goodwill. Amounts of restricted core capital elements in excess of these limits generally may be included in Tier 2 capital. The final rule provides a five-year transition period, ending March 31, 2009, for application of the quantitative limits.

On November 19, 2002, the Company executed a mortgage in the amount of $129,000 for the purchase of property for branch expansion. This loan bears interest at 6.00% and is to be paid in 60 quarterly installments of $3,277. The outstanding principal balance on this note was $111,525 at December 31, 2005.

As of December 31, 2005, the scheduled maturities of these advances (FHLB advances are reflected to the first convertible date or maturity date, as applicable), junior subordinated debentures, and notes payable are as follows:

Year ending December 31,	
2006	$ 7,406,561
2007	4,406,964
2008	12,843,875
2009	1,407,844
2010	2,408,325
Thereafter	10,629,456
Total	$39,103,025

Note 10 - Income Tax Matters

The significant components of income tax expense for the years ended December 31 are summarized as follows:

	2005	2004	2003
Current tax expense:			
Federal	$379,180	$ 122,670	$ 619,899
State	92,390	149,830	135,062
Total	471,570	272,500	754,961
Deferred tax expense (benefit):			
Federal	38,496	(391,945)	(183,485)
State	13,504	(80,055)	(39,996)
Total	52,000	(472,000)	(223,481)
Net provision (benefit) for income taxes	$523,570	$(199,500)	$ 531,480

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 10 - Income Tax Matters (Continued)

The difference between the provision for income taxes and the amounts computed by applying the statutory federal income tax rate of 34% to income before income taxes is summarized below:

	2005	2004	2003
Tax computed at the statutory federal rate	$ 693,655	$ 18,303	$ 711,042
Increases (decrease) resulting from:			
Tax exempt interest, net	(223,831)	(290,293)	(300,260)
State income taxes, net of federal benefit	69,890	101,400	95,154
Other	(16,144)	(28,910)	25,544
Provision (benefit) for income taxes	$ 523,570	$(199,500)	$ 531,480

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of deferred taxes at December 31, are as follows:

	2005	2004
Deferred tax assets relating to:		
Allowance for loan losses	$1,496,000	$ 1,740,000
Deferred compensation	279,000	233,000
Other	130,000	33,000
Valuation allowance	(8,000)	(6,000)
Total deferred tax assets	$1,897,000	$ 2,000,000
Deferred tax liabilities relating to:		
Net unrealized gain on securities available for sale	$ (205,976)	$ (493,203)
Property and equipment	(392,000)	(460,000)
Deferred loans fees and costs	(218,000)	(206,000)
Loan servicing	(60,000)	(70,000)
Prepaid expenses	(79,000)	(64,000)
Total deferred tax assets	(954,976)	(1,293,203)
Net recorded deferred tax asset	$ 942,024	$ 706,797

The net deferred tax asset is included in other assets on the accompanying consolidated balance sheets.

Note 11 - Commitments and Contingencies

Financial Instruments with Off-Balance-Sheet Risk

The subsidiary banks are parties to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of their customers. These financial instruments include commitments to extend credit, lines of credit and standby letters of credit. These instruments involve elements of credit risk in excess of amounts recognized in the accompanying financial statements.

The subsidiary banks' risks of loss with the unfunded loans and lines of credit or standby letters of credit are represented by the contractual amount of these instruments. The banks use the same credit policies in making commitments under such instruments as they do for on-balance sheet instruments. The amount of collateral obtained, if any, is based on management's credit evaluation of the borrower. Collateral held varies, but may include accounts receivable,

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 11 - Commitments and Contingencies (Continued)

inventory, real estate and time deposits with financial institutions. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Credit card commitments are unsecured. As of December 31, 2005 and 2004, outstanding financial instruments whose contract amounts represent credit risk were as follows:

	2005	2004
Commitments to extend credit	$61,579,076	$54,931,021
Credit card commitments	7,442,862	6,881,520
Standby letters of credit	463,100	500,000
	$69,485,038	$62,312,541

Contingencies

In the normal course of business, the Company is involved in various legal proceedings. In the opinion of management, any liability resulting from such proceedings would not have a material adverse effect on the consolidated financial statements.

Financial Instruments with Concentration of Credit Risk

The bank subsidiaries make commercial, agricultural, real estate mortgage, home equity and consumer loans primarily in Stanly, Anson and Cabarrus counties. A substantial portion of the Company's customers' ability to honor their contracts is dependent on the economy in these counties.

Although the Company's composition of loans is diversified, there is some concentration of mortgage loans in the total portfolio. The Bank Policy is to abide by real estate loan-to-value margin limits corresponding to guidelines issued by the Federal supervisory agencies on March 19,1993. Lending policy for all loans requires that they be supported by sufficient cash flows. Credit losses related to this real estate concentration are consistent with credit losses experienced in the portfolio as a whole.

Note 12 - Related Party Transactions

The Company has granted loans to certain directors and executive officers and their related interests. Such loans are made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other borrowers and, in management's opinion, do not involve more than the normal risk of collectibility. All loans to directors and executive officers or their interests are submitted to the Board of Directors for approval. A summary of loans to directors, executive officers and their related interests follows:

Balance at December 31, 2004	$17,114,452
Disbursements during the year	6,865,917
Collections during the year	8,357,417
Balance at December 31, 2005	$15,622,952

At December 31, 2005, the Company had approved but unused lines of credit totaling $4.3 million to executive officers, directors, officer and their related interests.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 13 - Regulatory Matters

The Company, and its bank subsidiaries, are subject to certain requirements imposed by state and federal banking statutes and regulations. These requirements, among other things, establish minimum levels of capital, restrict the amount of dividends that may be distributed, and require that reserves on deposit liabilities be maintained in the form of vault cash or noninterest-bearing deposits with the Federal Reserve Bank.

The Company and its subsidiary banks are subject to federal regulatory risk-based capital guidelines for banks and bank holding companies. Each must meet specific capital guidelines that involve quantitative measure of assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices which measure Total and Tier 1 Capital to risk-weighted assets and Tier 1 Capital to average assets. Quantitative measures established by regulation to ensure capital adequacy and the Company's consolidated capital ratios are set forth in the table below. The Company expects to meet or exceed these minimums without altering current operations or strategy.

	Actual		Minimum For Capital Requirement		Minimum to Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(Dollars in thousands)			
December 31, 2005:						
Total Capital to risk Weighted Assets:						
Consolidated	$34,538	12.8%	$21,650	8.00%	$ 27,062	10.00%
Bank of Stanly	23,284	12.2%	15,243	8.00%	19,054	10.00%
Anson Bank and Trust	4,246	15.7%	2,170	8.00%	2,712	10.00%
Cabarrus Bank and Trust	6,790	13.2%	4,120	8.00%	5,150	10.00%
Tier I Capital to Risk Weighted Assets:						
Consolidated	31,137	11.5%	10,825	4.00%	16,237	6.00%
Bank of Stanly	20,887	11.0%	7,622	4.00%	11,432	6.00%
Anson Bank and Trust	3,908	14.4%	1,085	4.00%	1,627	6.00%
Cabarrus Bank and Trust	6,143	11.9%	2,060	4.00%	3,090	6.00%
Tier I Capital to Average Assets:						
Consolidated	31,137	9.0%	13,784	4.00%	17,230	5.00%
Bank of Stanly	20,887	8.5%	9,826	4.00%	12,282	5.00%
Anson Bank and Trust	3,908	10.4%	1,513	4.00%	1,904	5.00%
Cabarrus Bank and Trust	6,143	9.6%	2,553	4.00%	3,191	5.00%

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 13 - Regulatory Matters (Continued)

	Actual		Minimum For Capital Requirement		Minimum to Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(Dollars in thousands)			
December 31, 2004						
Total Capital to risk Weighted Assets:						
Consolidated	$33,667	12.9%	$20,826	8.00%	$ 26,032	10.00%
Bank of Stanly	22,631	12.1%	14,997	8.00%	18,747	10.00%
Anson Bank and Trust	4,094	16.8%	1,950	8.00%	2,438	10.00%
Cabarrus Bank and Trust	6,586	14.1%	3,751	8.00%	4,689	10.00%
Tier I Capital to Risk Weighted Assets:						
Consolidated	30,383	11.7%	10,413	4.00%	15,619	6.00%
Bank of Stanly	20,262	10.8%	7,499	4.00%	11,248	6.00%
Anson Bank and Trust	3,788	15.5%	975	4.00%	1,463	6.00%
Cabarrus Bank and Trust	5,996	12.8%	1,876	4.00%	2,813	6.00%
Tier I Capital to Average Assets:						
Consolidated	30,383	9.2%	13,125	4.00%	16,406	5.00%
Bank of Stanly	20,262	8.5%	9,478	4.00%	11,848	5.00%
Anson Bank and Trust	3,788	10.5%	1,410	4.00%	1,762	5.00%
Cabarrus Bank and Trust	5,996	10.8%	2,219	4.00%	2,774	5.00%

As of December 31, 2005, the most recent notification from the Federal Deposit Insurance Corporation categorized all subsidiary banks as being well capitalized under the regulatory framework for prompt corrective action. There have been no conditions or events since such notification that management believes would have changed the categorizations.

For the reserve maintenance period in effect at December 31, 2005, the subsidiary banks were required to maintain reserve balances in cash or on deposit with the Federal Reserve Bank in the aggregate amount of $3,645,000 as reserves on deposit liabilities.

Note 14 - Stock Matters

Employee Stock Plans

During 1996, the Company adopted the 1996 Employment Stock Option Plan (“SOP”) and the Employee Stock Purchase Plan (“SPP”), under which options to purchase shares of the Company’s common stock may be granted to officers and eligible employees. Options granted under the SOP are exercisable in established increments according to vesting schedules, generally three to five years, and will expire if not exercised within ten years of the date of grant. Options granted under the SPP are fully vested at the date of grant and expire if not exercised within two years of the grant date.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 14 - Stock Matters (Continued)

Activity under all option plans, reflecting the effects of the 3% stock dividends issued in 2005, 2004 and 2003, are as follows:

	2005		2004		2003	
	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
Options outstanding at the beginning of the year	681,911	$ 4.48	758,729	$ 4.34	793,320	$ 4.26
Options granted	84,651	5.60	73,333	5.84	32,961	4.35
Options exercised	(71,227)	4.74	(128,600)	3.45	(42,498)	3.07
Forfeitures	(32,079)	4.88	(21,551)	4.35	(25,054)	3.66
Options outstanding at the end of the year	663,256	$ 4.58	681,911	$ 4.48	758,729	$ 4.34
Options exercisable at the end of the year	509,751	$ 4.27	493,538	$ 4.04	576,785	$ 4.17

At December 31, 2005, options outstanding had a weighted-average remaining term of 4.5 years. Total options outstanding at December 31, 2005 included 104,583 options exercisable at a range of $2.26 to $2.90 per share, and 558,673 options exercisable at a range of $4.57 to $6.02 per share. Exercisable options at December 31, 2004 included 104,583 options exercisable at a range of $2.26 to $2.90 per share, and 405,168 of $4.57 to $5.84 per share. No expense has been recognized in connection with the grant or exercise of these options. At December 31, 2005, authorized shares of common stock reserved for future grants of options totaled 153,132 under the SOP and 94,474 under the SPP.

Stock Offering

The Company completed the sale of 1,047,497 shares of its common stock at $5.50 per share on April 15, 2003. Expenses associated with the sale amounted to $403,666 resulting in net proceeds from the offering of $1,885,848 in 2003 for 361,730 shares and $389,767 in 2002 for 685,767 shares.

Stock Repurchase Program

On February 21, 1995, the Company's Board of Directors authorized and approved a Stock Repurchase Program, to be reaffirmed annually, pursuant to which the Company may repurchase shares of the Company's common stock for the primary purpose of providing liquidity to its shareholders. Pursuant to stock repurchase authorizations and limitations, the Company purchased 197,026 shares during 2005 and 245,658 shares during 2004 at an aggregate purchase price of $1,214,461 and $1,491,876, respectively.

Note 15 - Employee and Director Benefit Plans

Employees' Savings Plus and Profit Sharing Plan

The Company has established an associate tax deferred savings plan under Section 401(k) of the Internal Revenue Code of 1986. All associates who are scheduled to work 500 hours or more are eligible to participate upon completion of six months of employment.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 15 - Employee and Director Benefit Plans (Continued)

The Company's annual contribution to the plan was $143,210 in 2005, $129,918 in 2004 and $131,155 in 2003, determined as follows:

- A matching contribution equivalent to 50% of the first 6% of each associate's compensation contributed to the plan.
- A discretionary contribution, subject to approval by the Board of Directors, limited to an amount not to exceed the maximum amount deductible for income tax purposes.

Directors' Deferred Compensation Plan

On March 1, 1994, the Company established a Directors' Deferred Compensation Plan in accordance with the laws of the State of North Carolina under which each Director could elect to defer receipt for services rendered to the Company as a Director during the term of his or her service by entering into a written deferred compensation election. This plan was closed to new participants in 2001; subsequently, only two directors continue to defer receipt of fees. The balance in deferred directors' compensation, not yet disbursed, was $215,546, $234,692 and $219,033 at December 31, 2005, 2004 and 2003, respectively. Expense for the years then ended was $13,931, $13,501 and $14,478, respectively.

Employee Stock Ownership Plan

The Company established an Employee Stock Ownership Plan ("ESOP") to benefit all qualified employees. The ESOP purchased 268,335 dividend adjusted shares of common stock in 1999 with proceeds received from a loan of $1,200,000 from the Company. The loan is to be repaid over eighteen years with interest at 8%. The loan may be prepaid without penalty. The unallocated shares of stock held by the ESOP are pledged as collateral for the loan. The ESOP is funded by contributions made by the Company and its subsidiaries in amounts sufficient to retire the debt. At December 31, 2005, the outstanding balance of the loan is $914,088 and is presented as a reduction of shareholders' equity.

Shares released as the debt is repaid and earnings from the common stock held by the ESOP are allocated among active participants on the basis of compensation in the year of allocation. Benefits vest 100% as they are allocated to participants. Dividends on unallocated shares may be used by the ESOP to repay the loan to the Company and are not reported as dividends in the financial statements. Dividends on allocated or committed to be allocated shares are credited to the accounts of the participants and reported as dividends in the consolidated financial statements.

Expenses of $251,437, $245,420 and $223,078 during the years ended December 31, 2005, 2004 and 2003, respectively, have been incurred in connection with the ESOP. At December 31, 2005, 115,660 shares held by the ESOP have been released or committed to be released to the ESOP's participants for purposes of computing earnings per share. The fair value of the unallocated shares amounted to approximately $1.0 million at December 31, 2005.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 15 - Employee and Director Benefit Plans (Continued)

Supplemental Executive Retirement Plan

The Company has implemented a non-qualifying deferred compensation plan for certain executive officers. The Company has purchased life insurance policies in order to provide future funding of benefit payments. Certain of the plan benefits will accrue and vest during the period of employment, and will be paid in fixed monthly benefit payments from ten to fifteen years commencing with the officer's retirement at any time after attainment of the age specified in the officer's plan agreement. Other benefits will accrue based upon the performance of the underlying life insurance policies both during employment and after retirement. Such benefits will continue to accrue and be paid throughout the participant's life assuming satisfactory performance of the funding life insurance policy. The plan also provides for payment of death benefits and for payment of disability benefits in the event the officer becomes permanently disabled prior to attainment of retirement age. During 2005, 2004 and 2003 a provision of $137,688, $92,613 and $192,376, respectively, was expensed for future benefits to be provided under this plan. The liability accrued for compensation deferred under the plan amounts to $508,236, and $370,548 at December 31, 2005 and 2004, respectively.

Split-Dollar life Insurance

The Company has entered into Life Insurance Endorsement Method Split Dollar Agreements with certain officers. Under these agreements, upon death of the officer, the Company first recovers the cash surrender value of the contract and then shares the remaining death benefits from insurance contracts, which are written with different carriers, with the designated beneficiaries of the officers. The death benefit to the officers' beneficiaries is a multiple of base salary at the time of the agreements. The Company, as owner of the policies, retains an interest in the life insurance proceeds and a 100% interest in the cash surrender value of the policies.

Note 16 - Fair Values of Financial Instruments and Interest Rate Risk

The estimated fair values disclosed in the following table do not represent market values of all assets and liabilities of the Company and should not be interpreted to represent the underlying value of the Company. The following table reflects a comparison of carrying amounts and the estimated fair value of the financial instruments as of December 31.

	2005		2004	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial Assets				
Cash and cash equivalents	$ 21,368	$ 21,368	$ 19,575	$ 19,575
Securities available for sale	35,016	35,016	28,524	28,524
Loans, net of unearned income and allowance for loan losses	268,360	268,121	255,852	259,371
Loans held for sale	3,354	3,354	2,903	2,903
Other Financial assets	8,546	8,546	8,014	8,014
Financial Liabilities				
Deposits	$273,976	$274,208	$246,939	$247,549
Short-term borrowings	7,904	7,904	11,062	11,062
Long-term debt	39,103	38,815	42,734	43,102
Other financial liabilities	369	369	302	302

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 16 - Fair Values of Financial Instruments and Interest Rate Risk (Continued)

At December 31, 2005, the subsidiary banks had outstanding standby letters of credit and commitments to extend credit. These off-balance sheet financial instruments are generally exercisable at the market rate prevailing at the date the underlying transaction will be completed; therefore, they were deemed to have no current fair value. See Note 11.

Interest Rate Risk

The Company assumes interest rate risk (the risk that general interest rate levels will change) in the course of its normal operations. As a result, fair values of the Company's financial instruments will change when interest rate levels change and that change may be either favorable or unfavorable to the Company. Management attempts to match maturities of assets and liabilities to the extent believed necessary to minimize interest rate risk. However, borrowers with fixed rate obligations are more likely to prepay in a falling rate environment and less likely to prepay in a rising rate environment. Conversely, depositors who are receiving fixed rates are more likely to withdraw funds before maturity in a rising rate environment and less likely to do so in a falling rate environment. Management monitors rates and maturities of assets and liabilities and attempts to minimize interest rate risk by adjusting terms of new loans and deposits and by investing in securities with terms that mitigate the Company's overall interest rate risk.

Note 17 - Parent Company Financial Data

The following is a summary of the condensed financial statements of Uwharrie Capital Corp:

Condensed Balance Sheets

	December 31,	
	2005	**2004**
Assets		
Cash and demand deposits with bank subsidiaries	$ 336,944	$ 279,525
Interest-earning deposits with bank subsidiaries	4,756,097	5,941,650
Investments in:		
Bank subsidiaries	32,252,525	31,819,132
Nonbank subsidiaries	546,822	516,205
Other assets	1,764,277	2,205,064
Total assets	$39,656,665	$40,761,576
Liabilities and shareholders' equity		
Master notes	$ 4,454,584	$ 5,030,978
Long-term debt	2,400,000	2,800,000
Junior subordinated debentures	5,155,000	5,155,000
Other liabilities	194,305	619,799
Shareholders' equity	27,452,776	27,155,799
Total liabilities and shareholders' equity	$39,656,665	$40,761,576

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 17 - Parent Company Financial Data (Continued)

Condensed Statement of Operations

	2005	2004	2003
Equity in earnings of subsidiaries	$ 921,782	$ 83,989	$1,108,392
Interest income	175,288	101,272	164,217
Dividend income	1,000,000	800,000	800,000
Management and service fees	3,796,651	1,900,000	1,435,000
Other income	107,252	148,534	123,780
Interest expense	625,489	401,088	382,761
Other operating expense	4,029,873	2,649,676	1,850,789
Income tax benefit	(170,980)	(270,300)	(161,980)
Net income	$1,516,591	$ 253,331	$1,559,819

Effective January 1, 2005 support operations staff moved to the holding company, which had the effect of increasing operating expense and increased allocation of service fees to the subsidiary banks.

Condensed Statements of Cash Flows

	2005	2004	2003
Cash flows from operating activities			
Net income	$ 1,516,591	$ 253,331	$ 1,559,819
Adjustments to reconcile net income to net cash Provided (used) by operating activities:			
Equity in earnings of subsidiaries	(1,921,782)	(883,989)	(1,908,392)
(Increase) decrease in other assets	554,955	230,573	(554,026)
Increase (decrease) in other liabilities	(425,494)	505,444	(48,629)
Net cash provided (used) by operating activities	(275,730)	105,359	(951,228)
Cash flows from investing activities			
Dividends received from subsidiaries	1,000,000	800,000	800,000
Investment in subsidiaries	0	(100)	(7,000,000)
Net cash provided (used) by investing activities	1,000,000	799,900	(6,200,000)
Cash flows from financing activities			
Net increase (decrease in master notes	(576,394)	982,792	(345,713)
Net increase (decrease) in long-term debt	(400,000)	(400,000)	(400,000)
Proceeds from issuance of common stock	347,227	571,247	2,016,177
Repurchase of common stock	(1,214,461)	(1,491,875)	(675,662)
Cash paid for fractional shares	(8,776)	(10,683)	(7,845)
Other, net	—	(95,940)	71,526
Net cash provided (used) by financing activities	(1,852,404)	(444,459)	658,483
Net increase (decrease) in cash and cash equivalents	(1,128,134)	460,800	(6,492,745)
Cash and cash equivalents at beginning of period	6,221,175	5,760,375	12,253,120
Cash and cash equivalents at end of period	$ 5,093,041	$ 6,221,175	$ 5,760,375

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 18 - Quarterly Financial Data

	First	Second	Third	Fourth
	(in thousands, except per share data)			
2005				
Interest income	$ 4,408	$ 4,594	$ 4,886	$ 5,273
Interest expense	(1,359)	(1,500)	(1,730)	(2,041)
Net interest income	3,049	3,094	3,156	3,232
Provision for loan losses	(215)	(145)	(210)	(185)
Net interest income after provision for loan losses	2,834	2,949	2,946	3,047
Noninterest income	1,047	1,048	1,121	1,135
Noninterest expense	(3,425)	(3,525)	(3,584)	(3,553)
Income before taxes	456	472	483	629
Income taxes	116	113	132	162
Net income	$ 340	$ 359	$ 351	$ 467
Net income per common share				
Basic	$ 0.05	$ 0.05	$ 0.05	$ 0.07
Diluted	$ 0.05	$ 0.05	$ 0.05	$ 0.06

	First	Second	Third	Fourth
	(in thousands, except per share data)			
2004				
Interest income	$ 3,684	$ 3,824	$ 4,129	$ 4,269
Interest expense	(1,115)	(1,109)	(1,210)	(1,300)
Net interest income	2,569	2,715	2,919	2,969
Provision for loan losses	(149)	(252)	(325)	(1,366)
Net interest income after provision for loan losses	2,420	2,463	2,594	1,603
Noninterest income	1,256	901	1,067	1,047
Noninterest expense	(3,144)	(3,123)	(3,364)	(3,666)
Income before taxes	532	241	297	(1,016)
Income taxes (benefit)	122	47	72	(440)
Net income(loss)	$ 410	$ 194	$ 225	$ (576)
Net income(loss) per common share				
Basic	$ 0.06	$ 0.03	$ 0.03	$ (0.08)
Diluted	$ 0.05	$ 0.03	$ 0.03	$ (0.08)

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Selected Financial Data

Selected Financial Data
In Thousands Except Per Share and Shares Outstanding Information

	2005	2004	2003	2002	2001
Summary of Operations					
Interest income	$ 19,161	$ 15,906	$ 14,597	$ 14,649	$ 17,002
Interest expense	6,630	4,734	4,606	5,289	8,012
Net interest income	12,531	11,172	9,991	9,360	8,990
Provision for loan losses	755	2,092	593	835	1,179
Noninterest income	4,351	4,271	5,159	4,406	3,470
Noninterest expense	14,087	13,297	12,466	10,586	8,905
Income taxes	523	(199)	531	587	671
Net income	$ 1,517	$ 253	$ 1,560	$ 1,758	$ 1,705
Per Common Share					
Net income – basic (1)	$ .22	$ .04	$ .22	$ .28	$ .27
Net income – diluted (1)	.21	.03	.21	.27	.26
Book value (1)	3.85	3.74	3.76	3.54	3.11
Weighted Average Shares					
Outstanding:					
Basic (1)	7,031,322	7.147,074	7,158,342	6,374,602	6,396,403
Diluted (1)	7,202,692	7,314,407	7,292,338	6,482,639	6,500,614
Ratios					
Return on average assets	0.45%	.08%	.57%	.74%	.74%
Return on average equity	5.58%	0.91%	5.78%	8.05%	8.53%
Average equity to average assets	8.14%	8.64%	9.86%	9.16%	8.66%
Selected Year-end Balances					
Assets	$ 350,190	$ 329,262	$ 300,529	$ 250,763	$ 238,768
Loans	276,196	263,738	240,816	196,034	185,610
Securities	35,016	28,524	27,707	28,149	32,249
Deposits	273,976	246,939	212,563	173,556	173,515
Borrowed funds	47,007	53,796	58,924	50,549	43,610
Shareholders’ equity	27,453	27,156	27,852	25,122	20,556
Selected Average Balances					
Assets	$ 334,193	$ 321,093	$ 273,679	$ 238,371	$ 230,926
Loans	267,164	256,525	221,158	186,532	177,531
Securities	29,038	28,846	27,281	30,517	32,454
Deposits	254,591	234,424	188,803	169,371	164,821
Borrowed funds	50,265	57,296	56,263	45,502	44,643
Shareholders’ equity	27,187	27,741	26,980	21,833	19,988

(1) Net income per share, book value per share, weighted average shares outstanding and shares outstanding at year-end for 2001 through 2005 have been adjusted to reflect 3% stock dividends issued in 2005, 2004, 2003, 2002 and 2001.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Management's Discussion And Analysis of Financial Condition
And Results of Operations

A discussion and analysis of the Company's operating results and financial condition are presented in the following narrative and financial tables. The comments are intended to supplement and should be reviewed in conjunction with the consolidated financial statements and notes thereto appearing on pages 5 - 34. References to changes in assets and liabilities represent end of period balances unless otherwise noted. All references in this Annual Report to net income per share and weighted average common and common equivalent shares outstanding have been adjusted to reflect 3% stock dividends in 2005, 2004 and 2003. Statements contained in this annual report, which are not historical facts, are forward-looking statements, as that term is defined in the Private Securities Litigation Reform Act of 1995. Amounts herein could vary as a result of market and other factors. Such forward-looking statements are subject to risks and uncertainties which could cause actual results to differ materially from those currently anticipated due to a number of factors, which include, but are not limited to, factors discussed in documents filed by the Company with the Securities and Exchange Commission from time to time. Such forward-looking statements may be identified by the use of such words as "believe," "expect," "anticipate," "should," "might," "planned," "estimated," and "potential." Examples of forward-looking statements include, but are not limited to, estimates with respect to the financial condition, expected or anticipated revenue, results of operations and business of the Company that are subject to various factors which could cause actual results to differ materially from these estimates. These factors include, but are not limited to, general economic conditions, changes in interest rates, deposit flows, loan demand, real estate values, and competition; changes in accounting principles, policies, or guidelines; changes in legislation or regulation; and other economic, competitive, governmental, regulatory, and technological factors affecting the Company's operations, pricing, products and services.

Financial Condition at December 31, 2005 and December 31, 2004

The Company's total assets increased $20.9 million or 6.4% from $329.3 million at December 31, 2004 to $350.2 million at December 31, 2005. This increase resulted primarily from a $12.5 million increase in loans receivable, a $6.5 million increase in securities available for sale and a $1.8 million increase in cash and cash equivalents.

Loans receivable increased $12.5 million, from $263.7 million at December 31, 2004 to $276.2 million at December 31, 2005, an increase of 4.7%. The growth was largely due to the 13.7% or $14.1 million increase in our residential loan portfolio. Commercial real estate loans increased $2.6 million. Construction lending experienced a decrease of 16.8% or $4.3 million at December 31, 2005, while commercial loans decreased 1.1%. At December 31, 2005 the allowance for loan losses was $4.5 million which represents 1.62% of the loan portfolio.

Investment securities increased 22.8% during 2005, from $28.5 million at December 31, 2004 to $35.0 million at December 31, 2005. Throughout the year we invested in mortgage backed securities, municipals and commercial paper. Mortgage backed securities increased $2.8 million or 94.2% during the period, while municipals increased $574 thousand.

Cash and cash equivalents increased at $1.8 million at December 31, 2005. This increase was generated by a $2.1 million or 51.2% increase in federal funds sold, increasing from $4.1 million at December 31, 2004 to $6.2 million at December 31, 2005. Interest-earning deposits with banks declined $295 thousand during the period.

Other changes in our consolidated assets relate to interest receivable, Federal Home Loan Bank stock and other assets. Interest receivable grew $252 thousand or 19.8% during 2005, impacted by both loan and investment growth while Federal Home Loan Bank stock decreased $313 thousand or 13.1%. Federal Home Loan Bank stock ownership is a requirement for

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member banks that utilize Federal Home Loan Bank for borrowing funds. The amount of stock owned by each member bank is based on the amount of borrowings outstanding. Other assets also declined $524 thousand or 11.3%. This decrease resulted primarily from a decrease in foreclosed real estate of $312 thousand. Foreclosed real estate represents loans that were secured by real estate and defaulted, requiring the Company to foreclose on the property.

Customer deposits continued to be our principal funding source in 2005, allowing us to fund the growth in assets discussed above. At December 31, 2005, deposits from our customers totaled $274.0 million, an increase of $27.0 million or 11.0% from $247.0 million at December 31, 2004. Time deposits grew $16.5 million or 18.4% during the period while noninterest-bearing demand increased $10.4 million or 28.2%.

The growth in deposits allowed the Company to reduce net borrowings by $6.8 million during 2005. Borrowings consist of both short-term and long-term borrowed funds. The Company utilizes both short-term and long-term advances from the Federal Home Loan Bank. At December 31, 2005, $31.4 million of the total borrowings of $47.0 million were attributed to Federal Home Loan Bank advances.

At December 31, 2005, total shareholders' equity was $27.5 million, an increase of $297 thousand from $27.2 million at the end of 2004. The Company earned net income of $1.5 million and collected $347 thousand from the exercise of stock options. These increases to shareholders' equity were offset by unrealized losses on our investment securities, net of tax, of $458 thousand and by the Company's purchase of 197,026 shares of common stock at a cost of $1.2 million.

Results of Operations for the Years Ended December 31, 2005 and 2004

Earnings

The Company earned net income of $1.5 million or $0.22 per share for 2005 as compared with net income of $253 thousand or $0.04 per share in 2004.

Net Interest Income

As with most financial institutions, the primary component of earnings for our banks, is net interest income. Net interest income is the difference between interest income, principally from loan and investment securities portfolios, and interest expense, principally on customer deposits and borrowings. Changes in net interest income result from changes in volume, spread and margin. For this purpose, volume refers to the average dollar level of interest-earning assets and interest-bearing liabilities, spread refers to the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities, and margin refers to net interest income divided by average interest-earning assets. Margin is influenced by the level and relative mix of interest-earning assets and interest-bearing liabilities, as well as by levels of noninterest-bearing liabilities and capital.

Net interest income increased $1.4 million to $12.5 million for 2005 compared to the $11.2 million earned in 2004. During 2005 the Company benefited from a rising interest rate environment, augmented by loan and investment growth. The average yield on our interest-earning assets increased 79 basis points to 6.36%, while the average rate we paid for our interest bearing liabilities increased 68 basis points. These increases resulted in an increment of 11 basis points in our interest rate spread, from 3.71% in 2004 to 3.82% in 2005. Our net interest margin for 2005 was 4.21%, compared to 3.96% in 2004. Financial Table 1 on page 45 presents a detailed analysis of the components of the Company's net interest income while Financial Table 2 on page 46 summarizes the effects on net interest income of changes in interest rates and in the dollar volume of the components of interest earnings assets and interest bearing liabilities.

Noninterest Income

The Company generates most of its revenue from net interest income; however, diversification of our earnings base is of major importance to our long term success. Noninterest income increased 1.9%, from $4.3 million in 2004 to $4.4 million in 2005, an increase of $81 thousand. Other banking fees increased $180 thousand or 28.8% during 2005. Income generated from brokerage commissions and asset management fees increased $121 thousand to $921 thousand, while service charges on deposit accounts grew $271 thousand to $1.7 million. During 2005 the Company implemented a new non-sufficient funds program. This new program along with the growth in demand deposit accounts resulted in $247 thousand increase in NSF fees. The Company also benefited from an increase in gain on sale of fixed assets and other assets of $102 thousand. These increases were offset by a decline in income from mortgage loan sales of $290 thousand. During 2005 the Federal Reserve continued raising interest rates resulting in lower volume of mortgage loan activity. Other income also decreased from $529 thousand in 2004 to $290 thousand in 2005.

Provision and Allowance for Loan Losses

The Company's allowance for loan losses is established through charges to earnings in the form of a provision for loan losses. The allowance is increased by provisions charged to operations and by recoveries of amounts previously charged off, and reduced by loans charged off. Management evaluates the adequacy of the allowance at least quarterly. In evaluating the adequacy of the allowance, management considers the growth, composition and industry diversification of the portfolio, historical loan loss experience, current delinquency levels, adverse situations that may affect a borrower's ability to repay, estimated value of any underlying collateral, prevailing economic conditions and other relevant factors. The Company's credit administration function, through a review process, validates the accuracy of the initial risk grade assessment. In addition, as a given loan's credit quality improves or deteriorates, the credit administration department has the responsibility to change the borrowers risk grade accordingly. For loans determined to be impaired, the allowance is based either on discounted cash flows using the loan's initial effective interest rate or on the fair value of the collateral for certain collateral dependent loans. This evaluation is inherently subjective, as it requires material estimates, including the amounts and timing of future cash flows expected to be received on impaired loans, which may be susceptible to significant change. In addition, regulatory agencies, as an integral part of their examination process, periodically review the allowance for loan losses and may require additions for estimated losses based upon judgments different from those of management.

Management uses the risk-grading program to facilitate the evaluation of probable inherent loan losses and the adequacy of the allowance for loan losses. In this program, risk grades are initially assigned by loan officers and reviewed and monitored by credit administration. The Company strives to maintain its loan portfolio in accordance with conservative loan underwriting policies that result in loans specifically tailored to the needs of its market area. Every effort is made to identify and minimize the credit risks associated with such lending strategies. The Company has no foreign loans and does not engage in significant lease financing or highly leveraged transactions. The Company follows a loan review program designed to evaluate the credit risk in the loan portfolio. This process includes the maintenance of an internally classified

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watch list that helps management assess the overall quality of the loan portfolio and the adequacy of the allowance for loan losses. In establishing the appropriate classification for specific assets, management considers, among other factors, the estimated value of the underlying collateral, the borrower's ability to repay, the borrower's payment history and the current delinquent status. As a result of this process, certain loans are categorized as substandard, doubtful or loss and reserves are allocated based on management's judgment and historical experience.

Loans classified as "substandard" are those loans with clear and defined weaknesses such as unfavorable financial ratios, uncertain repayment sources or poor financial condition that may jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Company may sustain some losses if the deficiencies are not corrected. A reserve of 15% is generally allocated to these loans. Loans classified as "doubtful" are those loans that have characteristics similar to substandard loans but with an increased risk that collection or liquidation in full is highly questionable and improbable. A reserve of 50% is generally allocated to loans classified as doubtful. Loans classified as "loss" are considered uncollectible and of such little value that continuance as bankable assets is not warranted. This classification does not mean that the loan has absolutely no recovery or salvage value but rather it is not practical or desirable to defer writing off this asset even though partial recovery may be achieved in the future. As a practical matter, when loans are identified as loss they are charged off against the allowance for loan losses. In addition to the above classification categories, the Company also categorizes loans based upon risk grade and loan type, assigning an allowance allocation based upon each category.

The allowance for loan losses represents management's estimate of an amount adequate to provide for known and inherent losses in the loan portfolio in the normal course of business. While management believes that it uses the best information available to establish the allowance for loan losses, future adjustments to the allowance may be necessary and results of operations could be adversely affected if circumstances differ substantially from the assumptions used in making the determinations. Furthermore, while management believes it has established the allowance for loan losses in conformity with generally accepted accounting principles, there can be no assurance that regulators, in reviewing the Company's portfolio, will not require an adjustment to the allowance for loan losses. In addition, because future events affecting borrowers and collateral cannot be predicted with certainty, there can be no assurance that the existing allowance for loan losses is adequate or that increases will not be necessary should the quality of any loans deteriorate as a result of the factors discussed herein. Any material increase in the allowance for loan losses may adversely affect the Company's financial condition and results of operations.

The provision for loan losses declined from $2.1 million in 2004 to $755 thousand in 2005, a decrease of $1.3 million. During 2004, specific loan loss reserves were increased by $1.2 million in anticipation of potential losses on five commercial lending relationships. Certain of these losses were realized in 2005, thereby accounting for the increase in total loan charge-offs from $374 thousand in 2004 to $1.4 million in 2005. Accordingly, the ratio of net loan charge offs to average loans outstanding increased 34 basis points from .13% in 2004 to .47% in 2005.

In light of the loan charge-offs referred to above and the resulting decrease in specific loan loss reserves, the Company's allowance for loan losses was reduced to $4.5 million at December 31, 2005, from $5.0 million at December 31, 2004. The allowance as a percentage of gross loans outstanding decreased 27 basis points from 1.89% at December 31, 2004 to 1.62% at December 31, 2005. Nonperforming loans were $1.9 million at December 31, 2005, as compared to $3.4 million at year-end 2004. Nonperforming loans to total loans decreased from

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1.29% at December 31, 2004 to .68% at December 31, 2005, while the allowance for loan losses to nonperforming loans increased to 239.1% from 147.6% at the end of 2004. At December 31, 2005, loans 90 days past due and still accruing declined by $811 thousand to $339 thousand, compared to $1.2 million at December 31, 2004. Restructured loans, excluding those included in nonperforming loans, amounted to $3.3 million at December 31, 2005. Management believes the current level of the allowance for loan losses to be adequate at this time.

Noninterest Expense

Noninterest expense increased $790 thousand to $14.1 million in 2005 compared to $13.3 million in 2004. Salaries and employee benefits, the largest component of noninterest expense, increased $847 thousand, from $7.2 million in 2004 to $8.0 million in 2005. Additions at the executive and bank support staff levels together with normal salary increases, primarily account for this increase. Data processing costs increased 4.1% or $34 thousand in 2005. These increases were offset by decreases in equipment expense of $26 thousand and other noninterest expense of $67 thousand. While other noninterest expense increased $67 thousand for the year, electronic banking expense, a major component of this category, increased $200 thousand to $478 thousand. The increased usage of electronic banking products is the reason for the increase.

Income Tax Expense

The Company had income tax expense of $524 thousand for 2005, at an effective tax rate of 25.66% compared to an income tax benefit of $199 in 2004. Income taxes computed at the statutory rate are reduced primarily by the eligible amount of interest earned on state and municipal securities and income earned on bank owned life insurance.

Results of Operations for the Years Ended December 31, 2004 and 2003

Earnings

Net income for the year ended December 31, 2004 was $253 thousand or $0.04 per share, as compared with net income of $1.6 million or $0.22 per share, for the year ended December 31, 2003, a decrease of $1.3 million or $0.18 per share. This decrease resulted primarily from an increase in provision for loan losses of $1.5 million in 2004.

Net Interest Income

Net interest income increased $1.2 million to $11.2 million for 2004 compared to the $10.0 million earned in 2003. This increase resulted primarily from the significant increase in the level of our average interest-earning assets during the year. This increase in our average earning assets, combined with a decrease in the average rates we paid for our interest-bearing liabilities of 28 basis points, offset the factors that negatively affected our net interest income in 2004. This negative factor was a decrease in the average rate we realized for our earnings assets and an increase in the level of our average interest-bearing liabilities during the year. The aforementioned increases in the level of our average interest-earnings assets and interest- bearing liabilities were greatly enhanced by the growth that Cabarrus Bank and Trust Company had due in 2004.

The average yield on our interest-earning assets decreased 43 basis points to 5.57% while the average rate we paid for our interest-bearing liabilities decreased only 28 basis points.

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Therefore our interest spread dropped form 3.86% to 3.71% and our net yield on interest earning assets decreased from 4.17% to 3.96%.

Provision and Allowance for Loan Losses

The provision for loan losses increased $1.5 million from $593 thousand in 2003 to $2.1 million in 2004. This increase in our provision resulted principally from management's decision to increase specific loan loss reserves by $1.2 million in 2004. The specific reserves are related primarily to five lending relationships. During 2004 the economic conditions of the local market areas the Company serves continued to be somewhat uncertain. Some of the highest unemployment rates in the state were being experienced by the communities we serve. These challenges have carried over into our business. Along with the increase in specific reserves, net loan charge offs increased from $124 thousand in 2003 to $333 in 2004. Net loan charge offs as a percentage of average loans was 0.06% and 0.13% respectively.

Our allowance for loan losses increased from $3.2 million at December 31, 2003 to $5.0 million at December 31, 2004. The allowance expressed as a percentage of gross loans increased 55 basis points from 1.34% to 1.89%. Non performing loans were $3.4 million at December 31, 2004 as compared to $1.6 million at 2003. The rates of nonperforming loans to total loans at December 31, 2004 and 2003 was 1.29% and .65% respectively.

Noninterest Income

Total noninterest income decreased $889 thousand, from $5.2 million for the year ended at December 31, 2003 to $4.3 million for the same period in 2004. The primary factor in this decrease was a reduction in income from mortgage loan sales of $1.2 million or 59.2% in 2004. As the Federal Reserve started raising rates to help boast the economy mortgage rates also began to rise, bringing the mortgage refinancing boom of the past several years to a stop. Gains on sales of securities also contributed to the decrease, dropping $126 thousand in 2004. Offsetting the decrease, however, was an increase in other banking fees of $147 thousand. Brokerage commissions and asset management fees accounted for $227 thousand of that increase. Service charges of deposit accounts also increased $88 thousand during 2004.

Noninterest Expense

As a percentage of average total assets, total noninterest expenses decreased, from 4.6% in 2003 to 4.14% in 2004. For the years ended December 31, 2004, and to 2003, noninterest expenses totaled $13.3 million and $12.5 million, respectively, an increase of $831 thousand. As would be expected, the opening of a denovo bank during the second quarter of 2003 contributed largely to the increase, accounting for $420 thousand or 50.6% of the overall increase in the Company's noninterest expenses.

Salaries and employee benefits, the largest component of noninterest expense, increased $302 thousand or 4.4%, from $6.9 million for 2003 to $7.2 million for 2004. The addition of a new executive position coupled with the addition of the support staff for the new bank and normal annual salary increases were the factors behind this increase. Net occupancy expense increased 20.7% or $110 thousand for the period ended December 31, 2004. The increase in utility cost and depreciation are attributed to the new location in Cabarrus County.

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Income Tax Expense

Income taxes computed at the statutory rate are reduced primarily by the eligible amount of interest earned on state and municipal securities. For 2004 the Company had an income tax benefit of $199 thousand, compared to income tax expense of $531 thousand for 2003, for an effective tax rate of 25.4%.

Capital Resources

The Company continues to maintain good capital ratios that support its asset growth. The capital position is maintained through the retention of earnings and controlled growth. Regulatory agencies divide capital into Tier I (consisting of shareholders' equity less ineligible intangible assets and accumulated other comprehensive income and allowable portions of trust preferred securities) and Tier II (consisting of the allowable portion of the reserve for loan losses and certain long-term debt) and measure capital adequacy by applying both capital levels to a banking company's risk-adjusted assets and off-balance sheet items. In addition to these capital ratios, regulatory agencies have established a Tier I leverage ratio that measures Tier I capital to average assets less ineligible intangible assets.

Regulatory guidelines require a minimum of total capital to risk-adjusted assets ratio of 8% with one-half consisting of tangible common shareholders' equity and a minimum Tier I leverage ratio of 4%. Banks which meet or exceed a Tier I ratio of 6%, a total capital ratio of 10% and a Tier I leverage ratio of 5% are considered well capitalized by regulatory standards. At December 31, 2005, the Company and it's subsidiary banks were all well capitalized.

The Company expects to continue to exceed these minimums without altering current operations or strategy. Note 13 to the Consolidated Financial Statements presents additional information regarding the Company's and its subsidiary banks' capital ratios.

Dividends

The Board of Directors of Uwharrie Capital Corp declared a 3% stock dividend in 2005 and in 2004. All references in this annual report to net income per share and weighted average common and common equivalent shares outstanding reflect the effects of these stock dividends.

Liquidity

Liquidity, the ability to raise cash when needed without adversely impacting profits, is managed primarily by the selection of asset mix and the maturity mix of liabilities. Maturities and the marketability of securities and other funding sources provide a source of liquidity to meet deposit fluctuations. Maturities in the securities portfolio, presented in Financial Table 4 on page 49, are supported by cash flows from mortgage-backed securities that have longer-term contractual maturities.

Other funding sources at year-end 2005 included $20.2 million in federal funds lines of credit from correspondent banks and approximately $26.6 million of remaining credit availability from the Federal Home Loan Bank. The Company may also borrow from the Federal Reserve Bank discount window. Growth in deposits is typically the primary source of funding for loans, supported by long-term credit available from the Federal Home Loan Bank.

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At December 31, 2005 borrowings from federal funds lines and securities sold under repurchase agreements amounted to $3.4 million, while other short-term borrowings totaled $4.5 million. Long-term debt at that date consisted of advances of $31.4 million from the Federal Home Loan Bank, a note payable of $2.4 million to another bank and $5.2 million in junior subordinated debentures and mortgage payable of $112 thousand.

Management believes that the Company's current sources of funds provide adequate liquidity for its current cash flow needs.

Contractual Obligations

The following table reflects the contractual obligations of the Company outstanding as of December 31, 2005.

	Payments Due by Period (in thousands)				
	Total	On Demand or less than 1 year	1-3 Years	4-5 Years	After 5 Years
Contractual Obligations					
Short-term debt	$ 7,904	$ 7,904	$ —	$ —	$ —
Long-term debt	33,948	7,407	17,251	3,816	5,474
Trust Long-term debt	5,155	—	—	—	5,155
Total contractual cash obligations, excluding deposits	47,007	15,311	17,251	3,816	10,629
Deposits	273,976	238,095	33,710	2,117	54
Total contractual cash obligations, including deposits	$320,983	$ 253,406	$50,961	$5,933	$10,683

Critical Accounting Policy

The Company's most significant critical accounting policy is the determination of its allowance for loan losses. A critical accounting policy is one that is both very important to the portrayal of the Company's financial condition and results, and requires management's most difficult, subjective or complex judgments. What makes these judgments difficult, subjective and/or complex is the need to make estimates about the effects of matters that are inherently uncertain. Refer to the discussion within Provision and Allowance for Loan Losses and Note 1 to the consolidated financial statements for a comprehensive discussion regarding this accounting policy.

Off-Balance Sheet Arrangements

The Company has various financial instruments (outstanding commitments) with off-balance sheet risk that are issued in the normal course of business to meet the financing needs of its customers. See Note 11 to the consolidated financial statements for more information regarding these commitments and contingent liabilities.

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Interest Rate Sensitivity

The major component of income for the Company is net interest income, the difference between yield earned on assets and interest paid on liabilities. This differential or margin can vary over time as changes in interest rates occur. The volatility of changes in this differential can be measured by the timing (or repricing) difference between maturing assets and liabilities.

To identify interest rate sensitivity, a common measure is a gap analysis, which reflects the difference or gap between rate sensitive assets and liabilities over various time periods. Gap analysis at December 31, 2005 is reflected in Financial Table 3 on page 47. While management reviews this information, it has implemented the use of a simulation model which calculates expected net interest income based on projected interest-earning assets, interest-bearing liabilities and interest rates and provides a more relevant view of interest rate risk than traditional gap tables. The simulation allows comparison of flat, rising and falling rate scenarios to determine sensitivity of earnings to changes in interest rates.

The principal goals of the Company's asset liability management are the maintenance of adequate liquidity and the management of interest rate risk. Interest rate risk management attempts to balance the effects of interest rate changes on interest-sensitive assets and liabilities to protect net interest income from wide fluctuations that could result from changes in interest rates. The Company's Asset Liability Management Committee monitors market changes in interest rates and assists with pricing loan and deposit products consistent with funding source needs and asset growth projections.

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Financial Table 1

Average Balances and Net Interest Income Analysis
(dollars in thousands)

	2005			2004			2003		
	Average Balance	Interest Income/ Expense	Average Yield/ Rate (1)	Average Balance	Interest Income/ Expense	Average Yield/ Rate (1)	Average Balance	Interest Income Expense	Average Yield Rate (1)
Interest-earning assets									
Taxable securities	$ 19,363	$ 881	4.55%	$ 17,104	$ 741	4.33%	$ 15,554	$ 670	4.31%
Non-taxable securities	11,962	533	6.86%	11,741	598	7.84%	11,727	607	7.96%
Short-term investments	8,740	302	3.46%	7,862	99	1.26%	2,396	26	1.09%
Taxable loans (2)	263,168	17,252	6.56%	252,414	14,266	5.65%	216,469	13,047	6.03%
Non-taxable loans	3,996	193	7.43%	4,111	202	7.56%	4,689	247	8.10%
Total interest-earning assets	307,229	19,161	6.36%	293,232	15,906	5.57%	250,835	14,597	6.00%
Non-earning assets									
Cash and due from banks	11,904			10,320			8,656		
Premises and equipment, net	8,367			8,558			7,443		
Interest receivable and other	6,693			8,983			6,745		
Total non-earning assets	$ 26,964			$ 27,861			$ 22,844		
Total assets	$334,193			$321,093			$273,679		
Interest-bearing liabilities									
Savings deposits	$ 37,987	$ 580	1.53%	$ 41,883	$ 322	0.77%	$ 41,626	$ 372	0.89%
Interest checking & MMDA	72,755	1,002	1.38%	72,291	616	0.85%	50,408	453	0.90%
Time deposits	99,704	2,891	2.90%	83,516	1,738	2.08%	67,054	1,673	2.50%
Total deposits	210,446	4,473	2.13%	197,690	2,676	1.35%	159,088	2,498	1.57%
Short-term borrowed funds	8,564	239	2.78%	13,468	127	0.94%	12,032	147	1.22%
Long-term debt	41,701	1,918	4.60%	43,828	1,931	4.41%	44,231	1,961	4.43%
Total interest-bearing Liabilities	260,711	6,630	2.54%	254,986	4,734	1.86%	215,351	4,606	2.14%
Noninterest liabilities									
Transaction deposits interest payable and other	46,295			38,366			31,348		
Total liabilities	$307,006			$293,352			$246,699		
Shareholders' equity	27,187			27,741			26,980		
Total liabilities and Shareholders equity	$334,193			$321,093			$273,679		
Interest rate spread			3.82%			3.71%			3.86%
Net interest income and net interest margin		$12,531	4.21%		$11,172	3.96%		$ 9,991	4.17%

1) Yields related to securities and loans exempt from federal and/or state income taxes are stated on a fully tax-equivalent basis, assuming a 35% tax rate.
2) Nonaccrual loans are included in loans, net of unearned income.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Management's Discussion And Analysis of Financial Condition
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Financial Table 2

Volume and Rate Variance Analysis
(dollars in thousands)

	2005 Versus 2004			2004 Versus 2003		
	Volume	Rate	Net Change	Volume	Rate	Net Change
Interest-earning assets						
Taxable securities	$ 100	$ 40	$ 140	$ 67	$ 4	$ 71
Non-taxable securities	11	(76)	(65)	1	(10)	(9)
Short-term investments	21	182	203	64	9	73
Taxable loans	656	2,330	2,986	2,099	(880)	1,219
Non-taxable loans	(6)	(3)	(9)	(29)	(16)	(45)
Total Interest-earning assets	782	2,473	3,255	2,202	(893)	1,309
Interest-bearing liabilities						
Savings deposits	(45)	303	258	2	(52)	(50)
Transaction and MMDA deposits	5	381	386	192	(29)	163
Other time deposits	403	750	1,153	377	(312)	65
Short-term borrowed funds	(92)	204	112	16	(36)	(20)
Long-term debt	(96)	83	(13)	(18)	(12)	(30)
Total interest-bearing liabilities	175	1,721	1,896	569	(441)	128
Net interest income	$ 607	$ 752	$ 1,359	$1,633	$(452)	$ 1,181

The above table analyzes the dollar amount of changes in interest income and interest expense for major components of interest-earning assets and interest-bearing liabilities. The table distinguishes between (i) changes attributable to volume (changes in volume multiplied by the prior period's rate), (ii) changes attributable to rate (changes in rate multiplied by the prior period's volume), and (iii) net change (the sum of the previous columns). The change attributable to both rate and volume (changes in rate multiplied by changes in volume) has been allocated equally to the change attributable to volume and the change attributable to rate.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
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Financial Table 3

Interest Rate Sensitivity Analysis
(dollars in thousands)

	1-90 Day Position	3-6 Month Position	6-12 Month Position	1-5 Year Position	> 5 Year Position	Total Position
Interest-earning assets						
Due from banks	$ 3,730	$ —	$ —	—	$ —	$ 3,730
Federal funds sold	6,200	—	—	—	—	6,200
Investment securities	—	2,480	2,023	12,265	18,248	35,016
FHLB and other stock	—	—	—	—	2,144	2,144
Loans	188,610	3,791	6,801	47,186	29,808	276,196
Total interest-earning assets	198,540	6,271	8,824	59,451	50,200	323,286
Interest-bearing liabilities						
Deposits	111,724	22,749	23,906	48,193	20,125	226,697
Short-term borrowed funds	7,903	—	—	—	—	7,903
Long-term debt	400	—	7,007	19,065	12,631	39,103
Total interest-bearing liabilities	120,027	22,749	30,913	67,258	32,756	273,703
Interest sensitivity GAP per period	$ 78,513	$(16,478)	$(22,089)	$ (7,807)	$17,444	$ 49,583
Cumulative interest sensitivity GAP	$ 78,513	$ 62,035	$ 39,946	$32,139	$49,583	$ 49,583
Ratios						
Cumulative gap as a percentage of total interest-earning assets	24.29%	19.19%	12.36%	9.94%	15.34%	15.34%
Cumulative interest-earning assets as a percentage of interest-bearing liabilities	165.41%	143.45%	123.00%	113.34%	118.12%	118.12%

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
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Financial Table 4

Investment Securities Portfolio Analysis

	December 31, 2005		
	Amortized Cost	Estimated Fair Value	Book Yield(1)
Securities available for sale			
U.S. Treasury			
Due after one but within five years	$ 2,988,145	$ 2,901,562	3.28%
U.S. Government agencies			
Due after one but within five years	7,945,053	7,819,963	3.91%
Due after five but within ten years	1,905,253	1,918,125	4.86%
	9,850,306	9,738,088	4.09%
Mortgage-backed securities			
Due after one but within five years	21,711	22,146	6.63%
Due after five but within ten year	1,906,027	1,901,838	4.16%
Due after ten years	3,844,693	3,860,237	5.85%
	5,772,431	5,784,221	5.29%
State and political			
Due within one year	2,002,573	2,022,526	9.08%
Due after one but within five years	1,430,276	1,521,707	8.26%
Due after five but within ten year	2,453,590	2,579,255	7.92%
Due after ten years	6,969,326	7,432,864	8.21%
	12,855,765	13,556,352	8.30%
Commercial Paper			
Due within one year	2,479,513	2,479,513	4.34%
Corporate Bond			
Due after ten years	527,340	536,618	6.00%
Equity Securities			
Due within one year	8,125	19,524	2.13%
Total Securities available for sale			
Due within one year	4,490,211	4,521,563	6.45%
Due after one but within five years	12,385,185	12,265,378	4.26%
Due after five but within ten year	6,264,870	6,399,218	5.85%
Due after ten years	11,341,360	11,829,719	7.31%
	$34,481,625	$35,015,878	5.84%

1) Yields on securities and investments exempt from federal and/or state income taxes are stated on a fully tax- equivalent basis, assuming a 35% tax rate.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
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Financial Table 5

Noninterest Income

	Year Ended December 31,		
	2005	2004	2003
Service charges on deposit accounts	$1,706,784	$1,435,827	$1,347,538
Other banking fees	806,930	626,518	479,408
Asset management fees	497,081	356,725	135,083
Brokerage commissions	423,944	443,238	437,863
Other noninterest income	290,068	529,362	423,965
Core noninterest income	3,724,807	3,391,670	2,823,857
Income from mortgage loan sales	554,414	844,882	2,072,433
Security gains (losses)	(16,272)	2,373	128,845
Other gains from sale of assets	88,152	31,599	134,447
Total noninterest income	$4,351,101	$4,270,524	$5,159,582

Financial Table 6

Other Noninterest Expense

	Year Ended December 31,		
	2005	2004	2003
Professional fees and services	$ 456,365	$ 450,242	$ 434,224
Marketing and donations	434,322	521,655	404,085
Office supplies and printing	259,596	291,434	322,013
Postage	166,771	168,109	163,033
Telephone and data lines	200,280	209,757	208,266
Electronic banking expense	328,446	278,021	306,113
Software amortization and maintenance	257,177	357,926	282,637
Loan collection cost	298,585	240,374	98,025
Impairment of servicing assets	—	—	200,000
Other	1,558,098	1,508,852	1,220,388
Total	$3,959,640	$4,026,370	$3,638,784

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
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Financial Table 7

Loan Portfolio Composition
(dollars in thousands)

	At December 31,					
	2005		2004		2003	
	Amount	% of Total Loans	Amount	% of Total Loans	Amount	% of Total Loans
Loan type:						
Commercial	$ 37,299	13.51%	$ 37,718	14.31%	$ 38,517	16.00%
Real estate - construction	21,206	7.68%	25,480	9.67%	21,813	9.06%
Real estate - residential	116,715	42.29%	102,627	38.93%	76,933	31.95%
Real estate - commercial	83,861	30.39%	81,283	30.84%	84,920	35.27%
Consumer	13,479	4.88%	13,488	5.12%	12,741	5.29%
Loans held for sale	3,354	1.22%	2,903	1.10%	5,665	2.35%
Other	72	0.03%	90	0.03%	187	0.08%
Total loans	275,986	100.00%	263,589	100.00%	240,776	100.00%
Less:						
Allowance for loan losses	(4,482)		(4,983)		(3,224)	
Unearned net loan fees	210		149		40	
Net loans	$271,714		$258,755		$237,592	

	At December 31,			
	2002		2001	
	Amount	% of Total Loans	Amount	% of Total Loans
Loan type:				
Commercial	$ 38,680	19.73%	$ 35,846	19.31%
Real estate - construction	10,893	5.56%	13,063	7.04%
Real estate - residential	68,876	35.13%	86,811	46.76%
Real estate - commercial	61,027	31.13%	35,802	19.28%
Consumer	12,888	6.57%	13,969	7.52%
Loans held for sale	3,569	1.82%	—	0.00%
Other	123	0.06%	177	0.09%
Total loans	196,056	100.00%	185,668	100.00%
Less:				
Allowance for loan losses	(2,755)		(2,180)	
Unearned net loan fees	(23)		(58)	
Net loans	$193,278		$183,430	

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
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Financial Table 8

Selected Loan Maturities
(dollars in thousands)

	December 31, 2005			
	One Year or Less	One to Five Years	Over Five Years	Total
Commercial and agricultural	$ 15,244	$ 20,353	$ 1,702	$ 37,299
Real estate – construction	13,565	6,305	1,336	21,206
Total selected loans	$ 28,809	$ 26,658	$ 3,038	$ 58,505
Sensitivity to rate changes:				
Fixed interest rates	$ —	$ —	$ —	$ —
Variable interest rates	186,449	818	—	187,267
Total	$186,449	$ 818	$ —	$187,267

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
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Financial Table 9

Nonperforming Assets
(dollars in thousands)

	At December 31,				
	2005	**2004**	**2003**	**2002**	**2001**
Nonperforming Assets:					
Nonaccrual loans	$ 1,875	$ 3,376	$ 1,577	$ 788	$ 1,101
Other real estate owned	169	481	108	714	85
Total nonperforming assets	$ 2,044	$ 3,857	$ 1,685	$ 1,502	$ 1,186
Accruing loans past due 90 days or more	$ 339	$ 1,150	$ 607	$ 587	$ 29
Allowance for loan losses	4,482	4,983	3,224	2,755	2,181
Nonperforming loans to total loans	.68%	1.29%	0.65%	0.40%	0.59%
Allowance for loan losses to total loans	1.62%	1.89%	1.34%	1.41%	1.17%
Nonperforming assets to total loans and other real estate	.74%	1.47%	0.70%	0.76%	0.64%
Nonperforming assets to total assets	.58%	1.17%	0.56%	0.60%	0.50%
Allowance for loan losses to nonperforming loans	239.09%	147.59%	204.44%	349.62%	198.14%

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
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Financial Table 10

Activity in the Allowance for Loan Loss
(dollars in thousands)

	At or for the Year Ended December 31,				
	2005	2004	2003	2002	2001
Allowance for loan losses at beginning of year	$4,983	$3,224	$2,755	$2,181	$1,795
Provision for loan losses	755	2,092	593	835	1,179
	5,738	5,316	3,348	3,016	2,974
Loan charge-offs:					
Commercial	1,124	224	10	66	131
Real estate	—	—	45	65	527
Consumer	254	149	95	150	182
Total charge-offs	1,378	373	150	281	840
Recoveries of loans previously charged off:					
Commercial	3	1	—	—	20
Real estate	—	—	1	—	8
Consumer	119	39	25	20	19
Total recoveries	122	40	26	20	47
Net charge-offs	1,256	333	124	261	793
Allowance for loan losses at end of year	$4,482	$4,983	$3,224	$2,755	$2,181
Net charge-offs as a percent of average loans	(0.47)%	(0.13)%	(0.06)%	(0.14)%	(0.45)%

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Management's Discussion And Analysis of Financial Condition And Results of Operations

Financial Table 11

Allocation of the Allowance for Loan Losses
(dollars in thousands)

	At December 31,					
	2005		2004		2003	
	Amount	% of Total Loans (1)	Amount	% of Total Loans (1)	Amount	% of Total Loans (1)
Commercial	$2,474	13.51%	$ 897	14.31%	$1,204	16.00%
Real estate - construction	101	7.68%	185	9.67%	171	9.06%
Real estate - residential	323	43.51%	509	40.04%	472	34.30%
Real estate - commercial	1,159	30.39%	2,965	30.84%	877	35.27%
Consumer loans	369	4.88%	359	5.12%	450	5.29%
Other	—	— %	—	— %	—	— %
Unallocated	56	0.03%	68	0.02%	50	0.08%
Total loans	$4,482	100.00%	$4,983	100.00%	$3,224	100.00%

	At December 31,			
	2002		2001	
	Amount	% of Total Loans (1)	Amount	% of Total Loans (1)
Commercial	$ 711	19.73%	$ 532	19.31%
Real estate – construction	163	5.56%	196	7.04%
Real estate – residential	590	36.95%	625	46.76%
Real estate – commercial	915	31.13%	512	19.28%
Consumer	325	6.57%	99	7.52%
Other	2	0.00%	—	0.00%
Unallocated	49	0.06%	17	0.09%
Total loans	$2,755	100.00%	$2,181	100.00%

(1) Represents total of all outstanding loans in each category as a percent of total loans outstanding.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
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Financial Table 12

Maturities of Time Deposits of $100,000 or More
(dollars in thousands)

	3 Months or Less	Over 3 Months to 6 Months	Over 6 Months to 12 Months	Over 12 Months	Total
Time Deposits of $100,000 or more	$ 6,854	$ 9,598	$ 10,993	$ 11,436	$38,881

Financial Table 13

Securities Performance Ratios

	At December 31,				
	2005	2004	2003	2002	2001
Return on average assets	0.45%	0.08%	0.57%	0.74%	0.74%
Return on average equity	5.58%	0.91%	5.78%	8.05%	8.53%
Equity to assets ratio	8.14%	8.64%	9.86%	9.16%	8.66%

UWHARRIE CAPITAL CORP
Board of Directors

Robert P. Barbee
Retired – Chairman, President and Chief Executive Officer
Pneumafil Corporation

Joe S. Brooks
Owner and Manager
Brothers Precision Tool Co.

Charles F. Geschickter, III
President
ST Motorsports, Inc.;
JTG Racing, Inc. and
Wood Bros. / JTG Racing, Inc.

Thomas M. Hearne, Jr.
Geopavement Engineer
NC Department of Transportation

Joseph R. Kluttz, Jr.
President
Albemarle Insurance Agency, Inc

B. Franklin Lee
Owner and Manager
Franklin Lee Farm

W. Chester Lowder
Director of Livestock Program
Public Policy Division
NC Farm Bureau

John P. Murray, MD
Retired – Physician and Owner
Albemarle Ear, Nose and Throat

James E. Nance
Board Chair
President and Dealer Operator
Confederate Motors, Inc.

Emmett S. Patterson
Retired – General Manager and Executive Vice President
Pee Dee Electric Membership Corporation

Timothy J. Propst
Executive Vice President
Propst Construction Co., Inc

Susan J. Rourke
President and Owner
US Land Management Co.

Donald P. Scarborough
President, Treasurer and Owner
Plank Road Realty, Inc.

John W. Shealy, Jr.
President
Cabarrus Concrete Co.

Michael E. Snyder, Sr.
Board Vice Chair
Vice President
E.J. Snyder & Company, Inc.

Douglas L. Stafford
Principal
Griffin Stafford, LLC

Emily M. Thomas
Vice President - Administration and Finance
CMH Flooring Products, Inc.

Hugh E. Wallace
President
Anson Apparel Company and
Anson Apparel III

Executive Officers

Roger L. Dick
President and
Chief Executive Officer
Uwharrie Capital Corp

Brendan P. Duffey
Executive Vice President and
Chief Operating Officer
Uwharrie Capital Corp

Patricia K. Horton
Chief Executive Officer
Cabarrus Bank & Trust Company

Robert B. Brannan, III
President
Cabarrus Bank & Trust Company

W.D. "Bill" Lawhon, Jr.
President
Chief Executive Officer
Bank of Stanly

Christy D. Stoner
President / Chief Executive Officer
The Strategic Alliance Corporation
BOS Agency, Inc., and Strategic Investment Advisors, Inc.
Executive Vice President
Uwharrie Capital Corp

Jimmy L. Strayhorn
President
Chief Executive Officer
Anson Bank & Trust Co.

EX-13 2 dex13.htm 2006 ANNUAL REPORT TO SHAREHOLDERS

Exhibit 13

Uwharrie Capital Corp

2006

ANNUAL REPORT TO SHAREHOLDERS

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UWHARRIE CAPITAL CORP AND SUBSIDIARIES

Description of Business

Uwharrie Capital Corp (the "Company") is a North Carolina bank holding company. The Company was organized on July 1, 1993 to become the bank holding company for the Bank of Stanly ("Stanly"), a North Carolina commercial bank chartered on September 28, 1983, and its three wholly-owned subsidiaries, The Strategic Alliance Corporation, BOS Agency, Inc., and Gateway Mortgage, Inc., a mortgage origination company. The Company also owns three non-bank subsidiaries, Strategic Investment Advisors, Inc., Uwharrie Mortgage, Inc. and Uwharrie Statutory Trust 1.

Stanly engages in retail and commercial banking, with five banking offices in Stanly County. Stanly provides a wide range of banking services including deposit accounts, commercial, consumer, home equity and residential mortgage loans, safe deposit boxes, and electronic banking services.

On January 19, 2000, the Company completed its acquisition of Anson BanCorp, Inc. and its subsidiary, Anson Savings Bank. The savings bank retained its North Carolina savings bank charter and became a wholly-owned subsidiary of Uwharrie Capital Corp as Anson Bank & Trust Co. ("Anson") and provides financial services to customers through one banking office in Anson County.

On April 10, 2003, the Company capitalized a new wholly-owned subsidiary bank, Cabarrus Bank & Trust Company ("Cabarrus"), located in Concord, North Carolina. As of that date, Cabarrus purchased two branch offices located in Cabarrus County from Stanly to begin its operation. Cabarrus operates as a commercial bank and provides a full range of banking services.

The Company and its subsidiaries are located in Stanly County, Anson County and Cabarrus County. However, the Company intends to prudently expand its service area to include the entire Uwharrie Lakes Region of North Carolina.

Depository services offered by the subsidiary banks include personal and commercial checking, savings, money market, certificates of deposit accounts and individual retirement accounts, all tailored to meet customers' needs. The banks provide fixed and variable rate loans, which include mortgage, home equity, lines of credit, consumer and commercial loans. The banks also offer Internet Banking and 24-Hour Telephone Banking, providing customers the convenience of access to account information, rate information and accessibility of funds transfers between accounts. Other services include MasterCard® credit cards and a Visa® Check Card which functions as a point-of-sale (POS) and automated teller machine (ATM) card. Customers can use the Check Card for purchases at any merchant accepting Visa® and at any ATM displaying the STAR® or CIRRUS® networks regionally and worldwide, respectively.

Strategic Investment Advisors Inc. provides portfolio management services to its customers. The Strategic Alliance Corporation (Strategic Alliance®) is a registered broker-dealer with the National Association of Securities Dealers, Inc. ("NASD"). BOS Agency provides insurance products and is licensed in the state of North Carolina. Through Strategic Investment Group, a DBA for a partnership with UVEST Financial Services, Inc., securities and insurance products are offered including fixed annuities, long-term care, and life products. Group insurance products are offered through an arrangement with Benchmark Life Strategies as well as Medicare supplement products.

The Strategic Alliance Corporation. Member NASD/SIPC.

Securities and insurance products are offered by, and Financial Consultants are registered with UVEST Financial Services, member NASD/SIPC. UVEST, Strategic Investment Group and Uwharrie Capital Corp affiliates are independent entities. Securities and/or insurance products are not FDIC insured, are not deposits or other obligations of any depository institution, are not guaranteed by any depository institution and are subject to investment risks, including possible loss of the principal amount invested.

Bank of Stanly. Member FDIC. Equal Housing Lender.
Anson Bank & Trust Co. Member FDIC. Equal Housing Lender.
Cabarrus Bank & Trust Company, Member FDIC, Equal Housing Lender.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES

Financial Highlights

(Dollars in thousands except per share amounts)	2006	2005	Percent Increase
For the year:			
Net Income	$ 2,071	$ 1,517	36.52%
Basic net income per common share (1)	$ 0.29	$ 0.21	38.10%
Diluted net income per common share	$ 0.28	$ 0.20	40.00%
Weighted average common shares outstanding (diluted)	7,354,229	7,418,773	(0.87)%
At year-end:			
Total assets	$ 383,261	$ 350,190	9.44%
Total earning assets	351,149	323,286	8.62%
Loans, net of unearned income	291,949	276,196	5.70%
Total interest-bearing liabilities	303,780	273,703	10.99%
Shareholders' equity	29,633	27,453	7.94%
Book value per share (1)	$ 3.99	$ 3.73	6.97%
Averages for the year:			
Total assets	$ 368,781	$ 334,193	10.35%
Total earning assets	341,995	307,229	11.32%
Loans, net of unearned income	293,394	267,164	9.82%
Total interest-bearing liabilities	291,041	260,711	11.63%
Shareholders' equity	28,299	27,187	4.09%
Financial Ratios (in percentage):			
Return on average assts	0.56%	0.45%	
Return on average shareholders' equity	7.32%	5.58%	
Average equity to average assets	7.67%	8.14%	
Net interest margin (fully tax equivalent basis)	4.10%	4.21%	
Allowance as % of loans at year-end	1.09%	1.62%	
Allowance as % of nonperforming loans	261.78%	239.09%	
Nonperforming loans to total loans	0.41%	0.68%	
Nonperforming assets to total assets	0.37%	0.58%	
Net loan charge-offs to average loans	0.55%	0.47%	

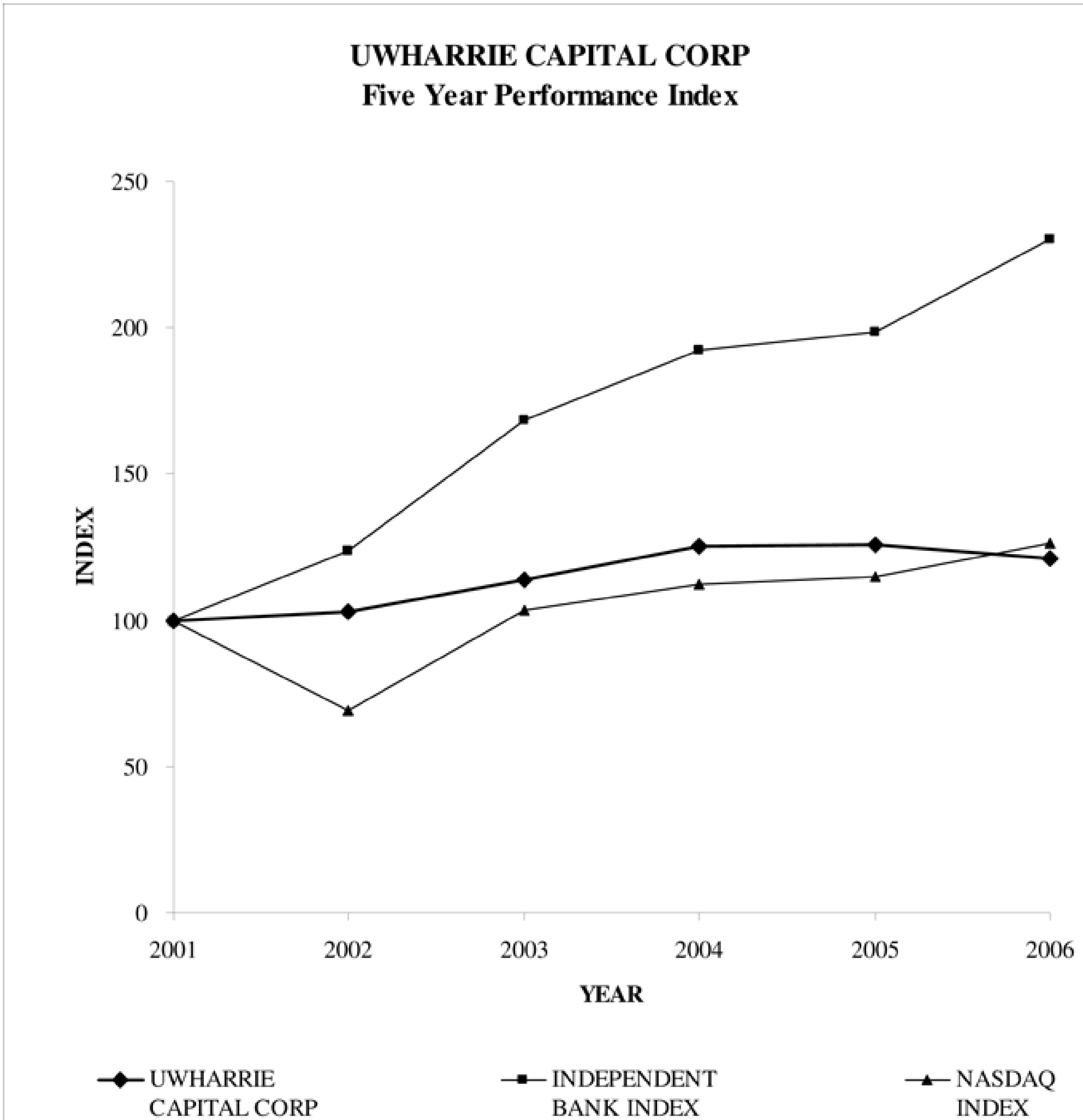
(1) Net income per share, book value per share, and shares outstanding at year-end have been adjusted to reflect the 3% stock dividends in 2006 and in 2005.

Market for the Company's Common Stock and Related Security Holder Matters

It is the philosophy of Uwharrie Capital Corp to promote a broad base of local shareholders. Therefore, management makes every reasonable effort to match willing buyers with willing sellers as they become known for the purpose of private negotiations for the purchase and sale of the Company's common stock. The Company, on a quarterly basis, has an independent valuation of the Company stock performed to assist with fairness and market efficiencies regarding these private negotiations and makes the most current valuation available to interested shareholders. Trades of the Company's stock also occur in the Over-the-Counter marketplace that involve a "spread" between the bid and ask prices to compensate the brokerage firms involved in the Over-the-Counter market. In addition, Uwharrie Capital Corp has adopted a program of on-going open market purchases of shares of the Company's stock. The combination of public and private trades as well as the holding company purchases provides good liquidity for the investors of Uwharrie Capital Corp stock. The Board of Directors has historically adopted a dividend policy on an annual basis. For 2006, Uwharrie Capital Corp declared a 3% stock dividend. The Board of Directors determines, on an annual basis, the dividend policy that is consistent with the capital needs of the Company.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES

The following graph compares (i) the yearly change in the cumulative total shareholder return on the Company's common stock with (ii) the cumulative return of The Carson Medlin Company Independent Bank Index, and (iii) the NASDAQ Composite. The graph assumes that the value of an investment in the Company's common stock and in each index was $100 on December 31, 2001, and that all dividends were reinvested. The performance shown in the graph represents past performance and should not be considered the indication of future performance.



Shareholders needing information about purchasing or selling shares of Uwharrie Capital Corp should contact Tamara M. Singletary or Lisa E. Hartsell, Investor Relations at Uwharrie Capital Corp, 132 N. First Street, Post Office Box 338, Albemarle, NC 28002.

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DIXON HUGHES PLLC
Certified Public Accountants and Advisors

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and Board of Directors
Uwharrie Capital Corp
Albemarle, North Carolina

We have audited the accompanying consolidated balance sheets of Uwharrie Capital Corp and Subsidiaries (the "Company") as of December 31, 2006 and 2005, and the related consolidated statements of income, comprehensive income, changes in shareholders' equity and cash flows for each of the years in the three-year period ended December 31, 2006. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Uwharrie Capital Corp and Subsidiaries as of December 31, 2006 and 2005, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2006, in conformity with accounting principles generally accepted in the United States of America.

Dixon Hughes PLLC

Raleigh, North Carolina
March 28, 2007

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
December 31, 2006 and 2005

	2006	2005
	(dollars in thousands)	
ASSETS		
Cash and due from banks	$ 14,762	$ 11,439
Interest-earning deposits with banks	2,473	3,730
Federal funds sold	17,525	6,200
Securities available for sale, at fair value	37,150	35,016
Loans:		
Loans held for sale	3,814	3,354
Loans held for investment	288,135	272,842
Less allowance for loan losses	(3,171)	(4,482)
Net loans	288,778	271,714
Premises and equipment, net	8,618	8,432
Interest receivable	1,775	1,525
Federal Home Loan Bank stock	1,980	2,072
Bank owned life insurance	5,133	4,949
Goodwill	987	987
Other assets	4,080	4,126
Total assets	$383,261	$350,190
LIABILITIES		
Deposits:		
Demand noninterest-bearing	$ 48,149	$ 47,280
Interest checking and money market accounts	101,470	83,680
Savings deposits	27,833	36,689
Time deposits, $100,000 and over	48,450	38,881
Other time deposits	83,698	67,446
Total deposits	309,600	273,976
Short-term borrowed funds	8,633	7,904
Long-term debt	33,696	39,103
Interest payable	503	369
Other liabilities	1,196	1,385
Total liabilities	353,628	322,737
Off balance sheet items, commitments and contingencies (Note 11)		
SHAREHOLDERS' EQUITY		
Common stock, $1.25 par value: 20,000,000 shares authorized; shares issued and outstanding 7,423,550 and 7,138,686 shares, respectively	9,279	8,923
Additional paid-in capital	13,541	12,410
Unearned ESOP compensation	(859)	(914)
Undivided profits	7,502	6,706
Accumulated other comprehensive income	170	328
Total shareholders' equity	29,633	27,453
Total liabilities and shareholders' equity	$383,261	$350,190

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

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
Years Ended December 31, 2006, 2005 and 2004

	2006	2005	2004
	(in thousands, except share and per share data)		
Interest Income			
Loans, including fees	$ 21,959	$ 17,446	$ 14,468
Investment securities:			
US Treasury	98	98	102
US Government agencies and corporations	832	537	439
State and political subdivisions	679	653	717
Other	174	125	81
Interest-earning deposits with banks and federal funds sold	611	302	99
Total interest income	24,353	19,161	15,906
Interest Expense			
Interest checking and money market accounts	2,342	1,002	616
Savings deposits	734	580	322
Time deposits $100,000 and over	2,100	1,168	788
Other time deposits	3,091	1,723	950
Short-term borrowed funds	627	239	84
Long-term debt	1,808	1,918	1,974
Total interest expense	10,702	6,630	4,734
Net interest income	13,651	12,531	11,172
Provision for loan losses	298	755	2,092
Net interest income after provision for loan losses	13,353	11,776	9,080
Noninterest Income			
Service charges on deposit accounts	2,000	1,707	1,436
Other service fees and commissions	2,329	1,728	1,427
Gain(loss) on sale of securities	60	(16)	2
Income from mortgage loan sales	764	554	845
Other income	316	378	561
Total noninterest income	5,469	4,351	4,271
Noninterest Expense			
Salaries and employee benefits	9,130	8,002	7,155
Net occupancy expense	711	643	641
Equipment expense	618	639	665
Data processing costs	939	843	810
Other	4,520	3,960	4,026
Total noninterest expense	15,918	14,087	13,297
Income before taxes	2,904	2,040	54
Income taxes (benefit)	833	523	(199)
Net income	$ 2,071	$ 1,517	$ 253
Net income per common share			
Basic	$ 0.29	$ 0.21	$ 0.03
Diluted	$ 0.28	$ 0.20	$ 0.03
Weighted average common shares outstanding			
Basic	7,244,772	7,242,262	7,361,486
Diluted	7,354,229	7,418,773	7,533,839

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

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
Years Ended December 31, 2006, 2005 and 2004

	2006	2005 (in thousands)	2004
Net Income	$2,071	$1,517	$ 253
Other comprehensive income (loss):			
Unrealized gains (losses) on available for sale securities	(197)	(761)	(252)
Related tax effect	76	293	97
Reclassification of losses(gains) recognized in net income	(60)	16	(2)
Related tax effect	23	(6)	1
Total other comprehensive loss	(158)	(458)	(156)
Comprehensive income	$1,913	$1,059	$ 97

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

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
Years Ended December 31, 2006, 2005 and 2004

	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Unearned ESOP Compensation	Undivided Profits	Accumulated Other Comprehensive Income	Total
		(in thousands, except share and per share data)					
Balance, January 1, 2004	6,977,384	$8,721	$ 11,735	$ (1,012)	$ 7,465	$ 942	$27,851
Net income	—	—	—	—	253	—	253
Other comprehensive income	—	—	—	—	—	(156)	(156)
Release of ESOP shares	—	—	41	47	—	—	88
Common stock issued pursuant to:							
3% stock dividend	206,657	256	982	—	(1,238)	—	—
Stock options exercised	119,372	152	419	—	—	—	571
Tax benefit of stock options exercised	—	—	51	—	—	—	51
Repurchase of common stock	(245,658)	(307)	(1,185)	—	—	—	(1,492)
Cash paid—fractional shares	—	—	—	—	(11)	—	(11)
Balance, December 31, 2004	7,057,755	8,822	12,043	(965)	6,469	786	27,155
Net income	—	—	—	—	1,517	—	1,517
Other comprehensive income	—	—	—	—	—	(458)	(458)
Release of ESOP shares	—	—	33	51	—	—	84
Common stock issued pursuant to:							
3% stock dividend	206,730	258	1,013	—	(1,271)	—	—
Stock options exercised	71,227	89	258	—	—	—	347
Tax benefit of stock options exercised	—	—	31	—	—	—	31
Repurchase of common stock	(197,026)	(246)	(968)	—	—	—	(1,214)
Cash paid—fractional shares	—	—	—	—	(9)	—	(9)
Balance, December 31, 2005	7,138,686	8,923	12,410	(914)	6,706	328	27,453
Net income	—	—	—	—	2,071	—	2,071
Other comprehensive income	—	—	—	—	—	(158)	(158)
Release of ESOP shares	—	—	37	55	—	—	92
Common stock issued pursuant to:							
3% stock dividend	214,634	269	997	—	(1,266)	—	—
Stock options exercised	94,094	117	107	—	—	—	224
Tax benefit of stock options exercised	—	—	48	—	—	—	48
Repurchase of common stock	(23,864)	(30)	(115)	—	—	—	(145)
Cash paid—fractional shares	—	—	—	—	(9)	—	(9)
Stock compensation expense	—	—	57	—	—	—	57
Balance, December 31, 2006	7,423,550	$9,279	$ 13,541	$ (859)	$ 7,502	$ 170	$29,633

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

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
Years Ended December 31, 2006, 2005 and 2004

	2006	2005	2004
Cash flows from operating activities			
Net income	$ 2,071	$ 1,517	$ 253
Adjustments to reconcile net income to net cash			
Provided (used) by operating activities:			
Depreciation	625	646	610
Net amortization of security premiums/discounts	(41)	37	74
Provision for loan losses	298	755	2,092
Deferred income taxes	439	52	(472)
Stock compensation	57	—	—
Net realized (gain) loss on available for sale securities	(60)	16	(2)
Income from mortgage loan sales	(764)	(554)	(845)
Proceeds from sales of loans held for sale	39,038	29,162	44,090
Origination of loans held for sale	(38,734)	(29,058)	(42,960)
(Gain)loss on sale of premises, equipment and other assets	2	(76)	(16)
Increase in cash surrender value of life insurance	(184)	(155)	(190)
(Gain)loss on sales of foreclosed real estate	24	(12)	2
Loss on sale of other assets	7	—	—
Release of ESOP Shares	92	84	88
Net change in interest receivable	(250)	(252)	(118)
Net change in other assets	(174)	622	195
Net change in interest payable	134	67	19
Net change in other liabilities	(190)	316	162
Net cash provided by operating activities	2,390	3,167	2,982
Cash flows from investing activities			
Proceeds from sales, maturities and calls of securities available for sale	9,190	1,487	3,535
Purchase of securities available for sale	(11,480)	(8,777)	(4,678)
Net increase in loans	(17,165)	(14,332)	(24,076)
Proceeds from sale of premises, equipment and other assets	—	230	404
Purchase of premises and equipment	(813)	(776)	(857)
Proceeds from sales of foreclosed real estate	205	1,392	162
Net cash used by investing activities	(20,063)	(20,776)	(25,510)
Cash flows from financing activities			
Net increase in deposit accounts	35,624	27,037	34,376
Net increase (decrease) in short-term borrowed funds	729	(3,158)	(1,752)
Net decrease in long-term debt	(5,407)	(3,631)	(3,531)
Repurchases of common stock	(145)	(1,214)	(1,492)
Net proceeds from issuance of common stock	224	347	571
Tax benefit of stock options exercised	48	31	51
Cash paid for fractional shares	(9)	(9)	(11)
Net cash provided by financing activities	31,064	19,403	28,212
Increase in cash and cash equivalents	13,391	1,794	5,684
Cash and cash equivalents, beginning of period	21,369	19,575	13,891
Cash and cash equivalents, end of period	$ 34,760	$ 21,369	$ 19,575
Supplemental disclosures of cash flow information			
Interest paid	$ 10,568	$ 6,563	$ 4,715
Income taxes paid	687	241	434
Supplemental schedule of non-cash investing and financing activities			
Decrease in fair value of securities available for sale, net of tax	(158)	(456)	(156)
Loans transferred to foreclosed real estate	262	1,064	537

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

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1—Significant Accounting Policies

Nature of Business

Uwharrie Capital Corp (the "Company") was incorporated under North Carolina law for the purpose of becoming the holding company for Bank of Stanly ("Stanly"). On July 1, 1993, Stanly became a wholly-owned subsidiary of the Company through a one-for-one exchange of the common stock of Stanly for common stock of the Company.

Stanly was incorporated on September 28, 1983, under the laws of the State of North Carolina and began operations on January 26, 1984 in Albemarle, North Carolina. Deposits with Stanly are insured by the Federal Deposit Insurance Corporation ("FDIC"). Stanly is under regulation of both the FDIC and the North Carolina State Banking Commission. Through its five branch locations in Stanly County, Stanly provides a wide range of deposit accounts, commercial, consumer, home equity and residential mortgage loans, safe deposit boxes and automated banking.

In 1987, Stanly established a wholly-owned subsidiary, BOS Agency, Inc. ("BOS Agency"), which engages in insurance product sales. In 1989, Stanly established a second wholly-owned subsidiary, BOS Financial Corporation, for the purpose of conducting business as a broker/dealer in securities. During 1993, BOS Financial Corporation changed its name to The Strategic Alliance Corporation ("Strategic Alliance") and was registered as a broker/dealer by the National Association of Securities Dealers.

The Company formed a new subsidiary, Strategic Investment Advisors, Inc. ("SIA"), during 1999 to provide investment advisory and asset management services. This subsidiary is registered as an investment advisor with the Securities and Exchange Commission.

On January 19, 2000, the Company completed its acquisition of Anson BanCorp, Inc. and its subsidiary, Anson Savings Bank. The savings bank retained its North Carolina savings bank charter and became a wholly-owned subsidiary of Uwharrie Capital Corp as Anson Bank & Trust Company ("Anson"), operating out of its main office branch in Wadesboro.

On August 4, 2000, Stanly acquired another subsidiary, Gateway Mortgage, Inc. ("Gateway"), a mortgage origination company.

On April 10, 2003, the Company capitalized a new wholly-owned subsidiary bank, Cabarrus Bank & Trust Company ("Cabarrus"), located in Concord, North Carolina. As of that date, Cabarrus purchased two branch offices located in Cabarrus County from Stanly to begin its operation. Cabarrus operates as a commercial bank and provides a full range of banking services.

On April 7, 2004 Uwharrie Mortgage, Inc. was established as a subsidiary of the Company to serve in the capacity of trustee and substitute trustee under deeds of trust.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company, Stanly, Anson, Cabarrus, SIA and its indirectly-owned subsidiaries, BOS Agency, Strategic Alliance and Gateway. All significant intercompany transactions and balances have been eliminated in consolidation.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1—Significant Accounting Policies (Continued)

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses.

Cash and Cash Equivalents

For the purpose of presentation in the consolidated statements of cash flows, cash and cash equivalents are defined as those amounts included in the balance sheet captions "Cash and due from banks," "Interest-earning deposits with banks", and "Federal funds sold".

Investment Securities Held To Maturity

Investment securities classified as held to maturity are debt securities the Company has both the intent and ability to hold to maturity regardless of changes in market conditions, liquidity needs or changes in general economic conditions. These securities are carried at cost adjusted for amortization of premium and accretion of discount, computed by the interest method over their contractual lives. Declines in the fair value of individual held to maturity securities below their cost that are other than temporary would result in write-downs of the individual securities to their fair value. Such write-downs would be included in earnings as realized losses. The Company had no securities held to maturity at December 31, 2006 and 2005.

Investment Securities Available for Sale

Investment securities available for sale consist of bonds and notes not classified as trading securities nor as held to maturity securities. Unrealized holding gains and losses on available for sale securities are reported as a net amount in other comprehensive income, net of income taxes. Gains and losses on the sale of available for sale securities are determined using the specific identification method. Declines in the fair value of individual available for sale securities below their cost that are other than temporary would result in write-downs of the individual securities to their fair value. Such write-downs would be included in earnings as realized losses. Premiums and discounts are recognized in interest income using the interest method over the period to maturity.

Loans Held for Sale

Loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated fair value in the aggregate. Net unrealized losses, if any, are recognized through a valuation allowance by charges to income.

Loans

The Company grants mortgage, commercial and consumer loans to customers. The ability of the Company's borrowers to honor their contracts is largely dependent upon the real estate and general economic conditions in the Company's market area. Loans that management has the

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1—Significant Accounting Policies (Continued)

intent and ability to hold for the foreseeable future or until maturity or pay-off are reported at their outstanding unpaid principal balances adjusted for charge-offs, the allowance for loan losses, and any deferred fees or costs. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the related loan yield using the interest method.

The accrual of interest on mortgage and commercial loans is discontinued at the time the loan is 90 days delinquent unless the credit is well-secured and in process of collection. Credit card loans and other personal loans are typically charged off no later than 180 days past due. In all cases, loans are placed on nonaccrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

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

Allowance for Loan Losses

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management’s periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower’s ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available. In addition, regulatory examiners may require the Company to recognize adjustments to the allowance for loan loss based on their judgment about information available to them at the time of their assessment.

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

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1—Significant Accounting Policies (Continued)

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Company does not separately identify individual consumer, residential and other loans for impairment disclosures.

Servicing Assets

Servicing assets are recognized as separate assets when rights are acquired through purchase or through sale of financial assets. Capitalized servicing rights are reported in other assets and are amortized into other income in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets, which ranged from five to twelve years as of December 31, 2006. Servicing assets are evaluated for impairment based upon the fair value. Fair value is determined using prices for similar assets with similar characteristics, when available, or based upon discounted cash flows using market-based assumptions. Impairment is recognized through a valuation allowance.

Transfers of Financial Assets

Transfers of financial assets are accounted for as sales when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Foreclosed Real Estate

Real estate properties acquired through foreclosure or other proceedings are initially recorded at fair value upon foreclosure, establishing a new cost basis. After foreclosure, valuations are performed and the foreclosed property is adjusted to the lower of cost or fair market value of the properties, less costs to sell. Any write-down at the time of transfer to foreclosed properties is charged to the allowance for loan losses. Subsequent write-downs are charged to other expenses. Property is evaluated regularly to ensure that the recorded amount is supported by its current fair market value.

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation. Land is carried at cost. Additions and major replacements or betterments which extend the useful lives of premises and equipment are capitalized. Maintenance, repairs and minor improvements are expensed as incurred. Depreciation is computed principally by the straight-line method over estimated useful lives, except in the case of leasehold improvements, which are amortized over the term of the leases, if shorter. Useful lives range from five to seven years for furniture, fixtures and equipment to ten to thirty years for leasehold improvements and buildings, respectively. Upon retirement or other disposition of the assets, the cost and the related accumulated depreciation are removed from the accounts and any gains or losses are reflected in income.

Federal Home Loan Bank Stock

As a requirement for membership, the banks invest in the stock of the Federal Home Loan Bank of Atlanta (“FHLB”). This investment is carried at cost. Due to the redemption provisions of the FHLB, the Company estimated that fair value equals cost and that this investment was not impaired.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1—Significant Accounting Policies (Continued)

Goodwill

Goodwill resulted from the 2000 acquisition of Anson BanCorp, Inc. and its subsidiary, Anson Savings Bank. Effective with the adoption of SFAS No. 142 on January 1, 2002, the Company ceased to amortize this goodwill and began to evaluate it on an annual basis for impairment as provided for under SFAS No. 144.

Stock-Based Compensation

Effective January 1, 2006, the Company adopted Statement of Financial Accounting Standards No. 123R (revised 2004, "Share-Based Payment", ("SFAS No. 123R")) which was issued by the FASB in December 2004. SFAS No. 123R revises SFAS No. 123 "Accounting for Stock-Based Compensation" and supersedes APB Opinion No. 25 "Accounting for Stock Issued to Employees" (APB No. 25) and its related interpretations. SFAS No. 123R requires recognition of the cost of employee services received in exchange for an award of equity instruments in the financial statements over the period the employee is required to perform the services in exchange for the award (presumptively the vesting period). SFAS No. 123R also requires measurement of the cost of employee services received in exchange for an award based on the grant-date fair value of the award. SFAS No. 123R also amends SFAS No. 95 "Statement of Cash Flows", to require that excess tax benefits be reported as financing cash inflows, rather than as a reduction of taxes paid, which is included within operating cash flows.

The Company adopted SFAS No. 123R using the modified prospective application as permitted under SFAS No. 123R. Accordingly, prior period amounts have not been restated. Under this application, the Company is required to record compensation expense for all awards granted after the date of adoption and for the unvested portion of previously granted awards that remain outstanding at the date of adoption. Prior to the adoption of SFAS No. 123R, the Company used the intrinsic value method as prescribed by APB No. 25 and thus recognized no compensation expense for options granted with exercise prices equal to the fair market value of the common stock on the date of grant.

During 1996, the Company adopted the 1996 Incentive Stock Option Plan ("SOP") and the Employee Stock Purchase Plan ("SPP"), under which options to purchase shares of the Company's common stock may be granted to officers and eligible employees. Options granted under the SOP are exercisable in established increments according to vesting schedules, generally three to five years, and will expire if not exercised within ten years of the date of grant. Options granted under the SPP are fully vested at the date of grant and expire, if not exercised, within two years of the grant date. The compensation cost charged against income for those plans for the twelve months ended December 31, 2006 was $57 thousand.

The fair market value of each option award is estimated on the date of grant using the Black-Scholes option pricing model. There were 15,000 shares granted during 2006. The fair value at the grant date was $1.55 using the following assumptions; a risk-free interest rate of 4.5%, a dividend yield of 0%, an expected life equal to 70% of the term of the option, and a volatility rating of 14%. There were three grants for 87,191 shares during the twelve months ended December 31, 2005. The average fair value at the grant date was $1.43 using the following assumptions; a risk-free interest rate of 3.5%, a dividend yield of 0%, an expected life equal to 70% of the term of the option, and a volatility rating of 14%.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1—Significant Accounting Policies (Continued)

The following is a summary of stock option activity for the twelve months ended December 31, 2006:

	Shares	Weighted Average Price	Aggregate Intrinsic (in thousands)
Outstanding at December 31, 2005	683,154	$ 4.45	
Granted	15,000	6.15	
Exercised	(96,782)	2.32	
Forfeited	(81,425)	5.48	
Outstanding at December 31, 2006	519,947	4.73	$ 530
Options exercisable at December 31, 2006	441,041	4.58	516

A summary of the status of the Company's non-vested stock options as of December 31, 2006, and changes during the year then ended is presented below:

	Shares	Weighted Average Grant Date Fair Value
Non-vested December 31, 2005	158,111	$ 1.46
Granted	15,000	1.55
Vested	(44,428)	1.40
Forfeited	(49,777)	1.54
Non-vested December 31, 2006	78,906	1.41

The fair value of stock options vested over the twelve months ended December 31, 2006 and 2005 was $64 thousand and $101 thousand, respectively.

As of December 31, 2006, there was $93 thousand of total unrecognized compensation cost related to non-vested share-based compensation arrangements granted under all of the Company's stock benefit plans. That cost is expected to be recognized over a weighted-average period of 2.7 years.

The Company funds the option shares from authorized but unissued shares. The Company does not typically purchase shares to fulfill the obligations of the stock benefit plans. Company policy does allow option holders to exercise options with seasoned shares.

The adoption of SFAS 123R and its fair value compensation cost recognition provisions are different from the non-recognition provisions under SFAS 123 and the intrinsic value method for compensation cost allowed under APB 25. The effect (increase/(decrease)) of the adoption of SFAS 123R is as follows:

	December 31, 2006
Income before income tax expense	(57)
Net Income	(57)
Cash flow from operating activities	57
Cash flow provided by financing activities	48
Basic earnings per share	—
Diluted earnings per share	(.01)

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1—Significant Accounting Policies (Continued)

For the twelve months ended December 31, 2006 and 2005, the intrinsic value of options exercised was $332 thousand and $114 thousand, respectively.

The following illustrates the effect on net income available to common stockholders if the Company had applied the fair value recognition provisions of SFAS No. 123 to the results for the twelve months ended December 31, 2005 and 2004 (in thousands, except per share data):

	2005	2004
Net income as reported	$1,517	$253
Add: Stock-based employee compensation expenses included in reported net income, net of related income tax effects	—	—
Less: Stock-based compensation determined under fair value based method of all awards, net of related income taxes	(136)	(77)
Net income, pro forma	$1,381	$176
Net income per share:		
Basic net income per common share		
As reported	$ .21	$ .03
Pro forma	.19	.02
Diluted net income per share		
As reported	.20	.03
Pro forma	.19	.02

Income Taxes

The Company and its subsidiaries file a consolidated Federal income tax return and separate North Carolina income tax returns. The provision for income taxes in the accompanying consolidated financial statements is provided on a liability method whereby deferred tax assets are recognized for deductible temporary differences and operating loss and tax credit carryforwards and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1—Significant Accounting Policies (Continued)

Fair Value of Financial Instruments

SFAS No. 107, Disclosures About Fair Value of Financial Instruments, requires disclosure of fair value information about financial instruments, whether or not recognized in the consolidated balance sheets, for which it is practicable to estimate that value. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. In that regard, the derived fair value estimates cannot be substantiated by comparison to independent markets and, in many cases, could not be realized in immediate settlement of the instrument. Statement No. 107 excludes certain financial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented do not represent the underlying market value or liquidation value of the Company.

The following methods and assumptions were used by the Company in estimating the fair value of its financial instruments:

Carrying amounts approximate fair values for cash and due from banks; interest-bearing deposits with banks; federal funds sold; interest receivable and payable; variable rate loans that reprice frequently where no significant change in credit risk has occurred; bank owned life insurance; Federal Home Loan Bank stock; variable rate money market, demand, interest checking and savings accounts; variable rate time deposits; federal funds purchased and securities sold under repurchase agreements and short-term borrowed funds.

Quoted market prices, where available, or if not available, quoted market prices of comparable instruments are used for investment securities.

Discounted cash flows using interest rates currently being offered on instruments with similar terms and with similar credit quality are used for long-term debt; all loans (except variable rate loans described above) and fixed rate time deposits.

Comprehensive Income

The Company reports as comprehensive income all changes in shareholders' equity during the year from sources other than shareholders. Other comprehensive income refers to all components (revenues, expenses, gains, and losses) of comprehensive income that are excluded from net income. The Company's only component of other comprehensive income is unrealized gains and losses, net of income tax, on investment securities available for sale.

Earnings per Common Share

The Company issued 3% stock dividends in 2006, 2005 and 2004. All references in these consolidated financial statements to earnings per common share and weighted average common and common equivalent shares outstanding have been adjusted for the effect of these stock dividends. In 2006, there were 15,000 stock options outstanding that were antidilutive since the exercise price exceeded the average market price. There were no anti-dilutive stock options outstanding during 2005 or 2004.

Basic earnings per share (“EPS”) excludes dilution and is computed by dividing income available to common shareholders by the weighted-average number of common shares

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1—Significant Accounting Policies (Continued)

outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the entity. The computation of basic and dilutive earnings per share is summarized below:

	2006	2005	2004
Weighted average number of common shares used in computing basic net income per common share	7,244,772	7,242,262	7,361,486
Effect of dilutive stock options	109,457	176,511	172,353
Weighted average number of common shares and dilutive potential common shares used in computing diluted net income per common share	7,354,229	7,418,773	7,533,839

Recent Accounting Pronouncements

FIN 48

In July 2006, the FASB issued Financial Interpretation No. 48, “Accounting for Uncertainty in Income Taxes—an interpretation of FASB Statement No. 109” (“FIN 48”), which is a change in accounting for income taxes. FIN 48 specifies how tax benefits for uncertain tax positions are to be recognized, measured, and derecognized in financial statements; requires certain disclosures of uncertain tax matters; specifies how reserves for uncertain tax positions should be classified on the balance sheet; and provides transition and interim period guidance, among other provisions. FIN 48 is effective for fiscal years beginning after December 15, 2006 and as a result, is effective for the Company in the first quarter of fiscal 2007. We currently believe that the adoption of FIN 48 will not have a material financial impact on our consolidated financial statements.

SAB 108

In September 2006, the SEC staff issued SAB No. 108, Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in the Current Year Financial Statements *(SAB No. 108)*. SAB No. 108 addresses the diversity in practice by registrants when quantifying the effect of an error on the financial statements. SAB No. 108 provides guidance on the consideration of the effects of prior year misstatements in quantifying current year misstatements and is effective for annual periods ending after November 15, 2006. The Company will be required to adopt the provisions of SAB No. 108 effective December 31, 2006. We currently believe that the adoption of SAB 108 will not have a material financial impact on our consolidated financial statements.

FAS 156

In March 2006, the FASB issued Statement of Financial Accounting Standards No. 156, “Accounting for Servicing of Financial Assets – an amendment of FASB Statement No. 140” which is effective for fiscal years beginning after September 15, 2006. This statement was issued to simplify the accounting for servicing rights and to reduce the volatility that results from using different measurement attributes. We currently believe that the adoption of FAS 156 will not have a material financial impact on our consolidated financial statements.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1—Significant Accounting Policies (Continued)

SFAS No. 158

Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans. This statement requires recognition on the balance sheet of a plan's overfunded or underfunded status with an offset to comprehensive income. This statement also requires, with limited exceptions, that the funded status of the plan be determined as of the employer's fiscal year end. The balance sheet recognition provisions of SFAS 158 are effective for entities with publicly traded equity securities for years ending after December 15, 2006 and for all other entities for years ending after June 15, 2007. The Company does not anticipate that this statement will have an impact on the Company's financial position, results of operations and cash flows.

EITF 06-4

The Emerging Issues Task Force (EITF) reached a consensus at its September 2006 meeting regarding EITF 06-4, Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements. The scope of EITF 06-4 is limited to the recognition of a liability and related compensation costs for endorsement split-dollar life insurance policies that provide a benefit to an employee that extends to postretirement periods. Therefore, this EITF would not apply to a split-dollar life insurance arrangement that provides a specified benefit to an employee that is limited to the employee's active service period with an employer. This EITF 06-4 is effective for fiscal years beginning after December 15, 2007, with earlier application permitted. The effects of this EITF have not yet been evaluated.

EITF 06-5

The EITF reached a consensus at its September 2006 meeting regarding EITF 06-5, Accounting for Purchases of Life Insurance Determining the Amount That Could be Realized in Accordance with FASB Technical Bulletin No. 85-4. The scope of EITF 06-5 is limited to the determination of net cash surrender value of a life insurance contract in accordance with Technical Bulletin 85-4. This EITF outlines when contractual limitations of the policy should be considered when determining the net realizable value of the contract. EITF 06-5 is effective for fiscal years beginning after December 15, 2006, with earlier application permitted. The Company has not yet evaluated the effects of this EITF.

From time to time the FASB issues exposure drafts for proposed statements of financial accounting standards. Such exposure drafts are subject to comment from the public, to revisions by the FASB and to final issuance by the FASB as statements of financial accounting standards. Management considers the effect of the proposed statements on the consolidated financial statements of the Company and monitors the status of changes to and proposed effective dates of exposure drafts.

Reclassification

Certain amounts in the 2005 and 2004 financial statements have been reclassified to conform to the 2006 presentation. The reclassifications had no effect on net income or shareholders' equity as previously reported.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 2—Investment Securities

Carrying amounts and fair values of securities available for sale are summarized below:

December 31,2006	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
		(dollars in thousands)		
U.S. Treasury	$ 2,992	$ —	$ 78	$ 2,914
U.S. Government agencies	7,509	—	149	7,360
Mortgage-backed securities and CMO's	12,918	38	50	12,906
State and political subdivisions	12,931	521	26	13,426
Corporate bonds	514	6	—	520
Total debt securities	36,864	565	303	37,126
Equity securities	8	16	—	24
Total securities available for sale	$ 36,872	$ 581	$ 303	$37,150

December 31,2005	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
		(dollars in thousands)		
U.S. Treasury	$ 2,988	$ —	$ 87	$ 2,901
U.S. Government agencies	9,850	72	184	9,738
Mortgage-backed securities and CMO's	5,773	38	26	5,785
State and political subdivisions	12,856	735	34	13,557
Commercial paper	2,480	—	—	2,480
Corporate bonds	527	9	—	536
Total debt securities	34,474	854	331	34,997
Equity securities	8	11	—	19
Total securities available for sale	$ 34,482	$ 865	$ 331	$35,016

Results from sales of securities available for sale for the years ended December 31, 2006, 2005 and 2004 are as follows:

	2006	2005	2004
	(dollars in thousands)		
Gross proceeds from sales	$2,885	$1,295	$263
Realized gains from sales	$ 60	$ 4	$ 2
Realized losses from sales	—	(20)	—
Net realized gains (losses)	$ 60	$ (16)	$ 2

At December 31, 2006, 2005 and 2004 securities available for sale with a carrying amount of $16.9 million, $13.1 million and $12.8 million, respectively, were pledged as collateral on public deposits and for other purposes as required or permitted by law.

The following tables show the gross unrealized losses and fair value of investments, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2006 and 2005. These unrealized losses on investment securities are a result of temporary fluctuations in the market prices due to a rise in interest rates, which will adjust if rates decline, and are in no way a reflection of the quality of the investments. At December 31, 2006 the unrealized losses related to three U.S. Treasuries, eight U.S. Government agencies, thirteen mortgage backed securities and CMOs, and nine state and political subdivisions. All unrealized losses on investment securities are considered by management to be temporary given the credit ratings on these investment securities and plans to hold these investments until maturity.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 2—Investment Securities (Continued)

	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
			(dollars in thousands)			
December 31, 2006						
Securities available for sale:						
U.S. Treasury	$ —	$ —	$ 2,992	$ 78	$ 2,992	$ 78
U.S. Government agencies	—	—	7,360	149	7,360	149
Mortgage-backed securities and CMO's	7,391	38	1,684	12	9,075	50
State and political subdivisions	1,025	16	1,464	10	2,489	26
	$ 8,416	$ 54	$ 13,500	$ 249	$ 21,916	$ 303
December 31, 2005						
Securities available for sale:						
U.S. Treasury	$ —	$ —	$ 2,902	$ 87	$ 2,902	$ 87
U.S. Government agencies	2,497	36	4,841	148	7,338	184
Mortgage-backed securities and CMO's	4,034	26	—	—	4,034	26
State and political subdivisions	1,445	34	—	—	1,445	34
	$ 7,976	$ 96	$ 7,743	$ 235	$ 15,719	$ 331

Note 3—Loans

The composition of net loans as of December 31, 2006 and 2005 is as follows:

	2006	2005
	(dollars in thousands)	
Commercial	$ 36,406	$ 37,299
Real estate—construction	27,342	21,206
Real estate—residential	126,111	116,715
Real estate—commercial	84,744	83,861
Consumer	13,262	13,479
Loans held for sale	3,814	3,354
Other	133	72
	291,812	275,986
Less:		
Allowance for loan losses	(3,171)	(4,482)
Deferred loan fees, net	137	210
Loans, net	$288,778	$271,714

Although the subsidiary banks' loan portfolios are diversified, there is a concentration of mortgage real estate loans, primarily one to four family residential mortgage loans, which represent 43.69% of net loans. Additionally, there is concentration in commercial loans secured primarily by real estate, to finance manufacturing buildings, shopping center locations, commercial land development, commercial buildings and equipment that comprise 29.35% of net loans. There is not a concentration of a particular type of credit in this group of commercial loans.

Impaired loans, which consisted of nonaccrual loans and other loans identified by management as impaired, totaled $3.1 million and $3.8 million at December 31, 2006 and 2005, respectively. The nonaccrual status of these loans had the effect of reducing net income by $72,800 in 2006 and $106,670 in 2005. Of the nonaccrual amount in 2006 and 2005, a total of $36,628 was government guaranteed as to principal in 2005. The allowance for impaired loans amounted to $889,000 at December 31, 2006 and $1.6 million at December 31, 2005. At December 31, 2006 and 2005, loans past due 90 days and still accruing interest totaled $499,982 and $338,724,

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 3—Loans (Continued)

respectively. Restructured loans, excluding those included in impaired loans, amounted to $631,000 at December 31, 2006. The carrying value of foreclosed properties held as other real estate was $202,976 and $169,466 at December 31, 2006 and 2005, respectively.

The Company's loan policies are written to address loan-to-value ratios and collateralization methods with respect to each lending category. Consideration is given to the economic and credit risk of lending areas and customers associated with each category.

Note 4—Allowance for Loan Losses

Changes in the allowance for loan losses for the years ended December 31, 2006, 2005 and 2004 are presented below:

	2006	2005	2004
	(dollars in thousands)		
Balance, beginning of year	$ 4,482	$ 4,983	$3,224
Charge-offs	(1,687)	(1,378)	(373)
Recoveries	78	122	40
Provision charged against income	298	755	2,092
Balance, end of year	$ 3,171	$ 4,482	$4,983

Note 5—Servicing Assets

Loans serviced for others are not included in the accompanying consolidated balance sheets. The unpaid principal balances of mortgage and other loans serviced for others were approximately $186 million and $167 million at December 31, 2006 and 2005, respectively. The carrying value of capitalized servicing rights, net of valuation allowances, is included in other assets. A summary of mortgage servicing rights follows:

	2006	2005	2004
	(dollars in thousands)		
Beginning of year mortgage servicing rights:	$1,138	$1,236	$1,233
Amounts capitalized	488	292	374
Amortization	(382)	(390)	(371)
End of year	$1,244	$1,138	$1,236

Amortization expense for each of the next five years is estimated to be as follows:

Year ending December 31, (dollars in thousands)	
2007	$ 294
2008	254
2009	215
2010	175
2011	136
Total	$1,074

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 6—Premises and Equipment

The major classes of premises and equipment and the total accumulated depreciation at December 31, 2006 and 2005 are listed below:

	2006	2005
	(dollars in thousands)	
Land	$ 2,785	$ 2,280
Building and improvements	6,280	6,220
Furniture and equipment	4,740	4,609
	13,805	13,109
Less accumulated depreciation	5,187	4,677
Total	$ 8,618	$ 8,432

Note 7—Deposits

The composition of deposits at December 31, 2006 and 2005 is as follows:

	2006		2005	
	Amount	Percentage of Total	Amount	Percentage of Total
	(dollars in thousands)			
Demand deposits	$ 48,149	16%	$ 47,280	17%
Interest checking and money market	101,470	32%	83,680	31%
Savings	27,833	9%	36,689	13%
Time deposits $100,000 and over	48,450	16%	38,881	14%
Other time deposits	83,698	27%	67,446	25%
Total	$309,600	100%	$273,976	100%

The maturities of fixed-rate time deposits at December 31, 2006 are reflected in the table below.

Year ending December 31,	Time Deposits $100,000 and Over	Other Time Deposits
	(dollars in thousands)	
2007	$45,782	$73,686
2008	2,105	7,339
2009	145	844
2010	300	1,580
2011	118	212
Thereafter	—	37
Total	$48,450	$83,698

Note 8—Short-Term Borrowed Funds

The following tables set forth certain information regarding the amounts, year-end weighted average rates, average balances, weighted average rate, and maximum month-end balances for short-term borrowed funds, at and during 2006 and 2005.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 8—Short-Term Borrowed Funds (Continued)

	2006 Amount	2006 Rate	2005 Amount	2005 Rate
At year-end				
Securities sold under repurchase agreements	$ 2,025	4.31%	$3,449	3.84%
Master notes	6,608	4.34%	4,455	3.60%
	$ 8,633	4.33%	$7,904	3.70%

	2006 Amount	2006 Rate	2005 Amount	2005 Rate
	(dollars in thousands)			
Average for the year				
Federal funds purchased	$ 1,478	5.10%	$ 231	3.33%
Securities sold under repurchase agreements	2,980	4.33%	2,920	2.50%
Master notes	7,692	4.29%	5,008	2.92%
Short-term advances from FHLB	1,381	5.40%	406	2.84%
	$13,531	4.50%	$8,565	2.78%

	2006	2005
	(dollars in thousands)	
Maximum month-end balance		
Federal Funds purchased	$11,000	$2,500
Securities sold under repurchase agreements	3,439	3,872
Master notes	11,007	8,135
Short-term advances from FHLB	7,000	2,000

Federal funds purchased represent unsecured overnight borrowings from other financial institutions. Securities sold under repurchase agreements represent short-term borrowings collateralized by securities of the United States government or its agencies. Master notes represent an overnight investment in commercial paper issued by the Company to customers of it's subsidiary banks, where an agreement is in place.

The subsidiary banks have combined available lines of credit for federal funds in the amount of $18.7 million at December 31, 2006.

Note 9—Long-Term Debt

The Company has a line of credit with the Federal Home Loan Bank secured by qualifying first lien and second mortgage loans and commercial real estate loans with eligible collateral value of $74.9 million at December 31, 2006. The long-term advances under this line amounted to $26.4 million and $31.4 million at December 31, 2006 and 2005, respectively. Interest rates ranged from 2.96% to 7.52% in 2006 and from 2.64% to 7.52% in 2005. Two subsidiary banks also have standby letters of credit issued by the Federal Home Loan Bank to be used as collateral for public funds deposits. The amount of the letters of credit was $14.0 million at December 31, 2006.

On April 30, 2001, the Company borrowed $4.0 million from a bank at an interest rate of prime less one percent. The note is payable in annual installments of $400 thousand. The balance outstanding at December 31, 2006 and 2005 was $2.0 million and $2.4 million, respectively.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 9—Long-Term Debt (Continued)

The Company issued $5.2 million of junior subordinated debentures to Uwharrie Statutory Trust 1 in exchange for the proceeds of the trust preferred securities issued by the Trust. The junior subordinated debentures are included in long-term debt and the Company's equity interest in the trust is included in other assets. The junior subordinated debentures pay interest quarterly at an annual rate, reset quarterly, equal to LIBOR plus 3.40%. The debentures are redeemable on September 26, 2007 or afterwards, in whole or in part, on March 26, June 26, September 26 or December 26 of each subsequent year through maturity at September 26, 2032. The Company fully and unconditionally guarantees the trust preferred securities through the combined operation of the junior subordinated debentures and other related documents. The Company's obligation under the guarantee is unsecured and subordinate to senior and subordinated indebtedness of the Company.

The trust preferred securities presently qualify as Tier 1 regulatory capital and are reported in Federal Reserve regulatory reports as a minority interest in a consolidated subsidiary. The junior subordinated debentures do not qualify as Tier 1 regulatory capital. On March 1, 2005, the Board of Governors of the Federal Reserve adopted a final rule that allows the continued limited inclusion of trust preferred securities in Tier 1 capital. The final rule limits trust preferred securities to 25 percent of all core capital elements, net of goodwill. Amounts of restricted core capital elements in excess of these limits generally may be included in Tier 2 capital. The final rule provides a five-year transition period, ending March 31, 2009, for application of the quantitative limits.

On November 19, 2002, the Company executed a mortgage in the amount of $129,000 for the purchase of property for branch expansion. This loan bears interest at 6.00% and is to be paid in 60 quarterly installments of $3,277. The outstanding principal balance on this note was $104,963 at December 31, 2006.

As of December 31, 2006, the scheduled maturities of these advances, junior subordinated debentures, and notes payable are as follows:

Year ending December 31, (dollars in thousands)	
2007	$ 4,407
2008	14,844
2009	1,408
2010	2,408
2011	5,409
Thereafter	5,220
Total	$33,696

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 10—Income Tax Matters

The significant components of income tax expense for the years ended December 31 are summarized as follows:

	2006	2005	2004
	(dollars in thousands)		
Current tax expense:			
Federal	$217	$379	$ 123
State	177	92	150
Total	394	471	273
Deferred tax expense (benefit):			
Federal	343	38	(392)
State	96	14	(80)
Total	439	52	(472)
Net provision (benefit) for income taxes	$833	$523	$(199)

The difference between the provision for income taxes and the amounts computed by applying the statutory federal income tax rate of 34% to income before income taxes is summarized below:

	2006	2005	2004
	(dollars in thousands)		
Tax computed at the statutory federal rate	$ 987	$ 693	$ 18
Increases (decrease) resulting from:			
Tax exempt interest, net	(245)	(224)	(290)
State income taxes, net of federal benefit	143	70	102
Other	(52)	(16)	(29)
Provision (benefit) for income taxes	$ 833	$ 523	$(199)

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of deferred taxes at December 31, are as follows:

	2006	2005	2004
	(dollars in thousands)		
Deferred tax assets relating to:			
Allowance for loan losses	$ 912	$1,496	$ 1,740
Deferred compensation	316	279	233
Other	236	130	33
Valuation allowance	(12)	(8)	(6)
Total deferred tax assets	$1,452	$1,897	$ 2,000
Deferred tax liabilities relating to:			
Net unrealized gain on securities available for sale	$ (107)	$ (206)	$ (493)
Property and equipment	(364)	(392)	(460)
Deferred loans fees and costs	(212)	(218)	(206)
Loan servicing	(71)	(60)	(70)
Prepaid expenses	(96)	(79)	(64)
Total deferred tax assets	(850)	(955)	(1,293)
Net recorded deferred tax asset	$ 602	$ 942	$ 707

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 10—Income Tax Matters (Continued)

The net deferred tax asset is included in other assets on the accompanying consolidated balance sheets.

Note 11—Commitments and Contingencies

Financial Instruments with Off-Balance Sheet Risk

The subsidiary banks are parties to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of their customers. These financial instruments include commitments to extend credit, lines of credit and standby letters of credit. These instruments involve elements of credit risk in excess of amounts recognized in the accompanying financial statements.

The subsidiary banks' risks of loss with the unfunded loans and lines of credit or standby letters of credit are represented by the contractual amount of these instruments. The banks use the same credit policies in making commitments under such instruments as they do for on-balance sheet instruments. The amount of collateral obtained, if any, is based on management's credit evaluation of the borrower. Collateral held varies, but may include accounts receivable, inventory, real estate and time deposits with financial institutions. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Credit card commitments are unsecured. As of December 31, 2006 and 2005, outstanding financial instruments whose contract amounts represent credit risk were as follows:

	2006	2005
	(dollars in thousands)	
Commitments to extend credit	$73,450	$61,579
Credit card commitments	7,672	7,443
Standby letters of credit	616	463
	$81,738	$69,485

Contingencies

In the normal course of business, the Company is involved in various legal proceedings. In the opinion of management, any liability resulting from such proceedings would not have a material adverse effect on the consolidated financial statements.

Financial Instruments with Concentration of Credit Risk

The bank subsidiaries make commercial, agricultural, real estate mortgage, home equity and consumer loans primarily in Stanly, Anson and Cabarrus counties. A substantial portion of the Company's customers' ability to honor their contracts is dependent on the economy in these counties.

Although the Company's composition of loans is diversified, there is some concentration of mortgage loans in the total portfolio. The Bank Policy is to abide by real estate loan-to-value margin limits corresponding to guidelines issued by the federal supervisory agencies on March 19, 1993. Lending policy for all loans requires that they be supported by sufficient cash flows. Credit losses related to this real estate concentration are consistent with credit losses experienced in the portfolio as a whole.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 12—Related Party Transactions

The Company has granted loans to certain directors and executive officers and their related interests. Such loans are made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other borrowers and, in management's opinion, do not involve more than the normal risk of collectibility. All loans to directors and executive officers or their interests are submitted to the Board of Directors for approval. A summary of loans to directors, executive officers and their related interests follows; (dollars in thousands)

Balance at December 31, 2005	$15,623
Disbursements during the year	13,902
Collections during the year	5,438
Balance at December 31, 2006	$24,086

At December 31, 2006, the Company had approved, but unused lines of credit totaling $4.6 million to executive officers, directors, officer and their related interests.

Note 13—Regulatory Matters

The Company, and its bank subsidiaries, are subject to certain requirements imposed by state and federal banking statutes and regulations. These requirements, among other things, establish minimum levels of capital, restrict the amount of dividends that may be distributed, and require that reserves on deposit liabilities be maintained in the form of vault cash or noninterest-bearing deposits with the Federal Reserve Bank.

The Company and its subsidiary banks are subject to federal regulatory risk-based capital guidelines for banks and bank holding companies. Each must meet specific capital guidelines that involve quantitative measure of assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices which measure Total and Tier 1 Capital to risk-weighted assets and Tier 1 Capital to average assets. Quantitative measures established by regulation to ensure capital adequacy and the Company's consolidated capital ratios are set forth in the table below. The Company expects to meet or exceed these minimums without altering current operations or strategy.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 13—Regulatory Matters (Continued)

	Actual		Minimum For Capital Requirement		Minimum to Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
	(Dollars in thousands)					
December 31, 2006						
Total Capital to risk						
Weighted Assets:						
Consolidated	$36,778	12.7%	$ 23,107	8.00%	$28,884	10.00%
Bank of Stanly	25,731	13.3%	15,406	8.00%	19,258	10.00%
Anson Bank and Trust	4,320	13.5%	2,563	8.00%	3,203	10.00%
Cabarrus Bank and Trust	7,013	11.0%	5,116	8.00%	6,395	10.00%
Tier I Capital to Risk						
Weighted Assets:						
Consolidated	33,601	11.6%	11,554	4.00%	17,330	6.00%
Bank of Stanly	23,402	12.2%	7,703	4.00%	11,555	6.00%
Anson Bank and Trust	3,983	12.4%	1,281	4.00%	1,922	6.00%
Cabarrus Bank and Trust	6,502	10.2%	2,558	4.00%	3,837	6.00%
Tier I Capital to						
Average Assets:						
Consolidated	33,601	8.8%	15,249	4.00%	19,061	5.00%
Bank of Stanly	23,402	9.0%	10,457	4.00%	13,072	5.00%
Anson Bank and Trust	3,983	8.8%	1,856	4.00%	2,320	5.00%
Cabarrus Bank and Trust	6,502	8.1%	3,223	4.00%	4,029	5.00%
December 31, 2005						
Total Capital to risk						
Weighted Assets:						
Consolidated	$34,538	12.8%	$ 21,650	8.00%	$27,062	10.00%
Bank of Stanly	23,284	12.2%	15,243	8.00%	19,054	10.00%
Anson Bank and Trust	4,246	15.7%	2,170	8.00%	2,712	10.00%
Cabarrus Bank and Trust	6,790	13.2%	4,120	8.00%	5,150	10.00%
Tier I Capital to Risk						
Weighted Assets:						
Consolidated	31,137	11.5%	10,825	4.00%	16,237	6.00%
Bank of Stanly	20,887	11.0%	7,622	4.00%	11,432	6.00%
Anson Bank and Trust	3,908	14.4%	1,085	4.00%	1,627	6.00%
Cabarrus Bank and Trust	6,143	11.9%	2,060	4.00%	3,090	6.00%
Tier I Capital to						
Average Assets:						
Consolidated	31,137	9.0%	13,784	4.00%	17,230	5.00%
Bank of Stanly	20,887	8.5%	9,826	4.00%	12,282	5.00%
Anson Bank and Trust	3,908	10.4%	1,513	4.00%	1,904	5.00%
Cabarrus Bank and Trust	6,143	9.6%	2,553	4.00%	3,191	5.00%

As of December 31, 2006, the most recent notification from the Federal Deposit Insurance Corporation categorized all subsidiary banks as being well capitalized under the regulatory framework for prompt corrective action. There have been no conditions or events since such notification that management believes would have changed the categorizations.

For the reserve maintenance period in effect at December 31, 2006, the subsidiary banks were required to maintain reserve balances in cash or on deposit with the Federal Reserve Bank in the aggregate amount of $4.0 million as reserves on deposit liabilities.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 14—Stock Matters

Employee Stock Plans

During 1996, the Company adopted the 1996 Employment Stock Option Plan ("SOP") and the Employee Stock Purchase Plan ("SPP"), under which options to purchase shares of the Company's common stock may be granted to officers and eligible employees. Options granted under the SOP are exercisable in established increments according to vesting schedules, generally three to five years, and will expire if not exercised within ten years of the date of grant. Options granted under the SPP are fully vested at the date of grant and expire if not exercised within two years of the grant date.

Activity under all option plans, reflecting the effects of the 3% stock dividends issued in 2006, 2005 and 2004, are as follows:

	2006		2005		2004	
	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
Options outstanding at the beginning of the year	683,154	$ 4.45	702,368	$ 4.35	781,491	$ 4.21
Options granted	15,000	6.15	87,191	5.44	75,533	5.67
Options exercised	(96,782)	2.32	(73,364)	4.60	(132,458)	3.35
Forfeitures	(81,425)	5.48	(33,041)	4.74	(22,198)	4.22
Options outstanding at the end of the year	519,947	$ 4.73	683,154	$ 4.45	702,368	$ 4.35
Options exercisable at the end of the year	441,041	$ 4.58	525,043	$ 4.15	508,344	$ 3.92

At December 31, 2006, options outstanding had a weighted-average remaining term of 4.2 years. Total options outstanding at December 31, 2006 included 519,947 options exercisable at a range of $2.82 to $6.12 per share. Exercisable options at December 31, 2006 included 441,041 options exercisable at a range of $2.82 to $5.67 per share. At December 31, 2006, authorized shares of common stock reserved for future grants of options totaled 142,726 under the SOP, and 128,944 under the SPP.

Stock Repurchase Program

On February 21, 1995, the Company's Board of Directors authorized and approved a Stock Repurchase Program, to be reaffirmed annually, pursuant to which the Company may repurchase shares of the Company's common stock for the primary purpose of providing liquidity to its shareholders. Pursuant to stock repurchase authorizations and limitations, the Company purchased 23,864 shares during 2006 and 197,026 shares during 2005 at an aggregate purchase price of $145,093 and $1,214,461, respectively.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 15—Employee and Director Benefit Plans

Employees' Savings Plus and Profit Sharing Plan

The Company has established an associate tax deferred savings plan under Section 401(k) of the Internal Revenue Code of 1986. All associates who are scheduled to work 500 hours or more are eligible to participate upon completion of six months of employment.

The Company's annual contribution to the plan was $169,982 in 2006, $143,210 in 2005 and $129,918 in 2004, determined as follows:

- A matching contribution equivalent to 50% of the first 6% of each associate's compensation contributed to the plan.
- A discretionary contribution, subject to approval by the Board of Directors, limited to an amount not to exceed the maximum amount deductible for income tax purposes.

Directors' Deferred Compensation Plan

On March 1, 1994, the Company established a Directors' Deferred Compensation Plan in accordance with the laws of the State of North Carolina under which each Director could elect to defer receipt for services rendered to the Company as a Director during the term of his or her service by entering into a written deferred compensation election. This plan was closed to new participants in 2001; subsequently, only two directors continue to defer receipt of fees. The balance in deferred directors' compensation, not yet disbursed, was $212,382 and $215,546 at December 31, 2006 and 2005, respectively. Expense for the years then ended was $12,283, $13,931 and $13,501, respectively.

Employee Stock Ownership Plan

The Company established an Employee Stock Ownership Plan ("ESOP") to benefit all qualified employees. The ESOP purchased 268,335 dividend adjusted shares of common stock in 1999 with proceeds received from a loan of $1.2 million from the Company. The loan is to be repaid over eighteen years with interest at 8%. The loan may be prepaid without penalty. The unallocated shares of stock held by the ESOP are pledged as collateral for the loan. The ESOP is funded by contributions made by the Company and its subsidiaries in amounts sufficient to retire the debt. At December 31, 2006, the outstanding balance of the loan is $859,174 and is presented as a reduction of shareholders' equity.

Shares released as the debt is repaid and earnings from the common stock held by the ESOP are allocated among active participants on the basis of compensation in the year of allocation. Benefits vest 100% as they are allocated to participants. Dividends on unallocated shares may be used by the ESOP to repay the loan to the Company and are not reported as dividends in the financial statements. Dividends on allocated or committed to be allocated shares are credited to the accounts of the participants and reported as dividends in the consolidated financial statements.

Expenses of $237,022, $251,437 and $245,240 during the years ended December 31, 2006, 2005 and 2004, respectively, have been incurred in connection with the ESOP. At December 31, 2006, 134,459 shares held by the ESOP have been released or committed to be released to the ESOP's participants for purposes of computing earnings per share. The fair value of the unallocated shares amounted to approximately $900 thousand at December 31, 2006.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 15—Employee and Director Benefit Plans (Continued)

Supplemental Executive Retirement Plan

The Company has implemented a non-qualifying deferred compensation plan for certain executive officers. The Company has purchased life insurance policies in order to provide future funding of benefit payments. Certain of the plan benefits will accrue and vest during the period of employment, and will be paid in fixed monthly benefit payments from ten to fifteen years commencing with the officer's retirement at any time after attainment of the age specified in the officer's plan agreement. Other benefits will accrue based upon the performance of the underlying life insurance policies both during employment and after retirement. Such benefits will continue to accrue and be paid throughout the participant's life assuming satisfactory performance of the funding life insurance policy. The plan also provides for payment of death benefits and for payment of disability benefits in the event the officer becomes permanently disabled prior to attainment of retirement age. During 2006, 2005 and 2004 a provision of $23,446, $137,688 and $92,613, respectively, was expensed for future benefits to be provided under this plan. The liability accrued for compensation deferred under the plan amounts to $531,682, and $508,236 at December 31, 2006 and 2005, respectively.

Split-Dollar life Insurance

The Company has entered into Life Insurance Endorsement Method Split Dollar Agreements with certain officers. Under these agreements, upon death of the officer, the Company first recovers the cash surrender value of the contract and then shares the remaining death benefits from insurance contracts, which are written with different carriers, with the designated beneficiaries of the officers. The death benefit to the officers' beneficiaries is a multiple of base salary at the time of the agreements. The Company, as owner of the policies, retains an interest in the life insurance proceeds and a 100% interest in the cash surrender value of the policies.

Note 16—Fair Values of Financial Instruments and Interest Rate Risk

The estimated fair values disclosed in the following table do not represent market values of all assets and liabilities of the Company and should not be interpreted to represent the underlying value of the Company. The following table reflects a comparison of carrying amounts and the estimated fair value of the financial instruments as of December 31, 2006 and 2005.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 16—Fair Values of Financial Instruments and Interest Rate Risk (Continued)

	2006		2005	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
	(dollars in thousands)			
Financial Assets				
Cash and cash equivalents	$ 34,760	$ 34,760	$ 21,369	$ 21,369
Securities available for sale	37,150	37,150	35,016	35,016
Loans, net of unearned income and allowance for loan losses	284,964	287,974	268,360	268,755
Loans held for sale	3,814	3,818	3,354	3,354
Other Financial assets	8,888	8,888	8,546	8,546
Financial Liabilities				
Deposits	$309,600	$314,986	$273,976	$274,208
Short-term borrowings	8,633	8,633	7,904	7,904
Long-term debt	33,696	33,554	39,103	38,815
Other financial liabilities	503	503	369	369

At December 31, 2006, the subsidiary banks had outstanding standby letters of credit and commitments to extend credit. These off-balance sheet financial instruments are generally exercisable at the market rate prevailing at the date the underlying transaction will be completed; therefore, they were deemed to have no current fair value. See Note 11.

Interest Rate Risk

The Company assumes interest rate risk (the risk that general interest rate levels will change) in the course of its normal operations. As a result, fair values of the Company’s financial instruments will change when interest rate levels change and that change may be either favorable or unfavorable to the Company. Management attempts to match maturities of assets and liabilities to the extent believed necessary to minimize interest rate risk. However, borrowers with fixed rate obligations are more likely to prepay in a falling rate environment and less likely to prepay in a rising rate environment. Conversely, depositors who are receiving fixed rates are more likely to withdraw funds before maturity in a rising rate environment and less likely to do so in a falling rate environment. Management monitors rates and maturities of assets and liabilities and attempts to minimize interest rate risk by adjusting terms of new loans and deposits and by investing in securities with terms that mitigate the Company’s overall interest rate risk.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 17—Parent Company Financial Data

The following is a summary of the condensed financial statements of Uwharrie Capital Corp:

Condensed Balance Sheets

	December 31, 2006	December 31, 2005
	(dollars in thousands)	
Assets		
Cash and demand deposits with bank subsidiaries	$ 214	$ 337
Interest-earning deposits with bank subsidiaries	6,865	4,756
Investments in:		
Bank subsidiaries	35,045	32,253
Nonbank subsidiaries	511	547
Other assets	894	1,764
Total assets	$ 43,529	$ 39,657
Liabilities and shareholders' equity		
Master notes	$ 6,608	$ 4,455
Long-term debt	2,000	2,400
Junior subordinated debentures	5,155	5,155
Other liabilities	133	194
Shareholders' equity	29,633	27,453
Total liabilities and shareholders' equity	$ 43,529	$ 39,657

Condensed Statement of Operations

	2006	2005	2004
	(dollars in thousands)		
Equity in earnings of subsidiaries	$ 2,915	$ 922	$ 84
Interest income	354	175	101
Dividend income	—	1,000	800
Management and service fees	3,854	3,797	1,900
Other income	190	107	149
Interest expense	921	625	401
Other operating expense	4,537	4,030	2,650
Income tax benefit	(216)	(171)	(270)
Net income	$ 2,071	$ 1,517	$ 253

Effective January 1, 2005 support operations staff moved to the holding company, which had the effect of increasing operating expense and increased allocation of service fees to the subsidiary banks.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 17—Parent Company Financial Data (Continued)

Condensed Statements of Cash Flows

	2006	2005	2004
	(dollars in thousands)		
Cash flows from operating activities			
Net income	$ 2,071	$ 1,517	$ 253
Adjustments to reconcile net income to net cash Provided (used) by operating activities:			
Equity in earnings of subsidiaries	(2,915)	(1,922)	(884)
Decrease in other assets	1,020	524	181
Increase (decrease) in other liabilities	(61)	(426)	505
Net cash provided (used) by operating activities	115	(307)	55
Cash flows from investing activities			
Dividends received from subsidiaries	—	1,000	800
Net cash provided by investing activities	—	1,000	800
Cash flows from financing activities			
Net increase(decrease) in master notes	2,153	(576)	983
Net decrease in long-term debt	(400)	(400)	(400)
Repurchase of common stock	(145)	(1,214)	(1,492)
Proceeds from issuance of common stock	224	347	571
Tax benefit of stock options exercised	48	31	51
Cash paid for fractional shares	(9)	(9)	(11)
Other, net	—	—	(96)
Net cash provided (used) by financing activities	1,871	(1,821)	(394)
Net increase (decrease) in cash and cash equivalents	1,986	(1,128)	461
Cash and cash equivalents at beginning of period	5,093	6,221	5,760
Cash and cash equivalents at end of period	$ 7,079	$ 5,093	$ 6,221

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 18—Quarterly Financial Data (unaudited)

	First	Second	Third	Fourth
	(in thousands, except per share data)			
2006				
Interest income	$ 5,477	$ 5,972	$ 6,412	$ 6,492
Interest expense	(2,171)	(2,562)	(2,960)	(3,009)
Net interest income	3,306	3,410	3,452	3,483
Provision for loan losses	(145)	(99)	(54)	—
Net interest income after provision for loan losses	3,161	3,311	3,398	3,483
Noninterest income	1,261	1,277	1,437	1,494
Noninterest expense	(3,856)	(4,002)	(3,900)	(4,160)
Income before taxes	566	586	935	817
Income taxes	140	145	282	266
Net income	$ 426	$ 441	$ 653	$ 551
Net income per common share				
Basic	$ 0.06	$ 0.06	$ 0.09	$ 0.08
Diluted	$ 0.06	$ 0.06	$ 0.09	$ 0.07

	First	Second	Third	Fourth
	(in thousands, except per share data)			
2005				
Interest income	$ 4,408	$ 4,594	$ 4,886	$ 5,273
Interest expense	(1,359)	(1,500)	(1,730)	(2,041)
Net interest income	3,049	3,094	3,156	3,232
Provision for loan losses	(215)	(145)	(210)	(185)
Net interest income after provision for loan losses	2,834	2,949	2,946	3,047
Noninterest income	1,047	1,048	1,121	1,135
Noninterest expense	(3,425)	(3,525)	(3,584)	(3,553)
Income before taxes	456	472	483	629
Income taxes	116	113	132	162
Net income	$ 340	$ 359	$ 351	$ 467
Net income per common share				
Basic	$ 0.05	$ 0.05	$ 0.05	$ 0.06
Diluted	$ 0.05	$ 0.05	$ 0.05	$ 0.05

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Selected Financial Data

Selected Financial Data
(In Thousands Except Per Share and Shares Outstanding Information)

	2006	2005	2004	2003	2002
Summary of Operations					
Interest income	$ 24,353	$ 19,161	$ 15,906	$ 14,597	$ 14,649
Interest expense	10,702	6,630	4,734	4,606	5,289
Net interest income	13,651	12,531	11,172	9,991	9,360
Provision for loan losses	298	755	2,092	593	835
Noninterest income	5,469	4,351	4,271	5,159	4,406
Noninterest expense	15,918	14,087	13,297	12,466	10,586
Income taxes	833	523	(199)	531	587
Net income	$ 2,071	$ 1,517	$ 253	$ 1,560	$ 1,758
Per Common Share					
Net income – basic (1)	$ .29	$ .21	$ .03	$ .21	$ .27
Net income – diluted (1)	.28	.20	.03	.21	.26
Book value (1)	3.99	3.73	3.63	3.65	3.44
Weighted Average Shares					
Outstanding:					
Basic (1)	7,244,772	7,242,262	7,361,486	7,373,092	6,565,840
Diluted (1)	7,354,229	7,418,773	7,533,839	7,511,108	6,677,118
Ratios					
Return on average assets	0.56%	0.45%	0.08%	0.57%	0.74%
Return on average equity	7.32%	5.58%	0.91%	5.78%	8.05%
Average equity to average assets	7.67%	8.14%	8.64%	9.86%	9.16%
Selected Year-end Balances					
Assets	$ 383,261	$ 350,190	$ 329,262	$ 300,529	$ 250,763
Loans	291,949	276,196	263,738	240,816	196,034
Securities	37,150	35,016	28,524	27,707	28,149
Deposits	309,600	273,976	246,939	212,563	173,556
Borrowed funds	42,329	47,007	53,796	58,924	50,549
Shareholders' equity	29,633	27,453	27,156	27,852	25,122
Selected Average Balances					
Assets	$ 368,781	$ 334,193	$ 321,093	$ 273,679	$ 238,371
Loans	293,394	267,164	256,525	221,158	186,532
Securities	35,227	29,038	28,846	27,281	30,517
Deposits	289,742	254,591	234,424	188,803	169,371
Borrowed funds	48,510	50,265	57,296	56,263	45,502
Shareholders' equity	28,299	27,187	27,741	26,980	21,833

(1) Net income per share, book value per share, weighted average shares outstanding and shares outstanding at year-end for 2002 through 2006 have been adjusted to reflect 3% stock dividends issued in 2006, 2005, 2004, 2003 and 2002.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Management's Discussion And Analysis of Financial Condition
And Results of Operations

A discussion and analysis of the Company's operating results and financial condition are presented in the following narrative and financial tables. The comments are intended to supplement and should be reviewed in conjunction with the consolidated financial statements and notes thereto appearing on pages 8—39. References to changes in assets and liabilities represent end of period balances unless otherwise noted. All references in this Annual Report to net income per share and weighted average common and common equivalent shares outstanding have been adjusted to reflect 3% stock dividends in 2006, 2005 and 2004. Statements contained in this annual report, which are not historical facts, are forward-looking statements, as that term is defined in the Private Securities Litigation Reform Act of 1995. Amounts herein could vary as a result of market and other factors. Such forward-looking statements are subject to risks and uncertainties which could cause actual results to differ materially from those currently anticipated due to a number of factors, which include, but are not limited to, factors discussed in documents filed by the Company with the Securities and Exchange Commission from time to time. Such forward-looking statements may be identified by the use of such words as "believe," "expect," "anticipate," "should," "might," "planned," "estimated," and "potential." Examples of forward-looking statements include, but are not limited to, estimates with respect to the financial condition, expected or anticipated revenue, results of operations and business of the Company that are subject to various factors which could cause actual results to differ materially from these estimates. These factors include, but are not limited to, general economic conditions, changes in interest rates, deposit flows, loan demand, real estate values, and competition; changes in accounting principles, policies, or guidelines; changes in legislation or regulation; and other economic, competitive, governmental, regulatory, and technological factors affecting the Company's operations, pricing, products and services.

Financial Condition at December 31, 2006 and December 31, 2005

The Company's total assets increased $33.1 million or 9.4% from $350.2 million at December 31, 2005 to $383.3 million at December 31, 2006. This increase resulted primarily from a $15.3 million increase in loans held for investment, a $2.1 million increase in securities available for sale and a $13.4 million increase in cash and cash equivalents.

Loans held for investment increased $15.3 million, from $272.8 million at December 31, 2005 to $288.1 million at December 31, 2006, an increase of 5.6%. The growth was largely due to the 7.4%, or $16.4 million, increase in our residential loan portfolio, while our commercial and consumer portfolios experienced slight declines. Loans held for sale increased $460 thousand, or 13.7%, for the period. At December 31, 2006 the allowance for loan losses was $3.2 million which represents 1.09% of the loan portfolio.

Investment securities increased 6.1% during 2006, from $35.0 million at December 31, 2005 to $37.2 million at December 31, 2006. Throughout the year we invested in mortgage backed securities and municipals. Mortgage backed securities increased $7.1 million, or 123.1%, during the period. The purchases made in the municipal portion of our investment portfolio were made to replace maturing investments in that area. There were also several investments sold during the year resulting in a gain of $60 thousand. The commercial paper we had in our portfolio matured during the year.

Cash and cash equivalents increased by $13.4 million during 2006. This increase was generated by an $11.3 million, or 182.7%, increase in federal funds sold, increasing from $6.2 million at December 31, 2005 to $17.5 million at December 31, 2006. The Company made the decision to keep a portion of their investments in short-term federal funds during 2006, resulting in the large increase in federal funds sold. Interest-earning deposits with banks declined $1.3 million during the period while cash and due from banks grew $3.3 million.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Management's Discussion And Analysis of Financial Condition
And Results of Operations

Other changes in our consolidated assets relate to interest receivable, Federal Home Loan Bank stock and other assets. Interest receivable grew $250 thousand, or 16.4%, during 2006, impacted by both loan and investment growth while Federal Home Loan Bank stock decreased $92 thousand, or 4.4%. Federal Home Loan Bank stock ownership is a requirement for member banks that utilize Federal Home Loan Bank for borrowing funds. The amount of stock owned by each member bank is based primarily on the amount of borrowings outstanding.

Customer deposits continued to be our principal funding source in 2006, allowing us to fund the growth in assets discussed above. At December 31, 2006, deposits from our customers totaled $309.6 million, an increase of $35.6 million, or 13.0%, from $274.0 million at December 31, 2005. Time deposits grew $25.8 million, or 24.3%, during the period, while interest checking and money market accounts increased $17.8 million, or 21.3%. Offsetting the growth in the aforementioned areas was a decline in savings accounts of 24.1%, or $8.9 million. During the past year with the increasing interest rate environment our customers have been moving their interest earning deposits into higher yielding deposit accounts.

The growth in deposits allowed the Company to reduce net borrowings by $4.7 million during 2006. Borrowings consist of both short-term and long-term borrowed funds. The Company utilizes both short-term and long-term advances from the Federal Home Loan Bank. At December 31, 2006, $26.4 million of the total borrowings of $42.3 million were attributed to Federal Home Loan Bank advances.

At December 31, 2006, total shareholders' equity was $29.6 million, an increase of $2.1 million from $27.5 million at the end of 2005. The Company earned net income of $2.1 million and collected $224 thousand from the exercise of stock options. These increases to shareholders' equity were offset by unrealized losses on our investment securities, net of tax, of $158 thousand and by the Company's purchase of 23,864 shares of common stock at a cost of $145 thousand.

Results of Operations for the Years Ended December 31, 2006 and 2005

Earnings

The Company earned net income of $2.1 million, or $0.29, per basic share for 2006 as compared with net income of $1.5 million, or $0.21 per basic share, in 2005.

Net Interest Income

As with most financial institutions, the primary component of earnings for our banks, is net interest income. Net interest income is the difference between interest income, principally from loan and investment securities portfolios, and interest expense, principally on customer deposits and borrowings. Changes in net interest income result from changes in volume, spread and margin. For this purpose, volume refers to the average dollar level of interest-earning assets and interest-bearing liabilities, spread refers to the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities, and margin refers to net interest income divided by average interest-earning assets. Margin is influenced by the level and relative mix of interest-earning assets and interest-bearing liabilities, as well as by levels of noninterest bearing liabilities and capital.

Net interest income increased $1.1 million to $13.6 million for 2006 compared to the $12.5 million earned in 2005. During 2006 with the interest rates stabilizing the increase in net interest income resulted from growth in the loan and investment portfolio. The average yield on our interest-earning assets increased 87 basis points to 7.23%, while the average rate we paid for our interest-bearing liabilities increased 114 basis points. These increases resulted in a decrease of 27 basis points in our interest rate spread, from 3.82% in 2005 to 3.55% in 2006. Our net interest margin for 2006 was 4.10%, compared to 4.21% in 2005. Financial Table 1 on page 50 presents a detailed analysis of the components of the Company's net interest income while Financial Table 2 on page 51 summarizes the effects on net interest income from changes in interest rates and in the dollar volume of the components of interest-earning assets and interest bearing liabilities.

Provision and Allowance for Loan Losses

The Company's allowance for loan losses is established through charges to earnings in the form of a provision for loan losses. The allowance is increased by provisions charged to operations and by recoveries of amounts previously charged off, and reduced by loans charged off. Management evaluates the adequacy of the allowance at least quarterly. In evaluating the adequacy of the allowance, management considers the growth, composition and industry diversification of the portfolio, historical loan loss experience, current delinquency levels, adverse situations that may affect a borrower's ability to repay, estimated value of any underlying collateral, prevailing economic conditions and other relevant factors. The Company's credit administration function, through a review process, validates the accuracy of the initial risk grade assessment. In addition, as a given loan's credit quality improves or deteriorates, the credit administration department has the responsibility to change the borrower's risk grade accordingly. For loans determined to be impaired, the allowance is based either on discounted cash flows using the loan's initial effective interest rate or on the fair value of the collateral for certain collateral dependent loans. This evaluation is inherently subjective, as it requires material estimates, including the amounts and timing of future cash flows expected to be received on impaired loans, which may be susceptible to significant change. In addition, regulatory agencies, as an integral part of their examination process, periodically review the allowance for loan losses and may require additions for estimated losses based upon judgments different from those of management.

Management uses the risk-grading program to facilitate the evaluation of probable inherent loan losses and the adequacy of the allowance for loan losses. In this program, risk grades are initially assigned by loan officers and reviewed and monitored by credit administration. The Company strives to maintain its loan portfolio in accordance with conservative loan underwriting policies that result in loans specifically tailored to the needs of its market area. Every effort is made to identify and minimize the credit risks associated with such lending strategies. The Company has no foreign loans and does not engage in significant lease financing or highly leveraged transactions. The Company follows a loan review program designed to evaluate the credit risk in the loan portfolio. This process includes the maintenance of an internally classified watch list that helps management assess the overall quality of the loan portfolio and the adequacy of the allowance for loan losses. In establishing the appropriate classification for specific assets, management considers, among other factors, the estimated value of the underlying collateral, the borrower's ability to repay, the borrower's payment history and the current delinquent status. As a result of this process, certain loans are categorized as substandard, doubtful or loss and reserves are allocated based on management's judgment and historical experience.

The allowance for loan losses represents management's estimate of an amount adequate to provide for known and inherent losses in the loan portfolio in the normal course of business. While management believes that it uses the best information available to establish the allowance for loan losses, future adjustments to the allowance may be necessary and results of operations could be adversely affected if circumstances differ substantially from the assumptions used in making the determinations. Furthermore, while management believes it has established the allowance for loan losses in conformity with generally accepted accounting principles, there can be no assurance that regulators, in reviewing the Company's portfolio, will not require an adjustment to the allowance for loan losses. In addition, because future events affecting borrowers and collateral cannot be predicted with certainty, there can be no assurance that the existing allowance for loan losses is adequate or that increases will not be necessary should the quality of any loans deteriorate as a result of the factors discussed herein. Any material increase in the allowance for loan losses may adversely affect the Company's financial condition and results of operations.

The provision for loan losses declined from $755 thousand in 2005 to $298 thousand in 2006, a decrease of $457 thousand. This decline in the level of our provision in 2006 resulted primarily from improved trends in our overall asset quality. During 2006, the levels of our impaired loans and the specific impairment identified for those impaired loans decreased by $677 thousand and $720 thousand, respectively. Additionally, other potential problem loans, which consist of loans which are currently performing and are deemed to be impaired, but about which we have serious doubts as to the borrower's ability to comply with present repayment terms, declined from $11.4 million at December 31, 2005 to $2.9 million at December 31, 2006. This decline in the level of our potential problem loans resulted principally from the improved condition of four borrower relationships which totaled $6.3 million at December 31, 2005. Net loan charge-offs increased from $1.3 million in 2005 to $1.6 million in 2006, resulting in the increase in the ratio of net loan charge-offs to average loans outstanding of eight basis points from .47% in 2005 to .55% in 2006. Three loans which were impaired as of December 31, 2005 represented $1.4 million of the total $1.6 million in net charge-offs in 2006. Nonperforming loans, which consist solely of nonaccrual loans, were $1.2 million at December 31, 2006, as compared to $1.9 million at December 31, 2005. Nonperforming loans to total loans decreased from 0.68% at December 31, 2005, to 0.41% at the end of 2006.

The allowance expressed as a percentage of gross loans decreased 53 basis points from 1.62% at December 31, 2005 to 1.09% at December 31, 2006. The most significant factor in this decrease is the decline in the level of our impaired and potential problem loans as discussed in the preceding paragraph. Although the allowance as a percentage of loans has decreased, the allowance as a percentage of total impaired and potential problem loans has increased from 29.3% at December 31, 2005 to 52.6% at December 31, 2006. Likewise, the portion of the allowance specifically allocable to impaired loans decreased from 35.9% at December 31, 2005 to 28.1% at December 31, 2006 and the total allowance relative to problem loans increased from 239.09% at the end of 2005 to 261.78% at this year end. This ratio of the total allowance to nonperforming loans at December 31, 2005 of 261.78% represents the highest year end percentage since December 31, 2002. Management believes the current level of allowance for loan losses to be adequate at this time.

Noninterest Income

The Company generates most of its revenue from net interest income; however, diversification of our earnings base is of major importance to our long term success. Noninterest income increased 25.7%, from $4.4 million in 2005 to $5.5 million in 2006, an increase of $1.1 million. Income generated from brokerage commissions and asset management fees increased $424 thousand to $1.3 million, while other banking fees increased $177 thousand or 21.9% during 2006. Service charges on deposit accounts grew $293 thousand to $2.0 million. During 2005, the Company implemented a new non-sufficient funds program. This new program along with the growth in demand deposit accounts resulted in a $348 thousand increase in NSF fees. The

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Company also benefited from an increase in income from mortgage loan sales of $210 thousand resulting in an increase in mortgage loan originations. During 2006, the Company sold investment securities realizing a gain of $60 thousand. These increases were offset by a decline in other income of $62 thousand.

Noninterest Expense

Noninterest expense increased $1.8 million to $15.9 million in 2006 compared to $14.1 million in 2005. Salaries and employee benefits, the largest component of noninterest expense, increased $1.1 million, from $8.0 million in 2005 to $9.1 million in 2006. Additions at the executive and bank support staff levels together with normal salary increases, primarily account for this increase. Data processing costs increased 11.4% or $96 thousand in 2006 with growth in loans and deposits. Other noninterest expense increased $560 thousand for the year, including electronic banking expense, a major component of this category, which increased by $276 thousand. Increased usage of electronic banking products is the reason for the increase. Marketing and donations another component of this category increased $235 thousand.

Income Tax Expense

The Company had income tax expense of $833 thousand for 2006 at an effective tax rate of 28.7% compared to income tax expense of $523 thousand in 2005 at an effective tax rate of 25.6%. Income taxes computed at the statutory rate are reduced primarily by the eligible amount of interest earned on state and municipal securities and income earned on bank owned life insurance.

Results of Operations for the Years Ended December 31, 2005 and 2004

Earnings

The Company earned net income of $1.5 million, or $0.21 per share, for 2005 as compared with net income of $253 thousand, or $0.03, per share in 2004.

Net Interest Income

Net interest income increased $1.4 million to $12.5 million for 2005 compared to the $11.1 million earned in 2004. During 2005 the Company benefited from a rising interest rate environment, augmented by loan and investment growth. The average yield on our interest-earning assets increased 79 basis points to 6.36%, while the average rate we paid for our interest-bearing liabilities increased 68 basis points. These increases resulted in an increment of 11 basis points in our interest rate spread, from 3.71% in 2004 to 3.82% in 2005. Our net interest margin for 2005 was 4.21%, compared to 3.96% in 2004.

Provision and Allowance for Loan Losses

The provision for loan losses declined from $2.1 million in 2004 to $755 thousand in 2005, a decrease of $1.3 million. During 2004, specific loan loss reserves were increased by $1.2 million due to identified impairment for five commercial lending relationships. Certain of these losses were realized in 2005, thereby accounting for the increase in total loan charge-offs from $373 thousand in 2004 to $1.4 million in 2005. Accordingly, the ratio of net loan charge-offs to average loans outstanding increased 34 basis points from 0.13% in 2004 to 0.47% in 2005.

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In light of the loan charge-offs referred to above and the resulting decrease in specific loan loss reserves, the Company's allowance for loan losses was reduced to $4.5 million at December 31, 2005, from $5.0 million at December 31, 2004. The allowance as a percentage of gross loans outstanding decreased 27 basis points from 1.89% at December 31, 2004 to 1.62% at December 31, 2005. Nonperforming loans, which consist entirely of nonaccrual loans, were $1.9 million at December 31, 2005, as compared to $3.4 million at year-end 2004. Nonperforming loans to total loans decreased from 1.29% at December 31, 2004 to 0.68% at December 31, 2005, while the allowance for loan losses to nonperforming loans increased to 239.1% from 147.6% at the end of 2004. At December 31, 2005, loans 90 days past due and still accruing declined by $811 thousand to $339 thousand, compared to $1.2 million at December 31, 2004. Restructured loans, excluding those included in nonperforming loans, amounted to $3.3 million at December 31, 2005.

Noninterest Income

Noninterest income increased 1.9%, from $4.3 million in 2004 to $4.4 million in 2005, an increase of $80 thousand. Income generated from brokerage commissions and asset management fees increased $121 thousand, while other banking fees increased $180 thousand or 28.8% during 2005. Service charges on deposit accounts grew $271 thousand to $1.7 million. During 2005 the Company implemented a new non-sufficient funds program. This new program along with the growth in demand deposit accounts resulted in $247 thousand increase in NSF fees. The Company also benefited from an increase in gain on sale of fixed assets and other assets of $102 thousand. These increases were offset by a decline in income from mortgage loan sales of $291 thousand. During 2005 the Federal Reserve continued raising interest rates resulting in lower volume of mortgage loan activity. Other income also decreased from $561 thousand in 2004 to $378 thousand in 2005.

Noninterest Expense

Noninterest expense increased $790 thousand to $14.1 million in 2005 compared to $13.3 million in 2004. Salaries and employee benefits, the largest component of noninterest expense, increased $847 thousand, from $7.2 million in 2004 to $8.0 million in 2005. Additions at the executive and bank support staff levels together with normal salary increases, primarily account for this increase. Data processing costs increased 4.1% or $34 thousand in 2005. These increases were offset by decreases in equipment expense of $26 thousand and other noninterest expense of $66 thousand. While other noninterest expense increased $66 thousand for the year, electronic banking expense, a major component of this category, increased $200 thousand. The increased usage of electronic banking products is the reason for the increase.

Income Tax Expense

The Company had income tax expense of $523 thousand for 2005, at an effective tax rate of 25.6% compared to an income tax benefit of $199 thousand in 2004. Income taxes computed at the statutory rate are reduced primarily by the eligible amount of interest earned on state and municipal securities and income earned on bank owned life insurance.

Capital Resources

The Company continues to maintain good capital ratios that support its asset growth. The capital position is maintained through the retention of earnings and controlled growth. Regulatory agencies divide capital into Tier I (consisting of shareholders' equity less ineligible intangible assets and accumulated other comprehensive income and allowable portions of trust preferred securities) and Tier II (consisting of the allowable portion of the reserve for loan losses and certain long-term debt) and measure capital adequacy by applying both capital levels to a banking company's risk-adjusted assets and off-balance sheet items. In addition to these capital ratios, regulatory agencies have established a Tier I leverage ratio that measures Tier I capital to average assets less ineligible intangible assets.

Regulatory guidelines require a minimum of total capital to risk-adjusted assets ratio of 8% with one-half consisting of tangible common shareholders' equity and a minimum Tier I leverage ratio of 4%. Banks which meet or exceed a Tier I ratio of 6%, a total capital ratio of 10% and a Tier I leverage ratio of 5% are considered well capitalized by regulatory standards. At December 31, 2006, the Company and it's subsidiary banks were all well capitalized.

The Company expects to continue to exceed these minimums without altering current operations or strategy. Note 13 to the Consolidated Financial Statements presents additional information regarding the Company's and its subsidiary banks' capital ratios.

Dividends

The Board of Directors of Uwharrie Capital Corp declared a 3% stock dividend in 2006, 2005, and in 2004. All references in this annual report to net income per share and weighted average common and common equivalent shares outstanding reflect the effects of these stock dividends.

Liquidity

Liquidity, the ability to raise cash when needed without adversely impacting profits, is managed primarily by the selection of asset mix and the maturity mix of liabilities. Maturities and the marketability of securities and other funding sources provide a source of liquidity to meet deposit fluctuations. Maturities in the securities portfolio, presented in Financial Table 4 on page 53, are supported by cash flows from mortgage-backed securities that have longer-term contractual maturities.

Other funding sources at year-end 2006 included $18.7 million in federal funds lines of credit from correspondent banks and approximately $34.9 million of remaining credit availability from the Federal Home Loan Bank. The Company may also borrow from the Federal Reserve Bank discount window. Growth in deposits is typically the primary source of funding for loans, supported by long-term credit available from the Federal Home Loan Bank.

At December 31, 2006, borrowings from federal funds lines and securities sold under repurchase agreements amounted to $2.0 million, while other short-term borrowings totaled $6.6 million. Long-term debt at that date consisted of advances of $26.4 million from the Federal Home Loan Bank, a note payable of $2.0 million to another bank, $5.2 million in junior subordinated debentures and a mortgage payable of $105 thousand.

Management believes that the Company's current sources of funds provide adequate liquidity for its current cash flow needs.

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Contractual Obligations

The following table reflects the contractual obligations of the Company outstanding as of December 31, 2006.

	Payments Due by Period (in thousands)				
	Total	On Demand or less than 1 year	1-3 Years	4-5 Years	After 5 Years
Contractual Obligations					
Short-term debt	$ 8,633	$ 8,633	$ —	$ —	$ —
Long-term debt	33,696	4,407	16,252	7,817	5,220
Total contractual cash obligations, excluding deposits	42,329	13,040	16,252	7,817	5,220
Deposits	309,600	296,921	10,434	2,209	36
Total contractual cash obligations, including deposits	$351,929	$ 309,961	$26,686	$10,026	$5,256

Critical Accounting Policy

The Company's most significant critical accounting policy is the determination of its allowance for loan losses. A critical accounting policy is one that is both very important to the portrayal of the Company's financial condition and results, and requires management's most difficult, subjective or complex judgments. What makes these judgments difficult, subjective and/or complex is the need to make estimates about the effects of matters that are inherently uncertain. Refer to the discussion within Allowance for Loan Losses and in Note 1 to the consolidated financial statements for a comprehensive discussion regarding this accounting policy.

Off-Balance Sheet Arrangements

The Company has various financial instruments (outstanding commitments) with off-balance sheet risk that are issued in the normal course of business to meet the financing needs of its customers. See Note 11 to the consolidated financial statements for more information regarding these commitments and contingent liabilities.

Interest Rate Sensitivity

The major component of income for the Company is net interest income, the difference between yield earned on assets and interest paid on liabilities. This differential or margin can vary over time as changes in interest rates occur. The volatility of changes in this differential can be measured by the timing (or repricing) difference between maturing assets and liabilities.

To identify interest rate sensitivity, a common measure is a gap analysis, which reflects the difference or gap between rate sensitive assets and liabilities over various time periods. Gap analysis at December 31, 2006 is reflected in Financial Table 3 on page 52. While management reviews this information, it has implemented the use of a simulation model which calculates expected net interest income based on projected interest-earning assets, interest-bearing liabilities and interest rates and provides a more relevant view of interest rate risk than traditional gap tables. The simulation allows comparison of flat, rising and falling rate scenarios to determine sensitivity of earnings to changes in interest rates.

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The principal goals of the Company's asset liability management are the maintenance of adequate liquidity and the management of interest rate risk. Interest rate risk management attempts to balance the effects of interest rate changes on interest-sensitive assets and liabilities to protect net interest income from wide fluctuations that could result from changes in interest rates. The Company's Asset Liability Management Committee monitors market changes in interest rates and assists with pricing loan and deposit products consistent with funding source needs and asset growth projections.

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Financial Table 1

Average Balances and Net Interest Income Analysis
(dollars in thousands)

	2006			2005			2004		
	Average Balance	Interest Income/ Expense	Average Yield/ Rate (1)	Average Balance	Interest Income/ Expense	Average Yield/ Rate (1)	Average Balance	Interest Income Expense	Average Yield Rate (1)
Interest-earning assets									
Taxable securities	$ 25,741	$ 1,266	4.92%	$ 19,363	$ 881	4.55%	$ 17,104	$ 741	4.33%
Non-taxable securities	11,586	517	6.87%	11,962	533	6.86%	11,741	598	7.84%
Short-term investments	11,274	611	5.42%	8,740	302	3.46%	7,862	99	1.26%
Taxable loans (2)	289,194	21,758	7.52%	263,168	17,252	6.56%	252,414	14,266	5.65%
Non-taxable loans	4,200	201	7.36%	3,996	193	7.43%	4,111	202	7.56%
Total interest-earning assets	341,995	24,353	7.23%	307,229	19,161	6.36%	293,232	15,906	5.57%
Non-earning assets									
Cash and due from banks	11,833			11,904			10,320		
Premises and equipment, net	8,419			8,367			8,558		
Interest receivable and other	6,534			6,693			8,983		
Total non-earning assets	26,786			26,964			27,861		
Total assets	$368,781			$334,193			$321,093		
Interest-bearing liabilities									
Savings deposits	$ 32,304	$ 734	2.27%	$ 37,987	$ 580	1.53%	$ 41,883	$ 322	0.77%
Interest checking & MMDA	89,174	2,342	2.63%	72,755	1,002	1.38%	72,291	616	0.85%
Time deposits	121,053	5,191	4.29%	99,704	2,891	2.90%	83,516	1,738	2.08%
Total deposits	242,531	8,267	3.41%	210,446	4,473	2.13%	197,690	2,676	1.35%
Short-term borrowed funds	13,521	627	4.64%	8,564	239	2.78%	13,468	127	0.94%
Long-term debt	34,989	1,808	5.17%	41,701	1,918	4.60%	43,828	1,931	4.41%
Total interest-bearing Liabilities	291,041	10,702	3.68%	260,711	6,630	2.54%	254,986	4,734	1.86%
Noninterest liabilities									
Transaction deposits									
Interest payable and other	49,441			46,295			38,366		
Total liabilities	340,482			307,006			293,352		
Shareholders' equity	28,299			27,187			27,741		
Total liabilities and Shareholders equity	$368,781			$334,193			$321,093		
Interest rate spread			3.55%			3.82%			3.71%
Net interest income and net interest margin		$13,651	4.10%		$12,531	4.21%		$11,172	3.96%

1) Yields related to securities and loans exempt from federal and/or state income taxes are stated on a fully tax-equivalent basis, assuming a 35% tax rate.
2) Nonaccrual loans are included in loans, net of unearned income.

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Financial Table 2

Volume and Rate Variance Analysis
(dollars in thousands)

	2006 Versus 2005			2005 Versus 2004		
	Volume	**Rate**	**Net Change**	**Volume**	**Rate**	**Net Change**
Interest-earning assets						
Taxable securities	$ 302	$ 83	$ 385	$ 100	$ 40	$ 140
Non-taxable securities	(17)	1	(16)	11	(76)	(65)
Short-term investments	112	197	309	21	182	203
Taxable loans	1,832	2,674	4,506	656	2,330	2,986
Non-taxable loans	10	(2)	8	(6)	(3)	(9)
Total Interest-earning assets	2,239	2,953	5,192	782	2,473	3,255
Interest-bearing liabilities						
Savings deposits	(108)	262	154	(45)	303	258
Transaction and MMDA deposits	329	1,011	1,340	5	381	386
Other time deposits	767	1,533	2,300	403	750	1,153
Short-term borrowed funds	184	204	388	(92)	204	112
Long-term debt	(328)	218	(110)	(96)	83	(13)
Total interest-bearing liabilities	844	3,228	4,072	175	1,721	1,896
Net interest income	$1,395	$ (275)	$ 1,120	$ 607	$ 752	$ 1,359

The above table analyzes the dollar amount of changes in interest income and interest expense for major components of interest-earning assets and interest-bearing liabilities. The table distinguishes between (i) changes attributable to volume (changes in volume multiplied by the prior period's rate), (ii) changes attributable to rate (changes in rate multiplied by the prior period's volume), and (iii) net change (the sum of the previous columns). The change attributable to both rate and volume (changes in rate multiplied by changes in volume) has been allocated equally to the change attributable to volume and the change attributable to rate.

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Financial Table 3

Interest Rate Sensitivity Analysis
(dollars in thousands)

	1-90 Day Position	3-6 Month Position	6-12 Month Position	1-5 Year Position	> 5 Year Position	Total Position
Interest-earning assets						
Interest-earning deposits with banks	$ 2,473	$ —	$ —	—	$ —	$ 2,473
Federal funds sold	17,525	—	—	—	—	17,525
Investment securities	24	—	988	10,982	25,156	37,150
FHLB and other stock	—	—	—	—	2,076	2,076
Loans	169,357	4,775	7,796	65,262	44,759	291,949
Total interest-earning assets	189,379	4,775	8,784	76,244	71,991	351,173
Interest-bearing liabilities						
Deposits	126,307	53,722	41,166	23,808	16,448	261,451
Short-term borrowed funds	8,633	—	—	—	—	8,633
Long-term debt	400	—	4,007	24,068	5,221	33,696
Total interest-bearing liabilities	135,340	53,722	45,173	47,876	21,669	303,780
Interest sensitivity GAP per period	$ 54,039	$(48,947)	$(36,389)	$28,368	$50,322	$ 47,393
Cumulative interest sensitivity GAP	$ 54,039	$ 5,092	$(31,297)	$ (2,929)	$47,393	$ 47,393
Ratios						
Cumulative gap as a percentage of total interest-earning assets	15.39%	1.45%	(8.91)%	(0.83)%	13.50%	13.50%
Cumulative interest-earning assets as a percentage of interest-bearing liabilities	139.93%	102.69%	86.64%	98.96%	115.60%	115.60%

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Financial Table 4

Investment Securities Portfolio Analysis
(dollars in thousands)

	December 31, 2006		
	Amortized Cost	Estimated Fair Value	Book Yield (1)
Securities available for sale			
U.S. Treasury			
Due after one but within five years	$ 2,992	$ 2,914	3.20%
U.S. Government agencies			
Due within one year	1,008	988	2.17%
Due after one but within five years	6,501	6,372	3.84%
	7,509	7,360	3.61%
Mortgage-backed securities			
Due after one but within five years	8	8	6.50%
Due after five but within ten year	1,877	1,868	4.88%
Due after ten years	11,033	11,030	5.62%
	12,918	12,906	5.51%
State and political			
Due after one but within five years	1,625	1,688	8.22%
Due after five but within ten year	3,655	3,787	7.36%
Due after ten years	7,651	7,951	7.86%
	12,931	13,426	7.77%
Corporate Bond			
Due after ten years	514	520	3.25%
Equity Securities			
Due within one year	8	24	5.12%
Total Securities available for sale			
Due within one year	1,016	1,012	2.19%
Due after one but within five years	11,126	10,982	4.31%
Due after five but within ten year	5,532	5,655	6.52%
Due after ten years	19,198	19,501	6.45%
	$ 36,872	$37,150	5.70%

1) Yields on securities and investments exempt from federal and/or state income taxes are stated on a fully tax- equivalent basis, assuming a 35% tax rate.

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Financial Table 5

Noninterest Income
(dollars in thousands)

	Year Ended December 31, 2006	2005	2004
Service charges on deposit accounts	$2,000	$1,707	$1,436
Other banking fees	984	807	627
Asset management fees	974	497	357
Brokerage commissions	371	424	443
Other noninterest income	348	290	547
Core noninterest income	4,677	3,725	3,410
Income from mortgage loan sales	764	554	845
Security gains (losses)	60	(16)	2
Gains (losses) from sale of OREO	(23)	16	(2)
Other gains (losses) from sale of assets	(9)	72	16
Total noninterest income	$5,469	$4,351	$4,271

Financial Table 6
(dollars in thousands)

Other Noninterest Expense

	Year Ended December 31, 2006	2005	2004
Professional fees and services	$ 618	$ 456	$ 450
Marketing and donations	669	434	522
Office supplies and printing	280	260	291
Postage	192	167	168
Telephone and data lines	212	200	210
Electronic banking expense	604	328	278
Software amortization and maintenance	372	257	358
Loan collection cost	172	299	240
Other	1,401	1,559	1,509
Total	$4,520	$3,960	$4,026

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Financial Table 7

Loan Portfolio Composition
(dollars in thousands)

	At December 31, 2006 Amount	2006 % of Total Loans	2005 Amount	2005 % of Total Loans	2004 Amount	2004 % of Total Loans
Loan type:						
Commercial	$ 36,406	12.48%	$ 37,299	13.51%	$ 37,718	14.31%
Real estate—construction	27,342	9.37%	21,206	7.68%	25,480	9.67%
Real estate—residential	126,111	43.22%	116,715	42.29%	102,627	38.93%
Real estate—commercial	84,744	29.04%	83,861	30.39%	81,283	30.84%
Consumer	13,262	4.54%	13,479	4.88%	13,488	5.12%
Loans held for sale	3,814	1.31%	3,354	1.22%	2,903	1.10%
Other	133	0.05%	72	0.03%	90	0.03%
Total loans	291,812	100.00%	275,986	100.00%	263,589	100.00%
Less:						
Allowance for loan losses	(3,171)		(4,482)		(4,983)	
Unearned net loan fees	137		210		149	
Net loans	$288,778		$271,714		$258,755	

	At December 31, 2003 Amount	2003 % of Total Loans	2002 Amount	2002 % of Total Loans
Loan type:				
Commercial	$ 38,517	16.00%	$ 38,680	19.73%
Real estate—construction	21,813	9.06%	10,893	5.56%
Real estate—residential	76,933	31.95%	68,876	35.13%
Real estate—commercial	84,920	35.27%	61,027	31.13%
Consumer	12,741	5.29%	12,888	6.57%
Loans held for sale	5,665	2.35%	3,569	1.82%
Other	187	0.08%	123	0.06%
Total loans	$240,776	100.00%	196,056	100.00%
Less:				
Allowance for loan losses	(3,224)		(2,755)	
Unearned net loan fees	40		(23)	
Net loans	$237,592		$193,278	

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Management's Discussion And Analysis of Financial Condition
And Results of Operations

Financial Table 8

Selected Loan Maturities
(dollars in thousands)

	December 31, 2006			
	One Year or Less	One to Five Years	Over Five Years	Total
Commercial and agricultural	$ 11,657	$ 21,562	$ 3,187	$ 36,406
Real estate—construction	14,743	11,033	1,566	27,342
Total selected loans	$ 26,400	$ 32,595	$ 4,753	$ 63,748
Fixed rate loans	$ 9,055	$ 60,926	$57,970	$127,951
Sensitivity to rate changes:				
Variable interest rates	$163,341	$ 657	$ —	$163,998

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Management's Discussion And Analysis of Financial Condition
And Results of Operations

Financial Table 9

Nonperforming Assets
(dollars in thousands)

	At December 31, 2006	2005	2004	2003	2002
Nonperforming Assets:					
Nonaccrual loans	$ 1,211	$ 1,875	$ 3,376	$ 1,577	$ 788
Other real estate owned	203	169	481	108	714
Total nonperforming assets	$ 1,414	$ 2,044	$ 3,857	$ 1,685	$ 1,502
Accruing loans past due 90 days or more	$ 500	$ 339	$ 1,150	$ 607	$ 587
Allowance for loan losses	3,171	4,482	4,983	3,224	2,755
Nonperforming loans to total loans	0.41%	0.68%	1.29%	0.65%	0.40%
Allowance for loan losses to total loans	1.09%	1.62%	1.89%	1.34%	1.41%
Nonperforming assets to total loans and other real estate	0.48%	0.74%	1.47%	0.70%	0.76%
Nonperforming assets to total assets	0.37%	0.58%	1.17%	0.56%	0.60%
Allowance for loan losses to nonperforming loans	261.78%	239.09%	147.59%	204.44%	349.62%

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Management's Discussion And Analysis of Financial Condition And Results of Operations

Financial Table 10

Activity in the Allowance for Loan Loss
(dollars in thousands)

	At or for the Year Ended December 31,				
	2006	2005	2004	2003	2002
Allowance for loan losses at beginning of year	$4,482	$4,983	$3,224	$2,755	$2,181
Provision for loan losses	298	755	2,092	593	835
	4,780	5,738	5,316	3,348	3,016
Loan charge-offs:					
Commercial	1,533	1,124	224	10	66
Real estate	14	—	—	45	65
Consumer	140	254	149	95	150
Total charge-offs	1,687	1,378	373	150	281
Recoveries of loans previously charged off:					
Commercial	34	3	1	—	—
Real estate	—	—	—	1	—
Consumer	44	119	39	25	20
Total recoveries	78	122	40	26	20
Net charge-offs	1,609	1,256	333	124	261
Allowance for loan losses at end of year	$3,171	$4,482	$4,983	$3,224	$2,755
Net charge-offs as a percent of average loans	(0.55)%	(0.47)%	(0.13)%	(0.06)%	(0.14)%

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Management's Discussion And Analysis of Financial Condition
And Results of Operations

Financial Table 11

Allocation of the Allowance for Loan Losses
(dollars in thousands)

	At December 31,					
	2006		2005		2004	
	Amount	% of Total Loans (1)	Amount	% of Total Loans (1)	Amount	% of Total Loans (1)
Commercial	$ 356	12.48%	$2,474	13.51%	$ 897	14.31%
Real estate—construction	255	9.37%	101	7.68%	185	9.67%
Real estate—residential	1,235	44.57%	323	43.51%	509	40.04%
Real estate—commercial	1,123	29.04%	1,159	30.39%	2,965	30.84%
Consumer loans	202	4.54%	369	4.88%	359	5.12%
Other	—	— %	—	— %	—	— %
Unallocated	—	— %	56	0.03%	68	0.02%
Total loans	$3,171	100.00%	$4,482	100.00%	$4,983	100.00%

	At December 31,			
	2003		2002	
	Amount	% of Total Loans (1)	Amount	% of Total Loans (1)
Commercial	$1,204	16.00%	$ 711	19.73%
Real estate—construction	171	9.06%	163	5.56%
Real estate—residential	472	34.30%	590	36.95%
Real estate—commercial	877	35.27%	915	31.13%
Consumer	450	5.29%	325	6.57%
Other	—	— %	2	— %
Unallocated	50	0.08%	49	0.06%
Total loans	$3,224	100.00%	$2,755	100.00%

(1) Represents total of all outstanding loans in each category as a percent of total loans outstanding.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Management's Discussion And Analysis of Financial Condition
And Results of Operations

Financial Table 12

Maturities of Time Deposits of $100,000 or More
(dollars in thousands)

	3 Months or Less	Over 3 Months to 6 Months	Over 6 Months to 12 Months	Over 12 Months	Total
Time Deposits of $100,000 or more	$ 8,647	$21,171	$ 15,964	$ 2,668	$48,450

Financial Table 13

Securities Performance Ratios

	At December 31,				
	2006	2005	2004	2003	2002
Return on average assets	0.56%	0.45%	0.08%	0.57%	0.74%
Return on average equity	7.32%	5.58%	0.91%	5.78%	8.05%
Equity to assets ratio	7.67%	8.14%	8.64%	9.86%	9.16%

UWHARRIE CAPITAL CORP
Board of Directors

Joe S. Brooks
Owner and Manager
Brothers Precision Tool Co

Henry E. Farmer, Sr
President and Owner
Henry E. Farmer, Inc.

Charles F. Geschickter, III
President
ST Motorsports, Inc.;
JTG Racing, Inc. and
Wood Bros. / JTG Racing, Inc.

Thomas M. Hearne, Jr.
Geopavement Engineer
NC Department of Transportation

Joseph R. Kluttz, Jr.
President
Albemarle Insurance Agency, Inc

B. Franklin Lee
Owner and Manager
Franklin Lee Farm

W. Chester Lowder
Director of Livestock Program
Public Policy Division
NC Farm Bureau Federation, Inc.

John P. Murray, MD
Retired – Physician and Owner
Albemarle Ear, Nose and Throat

James E. Nance
Board Vice Chairman
President and Dealer Operator
Confederate Motors, Inc.

Emmett S. Patterson
Retired – General Manager
and Executive Vice President
Pee Dee Electric Membership
Corporation

Timothy J. Propst
Executive Vice President
Propst Construction Co., Inc

Susan J. Rourke
President and Owner
US Land Management Co.

Donald P. Scarborough
President, Treasurer and Owner
Plank Road Realty, Inc.

John W. Shealy, Jr.
President
Capital Concrete Co.

Michael E. Snyder, Sr.
Board Chairman
Vice President
E.J. Snyder & Company, Inc.

Douglas L. Stafford
Principal
Griffin Stafford, LLC

Emily M. Thomas
Vice President - Administration
and Finance
CMH Flooring Products, Inc.

Hugh E. Wallace
President
Anson Apparel Company and
Anson Apparel III

Executive Officers

Roger L. Dick
President and
Chief Executive Officer
Uwharrie Capital Corp

Brendan P. Duffey
Executive Vice President and
Chief Operating Officer
Uwharrie Capital Corp

Patricia K. Horton
Chief Executive Officer
Cabarrus Bank & Trust Company

W.D. "Bill" Lawhon, Jr.
President and
Chief Executive Officer
Bank of Stanly

Christy D. Stoner
President and
Chief Executive Officer
The Strategic Alliance Corp
BOS Agency, Inc., and
Strategic Investment Advisors, Inc.
Executive Vice President
Uwharrie Capital Corp

Jimmy L. Strayhorn
President and
Chief Executive Officer
Anson Bank & Trust Co.

Barbara S. Williams
Executive Vice President and
Controller
Uwharrie Capital Corp

EX-13 2 dex13.htm 2007 ANNUAL REPORT TO SHAREHOLDERS

Exhibit 13

UWHARRIE CAPITAL CORP

2007 ANNUAL REPORT

Uwharrie Capital Corp

2007

ANNUAL REPORT TO SHAREHOLDERS

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UWHARRIE CAPITAL CORP AND SUBSIDIARIES

Description of Business

Uwharrie Capital Corp (the "Company") is a North Carolina bank holding company. The Company was organized on July 1, 1993 to become the bank holding company for the Bank of Stanly ("Stanly"), a North Carolina commercial bank chartered on September 28, 1983, and its three wholly-owned subsidiaries, The Strategic Alliance Corporation, BOS Agency, Inc., and Gateway Mortgage, Inc., a mortgage origination company. The Company also owns three non-bank subsidiaries, Strategic Investment Advisors, Inc., Uwharrie Mortgage, Inc. and Uwharrie Statutory Trust 1.

Stanly engages in retail and commercial banking, with five banking offices in Stanly County. Stanly provides a wide range of banking services including deposit accounts, commercial, consumer, home equity and residential mortgage loans, safe deposit boxes, and electronic banking services.

On January 19, 2000, the Company completed its acquisition of Anson BanCorp, Inc. and its subsidiary, Anson Savings Bank. The savings bank retained its North Carolina savings bank charter and became a wholly-owned subsidiary of Uwharrie Capital Corp as Anson Bank & Trust Co. ("Anson") and provides financial services to customers through one banking office in Anson County.

On April 10, 2003, the Company capitalized a new wholly-owned subsidiary bank, Cabarrus Bank & Trust Company ("Cabarrus"), located in Concord, North Carolina. As of that date, Cabarrus purchased two branch offices located in Cabarrus County from Stanly to begin its operation. Cabarrus operates as a commercial bank and provides a full range of banking services.

The Company and its subsidiaries are located in Stanly County, Anson County and Cabarrus County. However, the Company intends to prudently expand its service area to include the entire Uwharrie Lakes Region of North Carolina.

Depository services offered by the subsidiary banks include personal and commercial checking, savings, money market, certificates of deposit accounts and individual retirement accounts, all tailored to meet customers' needs. The banks provide fixed and variable rate loans, which include mortgage, home equity, lines of credit, consumer and commercial loans. The banks also offer Internet Banking and 24-Hour Telephone Banking, providing customers the convenience of access to account information, rate information and accessibility of funds transfers between accounts. Other services include MasterCard® credit cards and a Visa® Check Card which functions as a point-of-sale (POS) and automated teller machine (ATM) card. Customers can use the Check Card for purchases at virtually any merchant accepting Visa® and ATMs displaying the STAR® or CIRRUS® networks regionally and worldwide, respectively.

Strategic Investment Advisors Inc. provides portfolio management services to its customers. The Strategic Alliance Corporation (Strategic Alliance®) is a registered broker-dealer with the National Association of Securities Dealers, Inc. ("NASD"). BOS Agency provides insurance products and is licensed in the state of North Carolina. Through Strategic Investment Group, a DBA for a partnership with UVEST Financial Services, Inc., securities and insurance products are offered including fixed annuities, long-term care, and life products. Group insurance products are offered through an arrangement with Benchmark Life Strategies as well as Medicare supplement products.

The Strategic Alliance Corporation. Member NASD/SIPC.
Securities and insurance products are offered by, and Financial Consultants are registered with UVEST Financial Services, member NASD/SIPC. UVEST, Strategic Investment Group and Uwharrie Capital Corp affiliates are independent entities. Securities and/or insurance products are not FDIC insured, are not deposits or other obligations of any depository institution, are not guaranteed by any depository institution and are subject to investment risks, including possible loss of the principal amount invested.

Bank of Stanly, Member FDIC, Equal Housing Lender.
Anson Bank & Trust Co., Member FDIC, Equal Housing Lender.
Cabarrus Bank & Trust Company, Member FDIC, Equal Housing Lender.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES

Financial Highlights

(Dollars in thousands except per share amounts)	2007	2006	Percent Increase (Decrease)
For the year:			
Net income	$ 2,959	$ 2,071	42.88%
Basic net income per common share (1)	$ 0.40	$ 0.28	42.86%
Diluted net income per common share	$ 0.40	$ 0.27	48.15%
Weighted average common shares outstanding (diluted)	7,482,361	7,574,856	(1.22)%
At year-end:			
Total assets	$ 411,944	$ 383,261	7.48%
Total earning assets	380,549	350,823	8.47%
Loans held for investment	321,987	288,135	11.75%
Total interest-bearing liabilities	331,679	303,780	9.18%
Shareholders' equity	31,574	29,633	6.55%
Book value per share (1)	$ 4.26	$ 3.87	10.08%
Averages for the year:			
Total assets	$ 393,188	$ 368,781	6.62%
Total earning assets	365,579	341,995	6.90%
Loans held for investment	308,149	293,394	5.03%
Total interest-bearing liabilities	313,570	291,041	7.74%
Shareholders' equity	30,402	28,299	7.43%
Financial Ratios (in percentage):			
Return on average assets	0.75%	0.56%	
Return on average shareholders' equity	9.73%	7.32%	
Average equity to average assets	7.73%	7.67%	
Net interest margin (fully tax equivalent basis)	4.22%	4.10%	
Allowance as % of loans at year-end	1.09%	1.10%	
Allowance as % of nonperforming loans	195.57%	261.78%	
Nonperforming loans to total loans	0.56%	0.42%	
Nonperforming assets to total assets	0.48%	0.37%	
Net loan charge-offs (recoveries) to average loans	(0.11)%	0.55%	

(1) Net income per share, book value per share, and shares outstanding at year-end have been adjusted to reflect the 3% stock dividends in 2007 and in 2006.

Market for the Company's Common Stock and Related Security Holder Matters

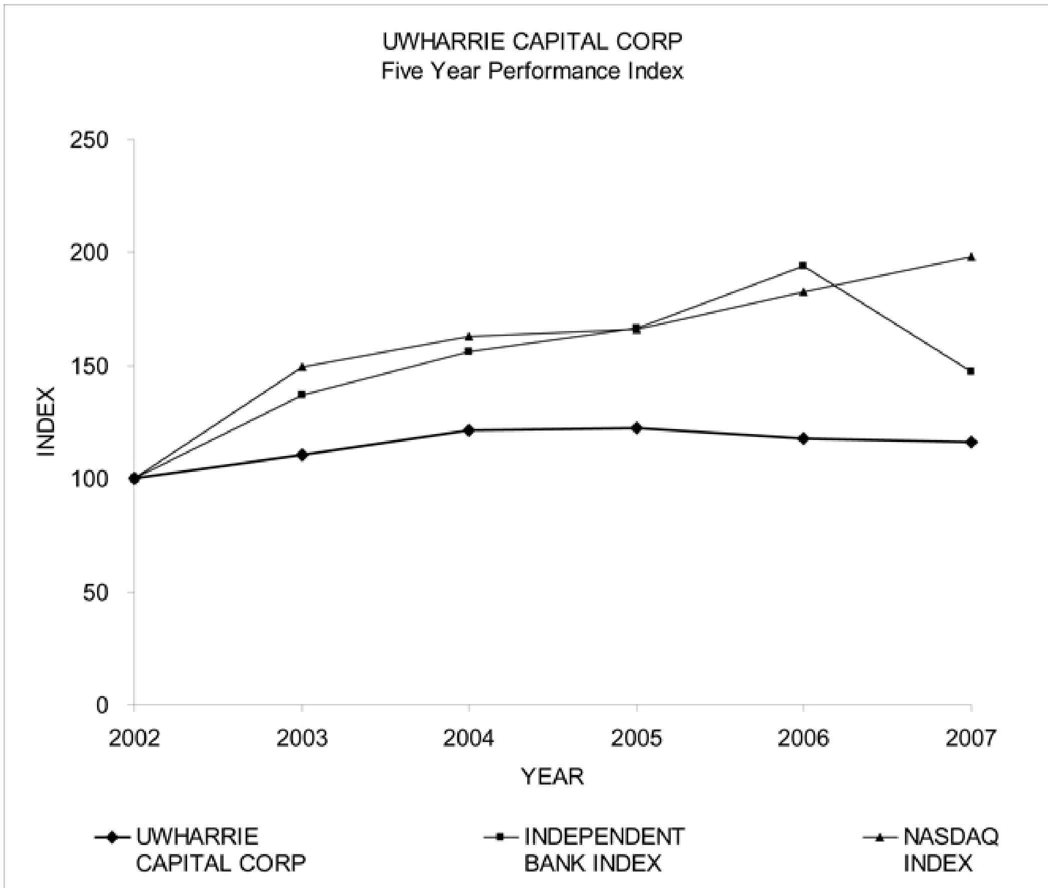
It is the philosophy of Uwharrie Capital Corp to promote a strong, base of local shareholders. While bid and asked prices for the Company's common stock are quoted on the Over the Counter Bulletin Board under the symbol UWHR, trading is sporadic with the most trades taking place in privately negotiated transactions. Management makes every reasonable effort to match willing buyers with willing sellers as they become known for the purpose of private negotiations for the purchase and sale of the Company's common stock. The Company has an independent valuation of its common stock performed on a quarterly basis and makes this valuation available to interested shareholders in order to promote fairness and market efficiency in privately negotiated transactions.

The Board of Directors has adopted a dividend policy on an annual basis. For 2007, Uwharrie Capital Corp declared a 3% stock dividend. The Board of Directors will determine on an annual basis, consistent with the capital needs of the Company an appropriate dividend. In addition, Uwharrie Capital Corp has adopted a stock repurchase program whereby the Company may make open market purchase of shares of its stock. The combination of private trades as well as the holding company purchases provides liquidity for the investors of Uwharrie Capital Corp.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES

The following graph compares (i) the yearly change in the cumulative total shareholder return on the Company's common stock with (ii) the cumulative return of The Carson Medlin Company Independent Bank Index, and (iii) the Nasdaq Composite. The graph assumes that the value of an investment in the Company's common stock and in each index was $100 on December 31, 2002, and that all dividends were reinvested. The performance shown in the graph represents past performance and should not be considered the indication of future performance.

Shareholders needing information about purchasing or selling shares of Uwharrie Capital Corp should contact Tamara M. Singletary or Lisa E. Hartsell, Investor Relations at Uwharrie Capital Corp, 132 N. First Street, Post Office Box 338, Albemarle, NC 28002.



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DIXON HUGHES PLLC

Certified Public Accountants and Advisors

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and Board of Directors
Uwharrie Capital Corp
Albemarle, North Carolina

We have audited the accompanying consolidated balance sheets of Uwharrie Capital Corp and Subsidiaries (the “Company”) as of December 31, 2007 and 2006, and the related consolidated statements of income, comprehensive income, changes in shareholders’ equity and cash flows for each of the years in the three-year period ended December 31, 2007. These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company’s internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Uwharrie Capital Corp and Subsidiaries as of December 31, 2007 and 2006, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2007, in conformity with accounting principles generally accepted in the United States of America.

Dixon Hughes PLLC

Raleigh, North Carolina
March 14, 2008

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
December 31, 2007 and 2006

	2007	2006
	(dollars in thousands)	
ASSETS		
Cash and due from banks	$ 13,765	$ 15,088
Interest-earning deposits with banks	2,432	2,147
Federal funds sold	—	17,525
Securities available for sale, at fair value	51,005	37,150
Loans held for sale	2,916	3,814
Loans:		
Loans held for investment	321,987	288,135
Less allowance for loan losses	(3,510)	(3,171)
Net loans held for investment	318,477	284,964
Premises and equipment, net	8,751	8,618
Interest receivable	2,055	1,775
Federal Home Loan Bank stock	2,137	1,980
Bank owned life insurance	5,318	5,133
Goodwill	987	987
Other assets	4,101	4,080
Total assets	$411,944	$383,261
LIABILITIES		
Deposits:		
Demand noninterest-bearing	$ 46,597	$ 48,149
Interest checking and money market accounts	102,411	101,470
Savings deposits	26,200	27,833
Time deposits, $100,000 and over	54,729	48,450
Other time deposits	94,720	83,698
Total deposits	324,657	309,600
Short-term borrowed funds	31,928	13,040
Long-term debt	21,691	29,289
Interest payable	596	503
Other liabilities	1,498	1,196
Total liabilities	380,370	353,628
Off balance sheet items, commitments and contingencies (Note 12)		
SHAREHOLDERS' EQUITY		
Common stock, $1.25 par value: 20,000,000 shares authorized; shares issued and outstanding 7,414,707 and 7,423,550 shares, respectively	9,268	9,279
Additional paid-in capital	13,453	13,541
Unearned ESOP compensation	(800)	(859)
Undivided profits	9,266	7,502
Accumulated other comprehensive income	387	170
Total shareholders' equity	31,574	29,633
Total liabilities and shareholders' equity	$411,944	$383,261

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

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
Years Ended December 31, 2007, 2006 and 2005

	2007	2006	2005
	(in thousands, except share and per share data)		
Interest Income			
Loans, including fees	$ 23,916	$ 21,959	$ 17,446
Investment securities:			
US Treasury	98	98	98
US Government agencies and corporations	1,401	832	537
State and political subdivisions	633	679	653
Other	128	174	125
Interest-earning deposits with banks and federal funds sold	733	611	302
Total interest income	26,909	24,353	19,161
Interest Expense			
Interest checking and money market accounts	2,550	2,342	1,002
Savings deposits	526	734	580
Time deposits $100,000 and over	2,316	2,100	1,168
Other time deposits	4,138	3,091	1,723
Short-term borrowed funds	1,128	758	354
Long-term debt	1,218	1,677	1,803
Total interest expense	11,876	10,702	6,630
Net interest income	15,033	13,651	12,531
Provision for loan losses	15	298	755
Net interest income after provision for loan losses	15,018	13,353	11,776
Noninterest Income			
Service charges on deposit accounts	2,188	2,000	1,707
Other service fees and commissions	3,097	2,329	1,728
Gain (loss) on sale of securities	(76)	60	(16)
Income from mortgage loan sales	957	764	554
Other income	424	316	378
Total noninterest income	6,590	5,469	4,351
Noninterest Expense			
Salaries and employee benefits	10,156	9,130	8,002
Net occupancy expense	871	711	643
Equipment expense	598	618	639
Data processing costs	742	939	843
Other noninterest expense	4,995	4,520	3,960
Total noninterest expense	17,362	15,918	14,087
Income before income taxes	4,246	2,904	2,040
Income taxes	1,287	833	523
Net income	$ 2,959	$ 2,071	$ 1,517
Net income per common share			
Basic	$ 0.40	$ 0.28	$ 0.20
Diluted	$ 0.40	$ 0.27	$ 0.20
Weighted average common shares outstanding			
Basic	7,382,033	7,462,115	7,459,530
Diluted	7,482,361	7,574,856	7,641,336

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

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
Years Ended December 31, 2007, 2006 and 2005

	2007	2006 (in thousands)	2005
Net Income	$2,959	$2,071	$1,517
Other comprehensive income (loss):			
Unrealized gains (losses) on available for sale securities	275	(197)	(761)
Related tax effect	(105)	76	293
Reclassification of losses (gains) recognized in net income	76	(60)	16
Related tax effect	(29)	23	(6)
Total other comprehensive income (loss)	217	(158)	(458)
Comprehensive income	$3,176	$1,913	$1,059

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

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
Years Ended December 31, 2007, 2006 and 2005

	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Unearned ESOP Compensation	Undivided Profits	Accumulated Other Comprehensive Income	Total
			(in thousands, except share data)				
Balance, December 31, 2004	7,057,755	$8,822	$ 12,043	$ (965)	$ 6,469	$ 786	$27,155
Net income	—	—	—	—	1,517	—	1,517
Other comprehensive loss	—	—	—	—	—	(458)	(458)
Release of ESOP shares	—	—	33	51	—	—	84
Common stock issued pursuant to:							
3% stock dividend	206,730	258	1,013	—	(1,271)	—	—
Stock options exercised	71,227	89	258	—	—	—	347
Tax benefit of stock options exercised	—	—	31	—	—	—	31
Repurchase of common stock	(197,026)	(246)	(968)	—	—	—	(1,214)
Cash paid—fractional shares	—	—	—	—	(9)	—	(9)
Balance, December 31, 2005	7,138,686	8,923	12,410	(914)	6,706	328	27,453
Net income	—	—	—	—	2,071	—	2,071
Other comprehensive loss	—	—	—	—	—	(158)	(158)
Release of ESOP shares	—	—	37	55	—	—	92
Common stock issued pursuant to:							
3% stock dividend	214,634	269	997	—	(1,266)	—	—
Stock options exercised	94,094	117	107	—	—	—	224
Tax benefit of stock options exercised	—	—	48	—	—	—	48
Repurchase of common stock	(23,864)	(30)	(115)	—	—	—	(145)
Cash paid—fractional shares	—	—	—	—	(9)	—	(9)
Stock compensation expense	—	—	57	—	—	—	57
Balance, December 31, 2006	7,423,550	9,279	13,541	(859)	7,502	170	29,633
Net income	—	—	—	—	2,959	—	2,959
Other comprehensive income	—	—	—	—	—	217	217
Release of ESOP shares	—	—	31	59	—	—	90
Common stock issued pursuant to:							
3% stock dividend	216,062	270	916	—	(1,186)	—	—
Stock options exercised	12,764	16	20	—	—	—	36
Tax benefit of stock options exercised	—	—	3	—	—	—	3
Repurchase of common stock	(237,669)	(297)	(1,107)	—	—	—	(1,404)
Cash paid—fractional shares	—	—	—	—	(9)	—	(9)
Stock compensation expense	—	—	49	—	—	—	49
Balance, December 31, 2007	7,414,707	$9,268	$ 13,453	$ (800)	$ 9,266	$ 387	$31,574

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

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
Years Ended December 31, 2007, 2006 and 2005

	2007	2006	2005
Cash flows from operating activities			
Net income	$ 2,959	$ 2,071	$ 1,517
Adjustments to reconcile net income to net cash			
Provided by operating activities:			
Depreciation	625	625	646
Net amortization of security premiums/discounts	(220)	(41)	37
Net amortization of mortgage servicing rights	407	382	390
Provision for loan losses	15	298	755
Deferred income taxes	205	439	52
Stock compensation	49	57	—
Net realized (gain) loss on available for sale securities	76	(60)	16
Income from mortgage loan sales	(957)	(764)	(554)
Proceeds from sales of loans held for sale	45,603	39,038	29,162
Origination of loans held for sale	(43,748)	(38,734)	(29,058)
(Gain) loss on sale of premises, equipment and other assets	(26)	9	(76)
Increase in cash surrender value of life insurance	(185)	(184)	(155)
(Gain) loss on sales of foreclosed real estate	2	24	(12)
Release of ESOP Shares	90	92	84
Net change in interest receivable	(280)	(250)	(252)
Net change in other assets	(866)	(243)	(13)
Net change in interest payable	93	134	67
Net change in other liabilities	302	(190)	316
Net cash provided by operating activities	4,144	2,703	2,922
Cash flows from investing activities			
Proceeds from sales, maturities and calls of securities available for sale	10,382	9,190	1,487
Purchase of securities available for sale	(23,744)	(11,480)	(8,777)
Net increase in loans	(33,588)	(17,165)	(14,332)
Proceeds from sale of premises, equipment and other assets	87	—	230
Purchase of premises and equipment	(758)	(813)	(776)
Proceeds from sales of foreclosed real estate	98	205	1,392
Net change in Federal Home Loan Bank stock	(157)	(313)	245
Net cash used by investing activities	(47,680)	(20,376)	(20,531)
Cash flows from financing activities			
Net increase in deposit accounts	15,057	35,624	27,037
Net increase (decrease) in short-term borrowed funds	18,888	5,136	(6,789)
Net decrease in long-term debt	(7,598)	(9,814)	—
Repurchases of common stock	(1,404)	(145)	(1,214)
Net proceeds from issuance of common stock	36	224	347
Tax benefit of stock options exercised	3	48	31
Cash paid for fractional shares	(9)	(9)	(9)
Net cash provided by financing activities	24,973	31,064	19,403
Decrease (increase) in cash and cash equivalents	(18,563)	13,391	1,794
Cash and cash equivalents, beginning of period	34,760	21,369	19,575
Cash and cash equivalents, end of period	$ 16,197	$ 34,760	$ 21,369
Supplemental disclosures of cash flow information			
Interest paid	$ 11,783	$ 10,568	$ 6,563
Income taxes paid	1,311	687	241
Supplemental schedule of non-cash investing and financing activities			
Increase (decrease) in fair value of securities available for sale, net of tax	217	(158)	(456)
Loans transferred to foreclosed real estate	60	262	1,064

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

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1 - Significant Accounting Policies

Nature of Business

Uwharrie Capital Corp (the “Company”) was incorporated under North Carolina law for the purpose of becoming the holding company for Bank of Stanly (“Stanly”). On July 1, 1993, Stanly became a wholly-owned subsidiary of the Company through a one-for-one exchange of the common stock of Stanly for common stock of the Company.

Stanly was incorporated on September 28, 1983, under the laws of the State of North Carolina and began operations on January 26, 1984 in Albemarle, North Carolina. Deposits with Stanly are insured by the Federal Deposit Insurance Corporation (“FDIC”). Stanly is under regulation of both the FDIC and the North Carolina State Banking Commission. Through its five branch locations in Stanly County, Stanly provides a wide range of deposit accounts, commercial, consumer, home equity and residential mortgage loans, safe deposit boxes and automated banking.

In 1987, Stanly established a wholly-owned subsidiary, BOS Agency, Inc. (“BOS Agency”), which engages in insurance product sales. In 1989, Stanly established a second wholly-owned subsidiary, BOS Financial Corporation, for the purpose of conducting business as a broker/dealer in securities. During 1993, BOS Financial Corporation changed its name to The Strategic Alliance Corporation (“Strategic Alliance”) and was registered as a broker/dealer by the National Association of Securities Dealers.

The Company formed a new subsidiary, Strategic Investment Advisors, Inc. (“SIA”), during 1999 to provide investment advisory and asset management services. This subsidiary is registered as an investment advisor with the Securities and Exchange Commission.

On January 19, 2000, the Company completed its acquisition of Anson BanCorp, Inc. and its subsidiary, Anson Savings Bank. The savings bank retained its North Carolina savings bank charter and became a wholly-owned subsidiary of Uwharrie Capital Corp as Anson Bank & Trust Company (“Anson”), operating out of its main office branch in Wadesboro.

On August 4, 2000, Stanly acquired another subsidiary, Gateway Mortgage, Inc. (“Gateway”), a mortgage origination company.

On April 10, 2003, the Company capitalized a new wholly-owned subsidiary bank, Cabarrus Bank & Trust Company (“Cabarrus”), located in Concord, North Carolina. As of that date, Cabarrus purchased two branch offices located in Cabarrus County from Stanly to begin its operation. Cabarrus operates as a commercial bank and provides a full range of banking services.

On April 7, 2004 Uwharrie Mortgage, Inc. was established as a subsidiary of the Company to serve in the capacity of trustee and substitute trustee under deeds of trust.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company, Stanly, Anson, Cabarrus, SIA and their subsidiaries, BOS Agency, Strategic Alliance and Gateway. All significant intercompany transactions and balances have been eliminated in consolidation.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1 - Significant Accounting Policies (Continued)

Use of Estimates

The preparation of financial statements, in conformity with accounting principles generally accepted in the United States of America, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses.

Cash and Cash Equivalents

For the purpose of presentation in the consolidated statements of cash flows, cash and cash equivalents are defined as those amounts included in the balance sheet captions “Cash and due from banks,” “Interest-earning deposits with banks,” and “Federal funds sold”.

Investment Securities Held To Maturity

Investment securities classified as held to maturity are debt securities the Company has both the intent and ability to hold to maturity regardless of changes in market conditions, liquidity needs or changes in general economic conditions. These securities are carried at cost adjusted for amortization of premium and accretion of discount, computed by the interest method over their contractual lives. Declines in the fair value of individual held to maturity securities below their cost that are other than temporary would result in write-downs of the individual securities to their fair value. Such write-downs would be included in earnings as realized losses. The Company had no securities held to maturity at December 31, 2007 and 2006.

Investment Securities Available for Sale

Investment securities available for sale consist of bonds and notes not classified as trading securities nor as held to maturity securities. Unrealized holding gains and losses on available for sale securities are reported as a net amount in other comprehensive income, net of income taxes. Gains and losses on the sale of available for sale securities are determined using the specific identification method. Declines in the fair value of individual available for sale securities below their cost that are other than temporary would result in write-downs of the individual securities to their fair value. Such write-downs would be included in earnings as realized losses. Premiums and discounts are recognized in interest income using the interest method over the period to maturity.

Loans Held for Sale

Loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated fair value in the aggregate. Net unrealized losses, if any, are recognized through a valuation allowance by charges to income.

Loans

The Company grants mortgage, commercial and consumer loans to customers. The ability of the Company’s borrowers to honor their contracts is largely dependent upon the real estate and general economic conditions in the Company’s market area. Loans that management has the

Note 1 - Significant Accounting Policies (Continued)

intent and ability to hold for the foreseeable future or until maturity or pay-off are reported at their outstanding unpaid principal balances adjusted for charge-offs, the allowance for loan losses, and any deferred fees or costs. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the related loan yield using the interest method.

The accrual of interest on mortgage and commercial loans is discontinued at the time the loan is 90 days delinquent unless the credit is well-secured and in process of collection. Credit card loans and other personal loans are typically charged off no later than 180 days past due. In all cases, loans are placed on nonaccrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

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

Allowance for Loan Losses

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management’s periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower’s ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available. In addition, regulatory examiners may require the Company to recognize adjustments to the allowance for loan loss based on their judgment about information available to them at the time of their assessment.

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

Note 1 - Significant Accounting Policies (Continued)

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Company does not separately identify individual consumer, residential and other loans for impairment disclosures.

Servicing Rights

The Company capitalizes servicing rights when loans are either securitized or sold and the loan servicing is retained. The cost of servicing rights is amortized in proportion to and over the estimated period of net servicing revenues. The amortization of servicing rights is recognized in the statement of income as an offset to other noninterest income. Servicing assets are evaluated for impairment based upon the fair value. Fair value is determined using prices for similar assets with similar characteristics, when available, or based upon discounted cash flows using market-based assumptions. Impairment is recognized through a valuation allowance.

Transfers of Financial Assets

Transfers of financial assets are accounted for as sales when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Foreclosed Real Estate

Real estate properties acquired through foreclosure or other proceedings are initially recorded at fair value upon foreclosure, establishing a new cost basis. After foreclosure, valuations are performed and the foreclosed property is adjusted to the lower of cost or fair value of the properties, less costs to sell. Any write-down at the time of transfer to foreclosed properties is charged to the allowance for loan losses. Subsequent write-downs are charged to other expenses. Property is evaluated regularly to ensure that the recorded amount is supported by its current fair value.

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation. Land is carried at cost. Additions and major replacements or betterments which extend the useful lives of premises and equipment are capitalized. Maintenance, repairs and minor improvements are expensed as incurred. Depreciation is computed principally by the straight-line method over estimated useful lives, except in the case of leasehold improvements, which are amortized over the term of the leases, if shorter. Useful lives range from five to seven years for furniture, fixtures and equipment, to ten to thirty-nine years for leasehold improvements and buildings, respectively. Upon retirement or other disposition of the assets, the cost and the related accumulated depreciation are removed from the accounts and any gains or losses are reflected in income.

Federal Home Loan Bank Stock

As a requirement for membership, the banks invest in the stock of the Federal Home Loan Bank of Atlanta (“FHLB”). This investment is carried at cost. Due to the redemption provisions of the FHLB, the Company estimated that fair value approximates cost and that this investment was not impaired.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1 - Significant Accounting Policies (Continued)

Goodwill

Goodwill resulted from the 2000 acquisition of Anson BanCorp, Inc. and its subsidiary, Anson Savings Bank. Goodwill is evaluated for impairment annually, or more frequently if circumstances indicate potential impairment.

Stock-Based Compensation

Effective January 1, 2006, the Company adopted Statement of Financial Accounting Standards No. 123R (revised 2004, "Share-Based Payment", ("SFAS No. 123R")) which was issued by the FASB in December 2004. SFAS No. 123R revises SFAS No. 123 "Accounting for Stock-Based Compensation" and supersedes APB Opinion No. 25 "Accounting for Stock Issued to Employees" (APB No. 25) and its related interpretations. SFAS No. 123R requires recognition of the cost of employee services received in exchange for an award of equity instruments in the financial statements over the period the employee is required to perform the services in exchange for the award (presumptively the vesting period). SFAS No. 123R also requires measurement of the cost of employee services received in exchange for an award based on the grant-date fair value of the award. SFAS No. 123R also amends SFAS No. 95 "Statement of Cash Flows", to require that excess tax benefits be reported as financing cash inflows, rather than as a reduction of taxes paid, which is included within operating cash flows.

The Company adopted SFAS No. 123R using the modified prospective application as permitted under SFAS No. 123R. Accordingly, prior period amounts have not been restated. Under this application, the Company is required to record compensation expense for all awards granted after the date of adoption and for the unvested portion of previously granted awards that remain outstanding at the date of adoption. Prior to the adoption of SFAS No. 123R, the Company used the intrinsic value method as prescribed by APB No. 25 and thus recognized no compensation expense for options granted with exercise prices equal to the fair market value of the common stock on the date of grant.

During 1996, the Company adopted the 1996 Incentive Stock Option Plan ("SOP") and the Employee Stock Purchase Plan ("SPP"), under which options to purchase shares of the Company's common stock may be granted to officers and eligible employees. Options granted under the SOP are exercisable in established increments according to vesting schedules, generally three to five years, and will expire if not exercised within ten years of the date of grant. Options granted under the SPP are fully vested at the date of grant and expire, if not exercised, within two years of the grant date. Both of these plans expired in 2006. At December 31, 2007, the SOP had 504,207 options still outstanding and the SPP had no options outstanding.

During 2006, the Company adopted the 2006 Incentive Stock Option Plan ("SOP II") and the Employee Stock Purchase Plan ("SPP II"), under which options to purchase shares of the Company's common stock may be granted to officers and eligible employees. Options granted under the SOP II are exercisable in established increments according to vesting schedules, generally three to five years, and will expire if not exercised within ten years of the date of grant. Options granted under the SPP II are fully vested at the date of grant and expire, if not exercised, within two years of the grant date. At December 31, 2007 there were no options outstanding under the SOP II or the SPP II. The compensation cost charged against income for the Company's options, plans for the twelve months ended December 31, 2007, and 2006 was $49 thousand and $57 thousand, respectively.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1 - Significant Accounting Policies (Continued)

The fair market value of each option award is estimated on the date of grant using the Black-Scholes option pricing model. There were no shares granted during the twelve months ended December 31, 2007. There were 15,450 shares granted during 2006 under the SOP II. The fair value at the grant date was $1.55 using the following assumptions; a risk-free interest rate of 4.5%, a dividend yield of 0%, an expected life equal to 70% of the term of the option, and volatility of 14%. These shares were forfeited in 2007. All options granted in 2005 were forfeited in 2006.

The following is a summary of stock option activity for the twelve months ended December 31, 2007:

	Shares	Weighted Average Exercise Price	Aggregate Intrinsic Value (in thousands)
Outstanding at December 31, 2006	535,546	$ 4.59	
Granted	—	—	
Exercised	(13,144)	2.74	
Forfeited	(18,195)	5.46	
Outstanding at December 31, 2007	504,207	4.61	$ 576
Options exercisable at December 31, 2007	473,088	4.55	568

A summary of the status of the Company's non-vested stock options as of December 31, 2007, and changes during the year then ended is presented below:

	Shares	Weighted Average Grant Date Fair Value
Non-vested December 31, 2006	81,276	$ 1.38
Granted	—	—
Vested	(34,707)	1.23
Forfeited	(15,450)	1.62
Non-vested December 31, 2007	31,119	1.44

The grant date fair value of stock options vested over the twelve months ended December 31, 2007, 2006 and 2005 was $42 thousand, $64 thousand and $101 thousand, respectively.

As of December 31, 2007, there was $31 thousand of total unrecognized compensation cost related to non-vested share-based compensation arrangements granted under all of the Company's stock benefit plans. That cost is expected to be recognized over a weighted-average period of 1.47 years.

The Company funds the option shares from authorized but unissued shares. The Company does not typically purchase shares to fulfill the obligations of the stock benefit plans. Company policy does allow option holders to exercise options with seasoned shares.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1 - Significant Accounting Policies (Continued)

For the twelve months ended December 31, 2007, 2006 and 2005 the intrinsic value of options exercised was $38 thousand, $332 thousand, and $114 thousand, respectively.

The following illustrates the effect on net income available to common stockholders if the Company had applied the fair value recognition provisions of SFAS No. 123 to the results for the twelve months ended December 31, 2005. (in thousands, except per share data):

	2005
Net income as reported	$1,517
Add: Stock-based employee compensation expenses included in reported net income, net of related income tax effects	—
Less: Stock-based compensation determined under fair value based method of all awards, net of related income taxes	(136)
Net income, pro forma	$1,381
Net income per share:	
Basic net income per common share	
As reported	$ .20
Pro forma	.19
Diluted net income per share	
As reported	.20
Pro forma	.18

Income Taxes

The Company and its subsidiaries file a consolidated Federal income tax return and separate North Carolina income tax returns. The provision for income taxes in the accompanying consolidated financial statements is provided on a liability method whereby deferred tax assets are recognized for deductible temporary differences and operating loss and tax credit carryforwards and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

Fair Value of Financial Instruments

SFAS No. 107, Disclosures About Fair Value of Financial Instruments, requires disclosure of fair value information about financial instruments, whether or not recognized in the consolidated balance sheets, for which it is practicable to estimate that value. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. In that regard, the derived fair value estimates cannot be substantiated by comparison to independent markets and, in many cases, could not be realized in immediate settlement of the instrument. Statement No. 107 excludes certain financial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented do not represent the underlying market value or liquidation value of the Company.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1 - Significant Accounting Policies (Continued)

The following methods and assumptions were used by the Company in estimating the fair value of its financial instruments:

Carrying amounts approximate fair values for cash and due from banks; interest-bearing deposits with banks; federal funds sold; interest receivable and payable; variable rate loans that reprice frequently where no significant change in credit risk has occurred; bank owned life insurance; Federal Home Loan Bank stock; variable rate money market, demand, interest checking and savings accounts; variable rate time deposits; federal funds purchased and securities sold under repurchase agreements and short-term borrowed funds.

Quoted market prices, where available, or if not available, quoted market prices of comparable instruments are used for investment securities.

Discounted cash flows using interest rates currently being offered on instruments with similar terms and with similar credit quality are used for long-term debt; all loans (except variable rate loans described above) and fixed rate time deposits.

Comprehensive Income

The Company reports as comprehensive income all changes in shareholders' equity during the year from sources other than shareholders. Other comprehensive income refers to all components (revenues, expenses, gains, and losses) of comprehensive income that are excluded from net income. The Company's only component of other comprehensive income is unrealized gains and losses, net of income tax, on investment securities available for sale.

Earnings per Common Share

The Company issued 3% stock dividends in 2007, 2006 and 2005. All references in these consolidated financial statements to earnings per common share and weighted average common and common equivalent shares outstanding have been adjusted for the effect of these stock dividends. In 2006, there were 15,450 stock options outstanding that were anti-dilutive since the exercise price exceeded the average market price. There were no anti-dilutive stock options outstanding during 2007 or 2005.

Basic earnings per share ("EPS") excludes dilution and is computed by dividing income available to common shareholders by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the entity.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1 - Significant Accounting Policies (Continued)

The computation of weighted average shares used in the calculation of basic and dilutive earnings per share is summarized below:

	2007	2006	2005
Weighted average number of common shares used in computing basic net income per common share	7,527,997	7,623,532	7,635,271
Effect of ESOP shares	(145,964)	(161,417)	(175,741)
Adjusted weighted average number of common shares used in computing basic net income per common share	7,382,033	7,462,115	7,459,530
Effect of dilutive stock options	100,328	112,741	181,806
Weighted average number of common shares and dilutive potential common shares used in computing diluted net income per common share	7,482,361	7,574,856	7,641,336

Recent Accounting Pronouncements

FIN 48

The Company adopted the Financial Accounting Standards Board's Interpretation No. 48 "Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109" ("FIN 48"), effective January 1, 2007. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in financial statements and requires the impact of a tax position to be recognized in the financial statements if that position is more likely than not of being sustained by the taxing authority. The adoption of FIN 48 did not have a material effect on our consolidated financial position or results of operations and unrecognized tax benefits as of December 31, 2007 and 2006 were immaterial. The Company classifies interest and penalties related to income tax assessments, if any, in income tax expense in the consolidated statement of operations and interest and penalties recognized in 2007, 2006, and 2005 were immaterial. Fiscal years ending on or after December 31, 2003 are subject to examination by federal and state tax authorities.

SFAS 156

The provisions of Statement of Financial Accounting Standards No.156 ("SFAS 156"), Accounting for Servicing of Financial Assets, an amendment of FASB Statement No. 10, were effective beginning January 1, 2007. The adoption of the provisions of SFAS No. 156 had no effect on financial position or results of operations.

SFAS 157

Statement of Financial Accounting Standards No. 157 ("SFAS 157"), Fair Value Measurements, defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007. The Company is in the process of evaluating the impact of the adoption of SFAS No. 157 on the consolidated financial statements.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 1 - Significant Accounting Policies (Continued)

SFAS 159

Statement of Financial Accounting Standards No. 159 ("SFAS 159"), The Fair Value Option for Financial Assets and Financial Liabilities, permits entities to choose to measure many financial instruments and certain other items at fair value. The objective of this standard is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This statement is effective for fiscal years beginning after November 15, 2007, with early adoption permitted under certain circumstances. The Company has chosen not to adopt the provision of SFAS 159 on an early basis. The Company has evaluated this statement and does not believe it will have a material effect on the Company's consolidated financial statements.

EITF 06-4

The Emerging Issues Task Force (EITF) reached a consensus at its September 2006 meeting regarding EITF 06-4, Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements. The scope of EITF 06-4 is limited to the recognition of a liability and related compensation costs for endorsement split-dollar life insurance policies that provide a benefit to an employee that extends to postretirement periods. Therefore, this EITF would not apply to a split-dollar life insurance arrangement that provides a specified benefit to an employee that is limited to the employee's active service period with an employer. This EITF 06-4 is effective for fiscal years beginning after December 15, 2007, with earlier application permitted. The Company adopted EITF 06-4 on January 1, 2008 and it had the effect of reducing beginning consolidated undivided profits by approximately $273,000.

From time to time, the FASB issues exposure drafts of proposed statements of financial accounting standards. Such exposure drafts are subject to comment from the public, to revisions by the FASB and to final issuance by the FASB as statements of financial accounting standards. Management considers the effect of the proposed statements on the consolidated financial statements of the Company and monitors the status of changes to and proposed effective dates of exposure drafts.

Reclassification

Certain amounts in the 2006 and 2005 financial statements have been reclassified to conform to the 2007 presentation. The reclassifications had no effect on net income or shareholders' equity as previously reported.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 2 - Investment Securities

Carrying amounts and fair values of securities available for sale are summarized below:

December 31, 2007	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
		(dollars in thousands)		
U.S. Treasury	$ 2,997	$ —	$ 2	$ 2,995
U.S. Government agencies	6,506	62	—	6,568
Mortgage-backed securities and CMO's	28,179	197	84	28,292
State and political subdivisions	12,187	452	5	12,634
Corporate bonds	501	—	1	500
Total debt securities	50,370	711	92	50,989
Equity securities	8	8	—	16
Total securities available for sale	$ 50,378	$ 719	$ 92	$51,005

December 31, 2006	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
		(dollars in thousands)		
U.S. Treasury	$ 2,992	$ —	$ 78	$ 2,914
U.S. Government agencies	7,509	—	149	7,360
Mortgage-backed securities and CMO's	12,918	38	50	12,906
State and political subdivisions	12,931	521	26	13,426
Corporate bonds	514	6	—	520
Total debt securities	36,864	565	303	37,126
Equity securities	8	16	—	24
Total securities available for sale	$ 36,872	$ 581	$ 303	$37,150

Results from sales of securities available for sale for the years ended December 31, 2007, 2006 and 2005 are as follows:

	2007	2006	2005
	(dollars in thousands)		
Gross proceeds from sales	$4,643	$2,885	$1,295
Realized gains from sales	$ —	$ 60	$ 4
Realized losses from sales	(76)	—	(20)
Net realized gains (losses)	$ (76)	$ 60	$ (16)

At December 31, 2007, 2006 and 2005 securities available for sale with a carrying amount of $15.2 million, $16.6 million and $13.1 million, respectively, were pledged as collateral on public deposits and for other purposes as required or permitted by law.

The following tables show the gross unrealized losses and fair value of investments, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2007 and 2006. These unrealized losses on investment securities are a result of temporary fluctuations in the market prices due to a rise in interest rates, which will adjust if rates decline, and are in no way a reflection of the quality of the investments. At December 31, 2007 the unrealized losses related to three U.S. Treasuries, one corporate bond, fifteen mortgage backed securities and CMOs, and four state and political subdivisions securities. All unrealized losses on investment securities are considered by management to be temporary given the credit ratings on these investment securities and management's intent and ability to hold these investments until maturity.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 2 - Investment Securities (Continued)

December 31, 2007	Less than 12 Months Fair Value	Less than 12 Months Unrealized Losses	12 Months or More Fair Value	12 Months or More Unrealized Losses	Total Fair Value	Total Unrealized Losses
			(dollars in thousands)			
Securities available for sale:						
U.S. Treasury	$ —	$ —	$ 2,995	$ 2	$ 2,995	$ 2
Mortgage-backed securities and CMO's	8,776	40	2,347	44	11,123	84
State and political subdivisions	751	5	—	—	751	5
	$ 9,527	$ 45	$ 5,342	$ 46	$ 14,869	$ 91
December 31, 2006						
Securities available for sale:						
U.S. Treasury	$ —	$ —	$ 2,992	$ 78	$ 2,992	$ 78
U.S. Government agencies	—	—	7,360	149	7,360	149
Mortgage-backed securities and CMO's	7,391	38	1,684	12	9,075	50
State and political subdivisions	1,025	16	1,464	10	2,489	26
	$ 8,416	$ 54	$ 13,500	$ 249	$ 21,916	$ 303

Note 3 - Loans Held for Investment

The composition of net loans held for investment as of December 31, 2007 and 2006 is as follows:

	2007	2006
	(dollars in thousands)	
Commercial	$ 37,724	$ 36,406
Real estate - construction	46,546	27,342
Real estate - residential	135,842	126,111
Real estate - commercial	86,593	84,744
Consumer	15,022	13,262
Other	143	133
	321,870	287,998
Less:		
Allowance for loan losses	(3,510)	(3,171)
Deferred loan (fees) costs, net	117	137
Loans held for investment, net	$318,477	$284,964

Although the subsidiary banks' loan portfolios are diversified, there is a concentration of mortgage real estate loans, primarily one to four family residential mortgage loans, which represent 42.20% of total loans. Additionally, there is concentration in commercial loans secured primarily by real estate, to finance manufacturing buildings, shopping center locations, commercial land development, commercial buildings and equipment that comprise 26.90% of total loans. There is not a concentration of a particular type of credit in this group of commercial loans.

Impaired loans, which consisted of nonaccrual loans and other loans identified by management as impaired, totaled $7.5 million and $6.8 million at December 31, 2007 and 2006, respectively. The nonaccrual status of these loans had the effect of reducing net income by $6,077 in 2007 and $72,800 in 2006. Of the $7.5 million in impaired loans at December 31, 2007, $5.3 million carried an allowance of $1.3 million while $2.2 million were evaluated and required no specific allowance. Of the $6.8 million in impaired loans at December 31, 2006, $4.8 million carried an allowance of $1.6 million while $2.0 million required no specific allowance. The allowance for impaired loans amounted to $1.3 million at December 31, 2007 and $1.6 million at December 31, 2006. Loans past due 90 days and still accruing interest were $0 and $499,982 at December 31, 2007 and 2006, respectively. Restructured loans, excluding those included in impaired loans, amounted to $168,489 at December 31, 2007.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 3 - Loans Held for Investment (Continued)

The carrying value of foreclosed properties held as other real estate was $163,452 and $202,976 at December 31, 2007 and 2006, respectively.

The Company's loan policies are written to address loan-to-value ratios and collateralization methods with respect to each lending category. Consideration is given to the economic and credit risk of lending areas and customers associated with each category.

Note 4 - Allowance for Loan Losses

Changes in the allowance for loan losses for the years ended December 31, 2007, 2006 and 2005 are presented below:

	2007	2006	2005
		(dollars in thousands)	
Balance, beginning of year	$3,171	$ 4,482	$ 4,983
Charge-offs	(224)	(1,687)	(1,378)
Recoveries	548	78	122
Provision charged against income	15	298	755
Balance, end of year	$3,510	$ 3,171	$ 4,482

Note 5 - Servicing Assets

Loans serviced for others are not included in the accompanying consolidated balance sheets. The unpaid principal balances of mortgage and other loans serviced for others were approximately $205 million and $186 million at December 31, 2007 and 2006, respectively. The carrying value of capitalized servicing rights, net of valuation allowances, is included in other assets. A summary of mortgage servicing rights follows:

	2007	2006	2005
		(dollars in thousands)	
Beginning of year mortgage servicing rights:	$1,244	$1,138	$1,236
Amounts capitalized	484	488	292
Amortization	(407)	(382)	(390)
End of year	$1,321	$1,244	$1,138

Amortization expense is estimated as follows:

Year ending December 31, (dollars in thousands)	
2008	$ 312
2009	270
2010	228
2011	187
2012	145
Thereafter	179
Total	$1,321

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 6 - Premises and Equipment

The major classes of premises and equipment and the total accumulated depreciation at December 31, 2007 and 2006 are listed below:

	2007	2006
	(dollars in thousands)	
Land	$ 2,915	$ 2,785
Building and improvements	6,579	6,280
Furniture and equipment	4,946	4,740
	14,440	13,805
Less accumulated depreciation	5,689	5,187
Total	$ 8,751	$ 8,618

The Company will begin renovations on one of their buildings during the first quarter of 2008. The contract bid for this project is $1.4 million. The Company has also entered into an agreement to purchase an adjacent piece of property for future parking needs for $255 thousand.

Note 7 - Leases

The Company's subsidiary, Bank of Stanly has entered into a noncancelable operating lease for a branch location in Albemarle that expires in 2008, with annual rental payments of $19 thousand. The lease has one five year renewal option at the expiration of the initial term. Stanly has also entered into a noncancelable operating lease for a branch location in Locust that expires in 2008 with annual rental payments of $42 thousand. The lease has two one year renewal options at the expiration of the initial term.

The Company's subsidiary, Cabarrus Bank and Trust has entered into a noncancelable operating lease for an administrative office location in Concord that expires in 2017 with annual rental payments of $60 thousand. The lease has two five year renewal options at the expiration of the initial term.

Future minimum lease payments under these leases for years subsequent to December 31, 2007 are as follows:

Year ending December 31, (dollars in thousands)	
2008	$121
2009	120
2010	113
2011	79
2012	78
Thereafter	293
Total	$804

Total rental expense related to the operating leases was $76,449, $23,807 and $18,575 for the years ended December 31, 2007, 2006 and 2005 respectively, and is included in occupancy expense.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 8 - Deposits

The composition of deposits at December 31, 2007 and 2006 is as follows:

	2007		2006	
	Amount	Percentage of Total	Amount	Percentage of Total
	(dollars in thousands)			
Demand deposits	$ 46,597	14%	$ 48,149	16%
Interest checking and money market	102,411	32%	101,470	32%
Savings	26,200	8%	27,833	9%
Time deposits $100,000 and over	54,729	17%	48,450	16%
Other time deposits	94,720	29%	83,698	27%
Total	$324,657	100%	$309,600	100%

The maturities of fixed-rate time deposits at December 31, 2007 are reflected in the table below:

Year ending December 31,	Time Deposits $100,000 and Over	Other Time Deposits
	(dollars in thousands)	
2008	$50,038	$84,012
2009	3,674	6,783
2010	546	2,799
2011	471	778
2012	—	348
Total	$54,729	$94,720

Note 9 - Short-Term Borrowed Funds

The following tables set forth certain information regarding the amounts, year-end weighted average rates, average balances, weighted average rate, and maximum month-end balances for short-term borrowed funds, at and during 2007 and 2006.

	2007		2006	
At year-end	Amount	Rate	Amount	Rate
Federal funds purchased	$ 5,900	4.60%	$ —	—
Securities sold under repurchase agreements	1,604	2.82%	2,025	4.31%
Master notes	9,630	2.67%	6,608	4.34%
Notes payable	7	6.00%	407	8.21%
Short-term advances from FHLB	14,787	3.85%	4,000	4.57%
	$31,928	3.58%	$13,040	3.12%

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 9 - Short-Term Borrowed Funds (Continued)

	2007 Amount	2007 Rate	2006 Amount	2006 Rate
	(dollars in thousands)			
Average for the year				
Federal funds purchased	$ 1,331	5.22%	$ 1,478	5.10%
Securities sold under repurchase agreements	1,798	3.81%	2,980	4.33%
Master notes	12,058	3.95%	7,692	4.29%
Notes payable	302	6.22%	407	6.94%
Short-term advances from FHLB	13,882	3.54%	4,129	4.15%
	$29,371	3.84%	$16,686	4.40%

	2007	2006
	(dollars in thousands)	
Maximum month-end balance		
Federal funds purchased	$ 6,150	$11,000
Securities sold under repurchase agreements	2,194	3,439
Master notes	15,830	11,007
Notes payable	407	407
Short-term advances from FHLB	16,587	12,000

Federal funds purchased represent unsecured overnight borrowings from other financial institutions. Securities sold under repurchase agreements represent short-term borrowings collateralized by securities of the United States government or its agencies. Master notes represent an overnight investment in commercial paper issued by the Company to customers of it's subsidiary banks, where an agreement is in place.

The subsidiary banks have combined available lines of credit for federal funds in the amount of $14.3 million at December 31, 2007.

Note 10 - Long-Term Debt

The Company has a line of credit with the Federal Home Loan Bank secured by qualifying first lien and second mortgage loans and commercial real estate loans with eligible collateral value of $79.6 million at December 31, 2007. The long-term advances under this line amounted to $15.0 million and $14.0 million at December 31, 2007 and 2006, respectively. Interest rates ranged from 2.96% to 7.52% in both 2007 and 2006. Two subsidiary banks also have standby letters of credit issued by the Federal Home Loan Bank to be used as collateral for public funds deposits. The amount of the letters of credit was $14.0 million at December 31, 2007.

On April 30, 2001, the Company borrowed $4.0 million from a bank at an interest rate of prime less one percent. The note is payable in annual installments of $400 thousand. The balance outstanding at December 31, 2006 was $2.0 million. This loan was paid off on September 25, 2007.

On September 25, 2007, the Company borrowed $6.6 million from a bank at an interest rate of prime less one percent. This is a two year note that is payable at maturity, with interest payable quarterly.

On September 26, 2002, the Company issued $5.2 million of junior subordinated debentures to Uwharrie Statutory Trust I in exchange for the proceeds of the trust preferred securities issued

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 10 - Long-Term Debt (Continued)

by the Trust. The junior subordinated debentures were included in long-term debt and the Company's equity interest in the Trust was included in other assets. The junior subordinated debentures paid interest quarterly at an annual rate, reset quarterly, equal to LIBOR plus 3.40%. The Company fully and unconditionally guaranteed the trust preferred securities through the combined operation of the junior subordinated debentures and other related documents. The Company's obligation under the guarantee was unsecured and subordinate to senior and subordinated indebtedness of the Company.

The trust preferred securities presently qualify as Tier 1 regulatory capital and are reported in Federal Reserve regulatory reports as a minority interest in a consolidated subsidiary. The junior subordinated debentures do not qualify as Tier 1 regulatory capital. On March 1, 2005, the Board of Governors of the Federal Reserve adopted a final rule that allows the continued limited inclusion of trust preferred securities in Tier 1 capital. The final rule limits trust preferred securities to 25 percent of all core capital elements, net of goodwill. Amounts of restricted core capital elements in excess of these limits generally may be included in Tier 2 capital. The final rule provides a five-year transition period, ending March 31, 2009, for application of the quantitative limits.

On September 26, 2007, the Company redeemed the $5.2 million in junior subordinated debentures. After the redemption, the Company still remained well capitalized under the regulatory guidelines for bank holding companies.

On November 19, 2002, the Company executed a mortgage in the amount of $129,000 for the purchase of property for branch expansion. This loan bears interest at 6.00% and is to be paid in 60 quarterly installments of $3,277. The outstanding principal balance on this note was $98,000 at December 31, 2007.

As of December 31, 2007, the scheduled maturities of these advances and notes payable are as follows:

Year ending December 31, (dollars in thousands)	
2009	$ 9,608
2010	5,009
2011	6,009
2012	1,009
2013	9
Thereafter	47
Total	$21,691

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 11 - Income Tax Matters

The significant components of income tax expense for the years ended December 31 are summarized as follows:

	2007	2006	2005
	(dollars in thousands)		
Current tax expense:			
Federal	$ 844	$ 217	$ 379
State	238	177	92
Total	1,082	394	471
Deferred tax expense:			
Federal	198	343	38
State	7	96	14
Total	205	439	52
Net provision for income taxes	$ 1,287	$ 833	$ 523

The difference between the provision for income taxes and the amounts computed by applying the statutory federal income tax rate of 34% to income before income taxes is summarized below:

	2007	2006	2005
	(dollars in thousands)		
Tax computed at the statutory federal rate	$ 1,443	$ 987	$ 693
Increases (decrease) resulting from:			
Tax exempt interest, net	(245)	(245)	(224)
State income taxes, net of federal benefit	162	143	70
Other	(73)	(52)	(16)
Provision for income taxes	$ 1,287	$ 833	$ 523

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of deferred taxes at December 31 are as follows:

	2007	2006	2005
	(dollars in thousands)		
Deferred tax assets relating to:			
Allowance for loan losses	$ 935	$ 912	$1,496
Deferred compensation	357	316	279
Other	—	236	130
Valuation allowance	(10)	(12)	(8)
Total deferred tax assets	$ 1,282	$1,452	$1,897
Deferred tax liabilities relating to:			
Net unrealized gain on securities available for sale	$ (241)	$ (107)	$ (206)
Premises and equipment	(369)	(364)	(392)
Deferred loans fees and costs	(213)	(212)	(218)
Loan servicing	(78)	(71)	(60)
Prepaid expenses	(110)	(96)	(79)
Other	(8)	—	—
Total deferred tax liabilities	(1,019)	(850)	(955)
Net recorded deferred tax asset	$ 263	$ 602	$ 942

The net deferred tax asset is included in other assets on the accompanying consolidated balance sheets.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 12 - Commitments and Contingencies

Financial Instruments with Off-Balance Sheet Risk

The subsidiary banks are parties to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of their customers. These financial instruments include commitments to extend credit, lines of credit and standby letters of credit. These instruments involve elements of credit risk in excess of amounts recognized in the accompanying financial statements.

The subsidiary banks' risks of loss with the unfunded loans and lines of credit or standby letters of credit are represented by the contractual amount of these instruments. The banks use the same credit policies in making commitments under such instruments as they do for on-balance sheet instruments. The amount of collateral obtained, if any, is based on management's credit evaluation of the borrower. Collateral held varies, but may include accounts receivable, inventory, real estate and time deposits with financial institutions. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Credit card commitments are unsecured. As of December 31, 2007 and 2006, outstanding financial instruments whose contract amounts represent credit risk were as follows:

	2007	2006
	(dollars in thousands)	
Commitments to extend credit	$79,162	$73,450
Credit card commitments	9,017	7,672
Standby letters of credit	1,641	616
	$89,820	$81,738

Contingencies

In the normal course of business, the Company is involved in various legal proceedings. In the opinion of management, any liability resulting from such proceedings would not have a material adverse effect on the consolidated financial statements.

Financial Instruments with Concentration of Credit Risk

The bank subsidiaries make commercial, agricultural, real estate mortgage, home equity and consumer loans primarily in Stanly, Anson and Cabarrus counties. A substantial portion of the Company's customers' ability to honor their contracts is dependent on the economy in these counties.

Although the Company's composition of loans is diversified, there is some concentration of mortgage loans in the total portfolio. The Bank Policy is to abide by real estate loan-to-value margin limits corresponding to guidelines issued by the federal supervisory agencies on March 19, 1993. Lending policy for all loans requires that they be supported by sufficient cash flows. Credit losses related to this real estate concentration are consistent with credit losses experienced in the portfolio as a whole.

Note 13 - Related Party Transactions

The Company has granted loans to certain directors and executive officers and their related interests. Such loans are made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other borrowers and,

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 13 - Related Party Transactions (Continued)

in management's opinion, do not involve more than the normal risk of collectibility. All loans to directors and executive officers or their interests are submitted to the Board of Directors for approval. A summary of loans to directors, executive officers and their related interests follows:

(dollars in thousands)

Balance at December 31, 2006	$ 22,459
Disbursements during the year	7,733
Collections during the year	(14,380)
Balance at December 31, 2007	$ 15,812

At December 31, 2007, the Company had approved, but unused lines of credit, totaling $2.2 million to executive officers, directors, officers and their related interests.

Note 14 - Regulatory Matters

The Company, and its bank subsidiaries, are subject to certain requirements imposed by state and federal banking statutes and regulations. These requirements, among other things, establish minimum levels of capital, restrict the amount of dividends that may be distributed, and require that reserves on deposit liabilities be maintained in the form of vault cash or noninterest-bearing deposits with the Federal Reserve Bank.

The Company and its subsidiary banks are subject to federal regulatory risk-based capital guidelines for banks and bank holding companies. Each must meet specific capital guidelines that involve quantitative measure of assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices which measure Total and Tier 1 Capital to risk-weighted assets and Tier 1 Capital to average assets. Quantitative measures established by regulation to ensure capital adequacy and the Company's consolidated capital ratios are set forth in the table below. The Company expects to meet or exceed these minimums without altering current operations or strategy.

December 31, 2007	Actual		Minimum For Capital Requirement		Minimum to Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
	(Dollars in thousands)					
Total Capital to Risk Weighted Assets:						
Consolidated	$33,713	10.2%	$26,346	8.00%	$ 32,933	10.00%
Bank of Stanly	27,035	12.2%	17,771	8.00%	22,214	10.00%
Anson Bank and Trust	4,511	12.5%	2,880	8.00%	3,600	10.00%
Cabarrus Bank and Trust	7,693	10.9%	5,653	8.00%	7,067	10.00%
Tier I Capital to Risk Weighted Assets:						
Consolidated	30,200	9.2%	13,173	4.00%	19,760	6.00%
Bank of Stanly	24,550	11.1%	8,885	4.00%	13,328	6.00%
Anson Bank and Trust	4,123	11.5%	1,440	4.00%	2,160	6.00%
Cabarrus Bank and Trust	7,053	10.0%	2,827	4.00%	4,240	6.00%

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 14 - Regulatory Matters (Continued)

Tier I Capital to						
Average Assets:						
Consolidated	30,200	7.6%	15,833	4.00%	19,791	5.00%
Bank of Stanly	24,550	9.1%	10,775	4.00%	13,468	5.00%
Anson Bank and Trust	4,123	8.8%	1,884	4.00%	2,355	5.00%
Cabarrus Bank and Trust	7,053	8.8%	3,212	4.00%	4,015	5.00%
December 31, 2006						
Total Capital to Risk						
Weighted Assets:						
Consolidated	$36,778	12.7%	$23,107	8.00%	$28,884	10.00%
Bank of Stanly	25,731	13.3%	15,406	8.00%	19,258	10.00%
Anson Bank and Trust	4,320	13.5%	2,563	8.00%	3,203	10.00%
Cabarrus Bank and Trust	7,013	11.0%	5,116	8.00%	6,395	10.00%
Tier I Capital to Risk						
Weighted Assets:						
Consolidated	33,601	11.6%	11,554	4.00%	17,330	6.00%
Bank of Stanly	23,402	12.2%	7,703	4.00%	11,555	6.00%
Anson Bank and Trust	3,983	12.4%	1,281	4.00%	1,922	6.00%
Cabarrus Bank and Trust	6,502	10.2%	2,558	4.00%	3,837	6.00%
Tier I Capital to						
Average Assets:						
Consolidated	33,601	8.8%	15,249	4.00%	19,061	5.00%
Bank of Stanly	23,402	9.0%	10,457	4.00%	13,072	5.00%
Anson Bank and Trust	3,983	8.8%	1,856	4.00%	2,320	5.00%
Cabarrus Bank and Trust	6,502	8.1%	3,223	4.00%	4,029	5.00%

As of December 31, 2007, the most recent notification from the Federal Deposit Insurance Corporation categorized all subsidiary banks as being well capitalized under the regulatory framework for prompt corrective action. There have been no conditions or events since such notification that management believes would have changed the categorizations.

For the reserve maintenance period in effect at December 31, 2007, the subsidiary banks were required to maintain reserve balances in cash or on deposit with the Federal Reserve Bank in the aggregate amount of $3.7 million as reserves on deposit liabilities.

Note 15 - Stock Matters

Employee Stock Plans

During 1996, the Company adopted the 1996 Incentive Stock Option Plan (“SOP”) and the Employee Stock Purchase Plan (“SPP”), under which options to purchase shares of the Company’s common stock may be granted to officers and eligible employees. Options granted under the SOP are exercisable in established increments according to vesting schedules, generally three to five years, and will expire if not exercised within ten years of the date of grant. Options granted under the SPP are fully vested at the date of grant and expire if not exercised within two years of the grant date. Both of these plans expired in 2006. At December 31, 2007, the SOP had 504,207 shares still outstanding and the SPP had no options outstanding.

During 2006, the Company adopted the 2006 Incentive Stock Option Plan (“SOP II”) and the Employee Stock Purchase Plan (“SPP II”), under which options to purchase shares of the Company’s common stock may be granted to officers and eligible employees. Options granted under the SOP are exercisable in established increments according to vesting schedules,

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 15 - Stock Matters (Continued)

generally three to five years, and will expire if not exercised within ten years of the date of grant. Options granted under the SPP II are fully vested at the date of grant and expire if not exercised within two years of the grant date. At December 31, 2007, neither the SOP II nor the SPP II had options outstanding.

Activity under all option plans, reflecting the effects of the 3% stock dividends issued in 2007, 2006 and 2005, are as follows:

	2007		2006		2005	
	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
Options outstanding at the beginning of the year	535,546	$ 4.59	703,650	$ 4.32	723,440	$ 4.22
Options granted	—	—	15,450	5.97	89,807	5.28
Options exercised	(13,144)	2.74	(99,686)	2.25	(75,565)	4.47
Forfeitures	(18,195)	5.46	(83,868)	5.32	(34,032)	4.60
Options outstanding at the end of the year	504,207	$ 4.61	535,546	$ 4.59	703,650	$ 4.32
Options exercisable at the end of the year	473,088	$ 4.55	454,272	$ 4.45	540,794	$ 4.03

At December 31, 2007, options outstanding had a weighted-average remaining term of 3.1 years. Total options outstanding at December 31, 2007 included 504,207 options exercisable at a range of $2.74 to $5.94 per share with a weighted average expected term of 3.1 years. Exercisable options at December 31, 2007 included 473,088 options exercisable at a range of $2.74 to $5.94 per share. At December 31, 2007, authorized shares of common stock reserved for future grants of options totaled 162,458 under the SOP II, and 100,227 under the SPP II.

Stock Repurchase Program

On February 21, 1995, the Company's Board of Directors authorized and approved a Stock Repurchase Program, to be reaffirmed annually, pursuant to which the Company may repurchase shares of the Company's common stock for the primary purpose of providing liquidity to its shareholders. Pursuant to stock repurchase authorizations and limitations, the Company purchased 237,669 shares during 2007 and 23,864 shares during 2006 at an aggregate purchase price of $1,403,749 and $145,093, respectively.

Note 16 - Employee and Director Benefit Plans

Employees' Savings Plus and Profit Sharing Plan

The Company has established an associate tax deferred savings plan under Section 401(k) of the Internal Revenue Code of 1986. All associates who are scheduled to work 500 hours or more are eligible to participate upon completion of six months of employment.

The Company's annual contribution to the plan was $192,776 in 2007, $169,982 in 2006 and $143,210 in 2005, determined as follows:

- A matching contribution equivalent to 50% of the first 6% of each associate's compensation contributed to the plan.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 16 - Employee and Director Benefit Plans (Continued)

- A discretionary contribution, subject to approval by the Board of Directors, limited to an amount not to exceed the maximum amount deductible for income tax purposes.

Directors' Deferred Compensation Plan

On March 1, 1994, the Company established a Directors' Deferred Compensation Plan in accordance with the laws of the State of North Carolina under which each Director could elect to defer receipt for services rendered to the Company as a Director during the term of his or her service by entering into a written deferred compensation election. This plan was closed to new participants in 2001; subsequently, only two directors continue to defer receipt of fees. The balance in deferred directors' compensation, not yet disbursed, was $195,938 and $212,382 at December 31, 2007 and 2006, respectively. Expense for the years ended December 31, 2007, 2006 and 2005 was $12,956, $12,283 and $13,931, respectively.

Employee Stock Ownership Plan

The Company established an Employee Stock Ownership Plan ("ESOP") to benefit all qualified employees. The ESOP purchased 284,676 dividend adjusted shares of common stock in 1999 with proceeds received from a loan of $1.2 million from the Company. The loan is to be repaid over eighteen years with interest at 8%. The loan may be prepaid without penalty. The unallocated shares of stock held by the ESOP are pledged as collateral for the loan. The ESOP is funded by contributions made by the Company and its subsidiaries in amounts sufficient to retire the debt. At December 31, 2007, the outstanding balance of the loan is $799,866 and is presented as a reduction of shareholders' equity.

Shares released as the debt is repaid and earnings from the common stock held by the ESOP are allocated among active participants on the basis of compensation in the year of allocation. Benefits vest 100% as they are allocated to participants. Dividends on unallocated shares may be used by the ESOP to repay the loan to the Company and are not reported as dividends in the financial statements. Dividends on allocated or committed to be allocated shares are credited to the accounts of the participants and reported as dividends in the consolidated financial statements.

Expenses of $317,256, $237,022 and $251,437 during the years ended December 31, 2007, 2006 and 2005, respectively, have been incurred in connection with the ESOP. At December 31, 2007, 201,740 shares held by the ESOP, including additional shares purchased, have been released or committed to be released to the ESOP's participants for purposes of computing earnings per share. The fair value of the unallocated shares amounted to approximately $783 thousand at December 31, 2007.

Supplemental Executive Retirement Plan

The Company has implemented a non-qualifying deferred compensation plan for certain executive officers. The Company has purchased life insurance policies in order to provide future funding of benefit payments. Certain of the plan benefits will accrue and vest during the period of employment, and will be paid in fixed monthly benefit payments from ten to fifteen years commencing with the officer's retirement at any time after attainment of the age specified in the

Note 16 - Employee and Director Benefit Plans (Continued)

officer's plan agreement. Other benefits will accrue based upon the performance of the underlying life insurance policies both during employment and after retirement. Such benefits will continue to accrue and be paid throughout the participant's life assuming satisfactory performance of the funding life insurance policy. The plan also provides for payment of death benefits and for payment of disability benefits in the event the officer becomes permanently disabled prior to attainment of retirement age.

Effective July 1, 2007, this plan was amended and restated for all but one of the plan participants to comply with Section 409A of the Internal Revenue Code. The participants' account liability balances as of December 31, 2007 will be transferred into a trust fund, where investments will be participant-directed. The plan is structured as a defined contribution plan and the Company's expected annual funding contribution for the participant has been calculated through the participant's expected retirement date. Under terms of the agreement, the Company has reserved the absolute right, at its sole discretion, to either fund or refrain from funding the plan. The plan also provides for payment of death benefits and for payment of disability benefits in the event the officer becomes permanently disabled prior to attainment of retirement age.

During 2007, 2006 and 2005 a provision of $199,328, $23,446 and $137,688, respectively, was expensed for future benefits to be provided under the plan. The liability accrued for compensation deferred under the plan amounts to $731,010, and $531,682 at December 31, 2007 and 2006, respectively.

Split-Dollar Life Insurance

The Company has entered into Life Insurance Endorsement Method Split Dollar Agreements with certain officers. Under these agreements, upon death of the officer, the Company first recovers the cash surrender value of the contract and then shares the remaining death benefits from insurance contracts, which are written with different carriers, with the designated beneficiaries of the officers. The death benefit to the officers' beneficiaries is a multiple of base salary at the time of the agreements. The Company, as owner of the policies, retains an interest in the life insurance proceeds and a 100% interest in the cash surrender value of the policies.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 17- Fair Values of Financial Instruments and Interest Rate Risk

The estimated fair values disclosed in the following table do not represent market values of all assets and liabilities of the Company and should not be interpreted to represent the underlying value of the Company. The following table reflects a comparison of carrying amounts and the estimated fair value of the financial instruments as of December 31, 2007 and 2006.

	2007		2006	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
	(dollars in thousands)			
Financial Assets				
Cash and cash equivalents	$ 16,197	$ 16,197	$ 34,760	$ 34,760
Securities available for sale	51,005	51,005	37,150	37,150
Loans, net of unearned income and allowance for loan losses	318,477	322,115	284,964	287,974
Loans held for sale	2,916	2,917	3,814	3,818
Other financial assets	9,510	9,510	8,888	8,888
Financial Liabilities				
Deposits	$324,657	$322,287	$309,600	$314,986
Short-term borrowings	31,928	31,928	13,040	13,040
Long-term debt	21,691	21,832	29,289	29,147
Other financial liabilities	596	596	503	503

At December 31, 2007, the subsidiary banks had outstanding standby letters of credit and commitments to extend credit. These off-balance sheet financial instruments are generally exercisable at the market rate prevailing at the date the underlying transaction will be completed; therefore, they were deemed to have no current fair value. See Note 12.

Interest Rate Risk

The Company assumes interest rate risk (the risk that general interest rate levels will change) in the course of its normal operations. As a result, fair values of the Company's financial instruments will change when interest rate levels change and that change may be either favorable or unfavorable to the Company. Management attempts to match maturities of assets and liabilities to the extent believed necessary to minimize interest rate risk. However, borrowers with fixed rate obligations are more likely to prepay in a falling rate environment and less likely to prepay in a rising rate environment. Conversely, depositors who are receiving fixed rates are more likely to withdraw funds before maturity in a rising rate environment and less likely to do so in a falling rate environment. Management monitors rates and maturities of assets and liabilities and attempts to minimize interest rate risk by adjusting terms of new loans and deposits and by investing in securities with terms that mitigate the Company's overall interest rate risk.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 18 - Parent Company Financial Data

The following is a summary of the condensed financial statements of Uwharrie Capital Corp:

Condensed Balance Sheets

	December 31, 2007	December 31, 2006
	(dollars in thousands)	
Assets		
Cash and demand deposits with bank subsidiaries	$ 289	$ 214
Interest-earning deposits with bank subsidiaries	9,830	6,865
Investments in:		
Bank subsidiaries	37,100	35,045
Nonbank subsidiaries	252	511
Other assets	770	894
Total assets	$48,241	$43,529
Liabilities and shareholders' equity		
Master notes	$ 9,630	$ 6,608
Long-term debt	6,600	2,000
Junior subordinated debentures	—	5,155
Other liabilities	437	133
Shareholders' equity	31,574	29,633
Total liabilities and shareholders' equity	$48,241	$43,529

Condensed Statement of Operations

	2007	2006	2005
		(dollars in thousands)	
Equity in earnings of subsidiaries	$3,734	$2,915	$1,922
Interest income	493	354	175
Management and service fees	4,227	3,854	3,797
Other income	119	190	107
Interest expense	1,029	921	625
Other operating expense	4,978	4,537	4,030
Income tax benefit	(393)	(216)	(171)
Net income	$2,959	$2,071	$1,517

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 18 - Parent Company Financial Data (Continued)

Condensed Statements of Cash Flows

	2007	2006	2005
	(dollars in thousands)		
Cash flows from operating activities			
Net income	$ 2,959	$ 2,071	$ 1,517
Adjustments to reconcile net income to net cash Provided (used) by operating activities:			
Equity in earnings of subsidiaries	(3,734)	(2,915)	(1,922)
Decrease in other assets	618	1,020	524
Increase (decrease) in other liabilities	304	(61)	(426)
Net cash provided (used) by operating activities	147	115	(307)
Cash flows from investing activities			
Dividends received from subsidiaries	1,800	—	1,000
Net cash provided by investing activities	1,800	—	1,000
Cash flows from financing activities			
Net increase (decrease) in master notes	3,022	2,153	(576)
Net increase (decrease) in long-term debt	4,600	(400)	(400)
Net decrease in subordinated debentures	(5,155)	—	—
Repurchase of common stock	(1,404)	(145)	(1,214)
Proceeds from issuance of common stock	36	224	347
Tax benefit of stock options exercised	3	48	31
Cash paid for fractional shares	(9)	(9)	(9)
Net cash provided (used) by financing activities	1,093	1,871	(1,821)
Net increase (decrease) in cash and cash equivalents	3,040	1,986	(1,128)
Cash and cash equivalents at beginning of period	7,079	5,093	6,221
Cash and cash equivalents at end of period	$10,119	$ 7,079	$ 5,093

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements

Note 19 - Quarterly Financial Data

	First	Second	Third	Fourth
	(in thousands, except per share data)			
2007				
Interest income	$ 6,542	$ 6,650	$ 6,846	$ 6,871
Interest expense	(3,058)	(2,972)	(2,964)	(2,882)
Net interest income	3,484	3,678	3,882	3,989
Provision for loan losses	—	138	(18)	(135)
Net interest income after provision for loan losses	3,484	3,816	3,864	3,854
Noninterest income	1,542	1,492	1,660	1,896
Noninterest expense	(4,083)	(4,273)	(4,414)	(4,592)
Income before taxes	943	1,035	1,110	1,158
Income taxes	285	318	336	348
Net income	$ 658	$ 717	$ 774	$ 810
Net income per common share				
Basic	$ 0.09	$ 0.10	$ 0.10	$ 0.11
Diluted	$ 0.09	$ 0.10	$ 0.10	$ 0.11

	First	Second	Third	Fourth
	(in thousands, except per share data)			
2006				
Interest income	$ 5,477	$ 5,972	$ 6,412	$ 6,492
Interest expense	(2,171)	(2,562)	(2,960)	(3,009)
Net interest income	3,306	3,410	3,452	3,483
Provision for loan losses	(145)	(99)	(54)	—
Net interest income after provision for loan losses	3,161	3,311	3,398	3,483
Noninterest income	1,261	1,277	1,437	1,494
Noninterest expense	(3,856)	(4,002)	(3,900)	(4,160)
Income before taxes	566	586	935	817
Income taxes	140	145	282	266
Net income	$ 426	$ 441	$ 653	$ 551
Net income per common share				
Basic	$ 0.06	$ 0.06	$ 0.09	$ 0.07
Diluted	$ 0.06	$ 0.06	$ 0.09	$ 0.06

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Selected Financial Data

Selected Financial Data
(In Thousands Except Per Share and Shares Outstanding Information)

	2007	2006	2005	2004	2003
Summary of Operations					
Interest income	$ 26,909	$ 24,353	$ 19,161	$ 15,906	$ 14,597
Interest expense	11,876	10,702	6,630	4,734	4,606
Net interest income	15,033	13,651	12,531	11,172	9,991
Provision for loan losses	15	298	755	2,092	593
Noninterest income	6,590	5,469	4,351	4,271	5,159
Noninterest expense	17,362	15,918	14,087	13,297	12,466
Income taxes	1,287	833	523	(199)	531
Net income	$ 2,959	$ 2,071	$ 1,517	$ 253	$ 1,560
Per Common Share					
Net income – basic (1)	$ 0.40	$ 0.28	$ 0.20	$ 0.03	$ 0.20
Net income – diluted (1)	0.40	0.27	0.20	0.03	0.20
Book value (1)	4.26	3.87	3.62	3.52	3.54
Weighted Average Shares					
Outstanding:					
Basic (1)	7,382,033	7,462,115	7,459,530	7,582,331	7,594,285
Diluted (1)	7,482,361	7,574,856	7,641,336	7,759,854	7,736,441
Ratios					
Return on average assets	0.75%	0.56%	0.45%	0.08%	0.57%
Return on average equity	9.73%	7.32%	5.58%	0.91%	5.78%
Average equity to average assets	7.73%	7.67%	8.14%	8.64%	9.86%
Selected Year-end Balances					
Assets	$ 411,944	$ 383,261	$ 350,190	$ 329,262	$ 300,529
Loans held for investment	321,987	288,135	272,842	260,835	235,151
Securities	51,005	37,150	35,016	28,524	27,707
Deposits	324,657	309,600	273,976	246,939	212,563
Borrowed funds	53,619	42,329	47,007	53,796	58,924
Shareholders' equity	31,574	29,633	27,453	27,156	27,852
Selected Average Balances					
Assets	$ 393,188	$ 368,781	$ 334,193	$ 321,093	$ 273,679
Loans held for investment	308,149	293,394	267,164	256,525	221,158
Securities	41,188	35,227	29,038	28,846	27,281
Deposits	312,261	289,742	254,591	234,424	188,803
Borrowed funds	48,075	48,510	50,265	57,296	56,263
Shareholders' equity	30,402	28,299	27,187	27,741	26,980

(1) Net income per share, book value per share, weighted average shares outstanding and shares outstanding at year-end for 2003 through 2007 have been adjusted to reflect 3% stock dividends issued in 2007, 2006, 2005, 2004 and 2003.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Management's Discussion And Analysis of Financial Condition And Results of Operations

A discussion and analysis of the Company's operating results and financial condition are presented in the following narrative and financial tables. The comments are intended to supplement and should be reviewed in conjunction with the consolidated financial statements and notes thereto appearing on pages 8-40. References to changes in assets and liabilities represent end of period balances unless otherwise noted. All references in this Annual Report to net income per share and weighted average common and common equivalent shares outstanding have been adjusted to reflect 3% stock dividends in 2007, 2006 and 2005. Statements contained in this annual report, which are not historical facts, are forward-looking statements, as that term is defined in the Private Securities Litigation Reform Act of 1995. Amounts herein could vary as a result of market and other factors. Such forward-looking statements are subject to risks and uncertainties which could cause actual results to differ materially from those currently anticipated due to a number of factors, which include, but are not limited to, factors discussed in documents filed by the Company with the Securities and Exchange Commission from time to time. Such forward-looking statements may be identified by the use of such words as "believe," "expect," "anticipate," "should," "might," "planned," "estimated," and "potential." Examples of forward-looking statements include, but are not limited to, estimates with respect to the financial condition, expected or anticipated revenue, results of operations and business of the Company that are subject to various factors which could cause actual results to differ materially from these estimates. These factors include, but are not limited to, general economic conditions, changes in interest rates, deposit flows, loan demand, real estate values, and competition; changes in accounting principles, policies, or guidelines; changes in legislation or regulation; and other economic, competitive, governmental, regulatory, and technological factors affecting the Company's operations, pricing, products and services.

Financial Condition at December 31, 2007 and December 31, 2006

The Company's total assets increased $28.6 million or 7.5% from $383.3 million at December 31, 2006 to $411.9 million at December 31, 2007. This increase resulted primarily from a $33.9 million increase in loans held for investment and a $13.8 million increase in securities available for sale. These increases were offset by a decrease of $18.6 million in cash and cash equivalents.

Loans held for investment increased $33.9 million, from $288.1 million at December 31, 2006 to $322.0 million at December 31, 2007, an increase of 11.8%. The growth was largely due to the 12.9%, or $30.8 million, increase in our loans secured by real estate. Our commercial and consumer portfolios experienced growth as well. Loans held for sale decreased $898 thousand, or 23.54%, for the period. At December 31, 2007 the allowance for loan losses was $3.5 million which represents 1.09% of the loan held for investment portfolio.

Investment securities increased 37.3% during 2007, from $37.2 million at December 31, 2006 to $51.0 million at December 31, 2007. Throughout the year we invested in mortgage backed securities and US Government Agencies. Mortgage backed securities increased $15.4 million, or 119.2%, during the period. During the year the Company executed a transaction selling $4.0 million in US Government Agencies realizing a loss of $75 thousand and reinvested the proceeds to improve its yield. The Company also had an additional sale realizing a loss of $1 thousand.

Cash and cash equivalents decreased by $18.6 million during 2007. This decrease was generated by a $17.5 million, or 100%, decrease in federal funds sold. At December 31, 2006 the Company had made a decision to keep a portion of its investments in short-term federal funds. During 2007 this short-term investment was used to fund growth in both our investment and loan portfolios resulting in an improved yield. Cash and due from banks declined $1.3 million while interest earning deposits with banks grew $285 thousand.

Other changes in our consolidated assets related to premises and equipment, interest receivable, Federal Home Loan Bank stock and bank owned life insurance. Premises and equipment increased due to the opening of a new retail branch in 2007, while interest receivable grew $280 thousand or 15.8% impacted by both loan and investment growth. Federal Home Loan Bank stock increased $157 thousand. Federal Home Loan Bank stock ownership is a requirement for member banks that utilize Federal Home Loan Bank for borrowing funds. The amount of stock owned by each member bank is based primarily on the amount of borrowings outstanding. Bank owned life insurance also experienced growth of $185 thousand.

Customer deposits continued to be our principal funding source in 2007, allowing us to fund the growth in assets discussed above. At December 31, 2007, deposits from our customers totaled $324.7 million, an increase of $15.1 million, or 4.9%, from $309.6 million at December 31, 2006. Time deposits grew $17.3 million, or 13.1%, during the period, while interest checking and money market accounts increased $941 thousand, or 0.9%. Offsetting the growth in the aforementioned areas were declines in savings accounts of 5.9%, or $1.6 million and demand, noninterest bearing of $1.6 million. During the past year with the increasing interest rate environment our customers have been moving their interest earning deposits into higher yielding deposit accounts.

The aforementioned growth in the loan and investment portfolios required the Company to increase net borrowings by $11.3 million during 2007. Borrowings consist of both short-term and long-term borrowed funds. The Company utilizes both short-term and long-term advances from the Federal Home Loan Bank. At December 31, 2007, $29.8 million of the total borrowings of $53.6 million were attributed to Federal Home Loan Bank advances.

The Company had long-term debt of $5.2 million of junior subordinated debentures to Uwharrie Statutory Trust I, issued in 2002, in exchange for the proceeds of the trust preferred securities issued by the Trust. The junior subordinated debentures were incurred in long-term debt and were redeemable on September 26, 2007 or afterwards. The annual interest rate was LIBOR plus 3.40%. During the third quarter, the Company made a decision to help improve its interest margin by refinancing the subordinated debt. The Company redeemed the debt during 2007, however market rates increased during the process and the replacement of the subordinated debt was placed on hold pending more favorable market conditions. The Company did replace the debt with other shorter term borrowings.

At December 31, 2007, total shareholders' equity was $31.6 million, an increase of $2.0 million from December 31, 2006. Net income for the period was $2.9 million and the Company received $36 thousand from the exercise of stock options. Unrealized gains on investment securities, net of tax, increased $217 thousand. These increases were offset by the repurchase of 237,669 shares of the Company's common stock at a cost of $1.4 million.

Results of Operations for the Years Ended December 31, 2007 and 2006

Earnings

The Company earned net income of $2.9 million, or $0.40, per basic share for 2007 as compared with net income of $2.1 million, or $0.28 per basic share, in 2006.

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

Net Interest Income

As with most financial institutions, the primary component of earnings for our banks, is net interest income. Net interest income is the difference between interest income, principally from loan and investment securities portfolios, and interest expense, principally on customer deposits and borrowings. Changes in net interest income result from changes in volume, spread and margin. For this purpose, volume refers to the average dollar level of interest-earning assets and interest-bearing liabilities, spread refers to the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities, and margin refers to net interest income divided by average interest-earning assets. Margin is influenced by the level and relative mix of interest-earning assets and interest-bearing liabilities, as well as by levels of noninterest bearing liabilities and capital.

Net interest income increased $1.4 million to $15.0 million for 2007 compared to the $13.6 million earned in 2006. During 2007 with the interest rates stabilizing the increase in net interest income resulted from growth in the loan and investment portfolio. The average yield on our interest-earning assets increased 24 basis points to 7.49%, while the average rate we paid for our interest-bearing liabilities increased 11 basis points. These increases resulted in an increase of 13 basis points in our interest rate spread, from 3.57% in 2006 to 3.70% in 2007. Our net interest margin for 2007 was 4.22%, compared to 4.10% in 2006. Financial Table 1 on page 52 presents a detailed analysis of the components of the Company's net interest income while Financial Table 2 on page 53 summarizes the effects on net interest income from changes in interest rates and in the dollar volume of the components of interest-earning assets and interest bearing liabilities.

Provision for Loan Losses

The provision for loan losses was $15 thousand and $298 thousand for the twelve months ended December 31, 2007 and 2006 respectively. There were net loan recoveries of $324 thousand for the twelve months ended December 31, 2007 as compared with net loan charge-offs of $1.6 million during the same period of 2006. Refer to the Asset Quality discussion beginning on page 46 for further information.

Noninterest Income

The Company generates most of its revenue from net interest income; however, diversification of our earnings base is of major importance to our long term success. Noninterest income increased 20.5%, from $5.5 million in 2006 to $6.6 million in 2007, an increase of $1.1 million. Income generated from brokerage commissions and asset management fees increased $554 thousand to $1.9 million, while other banking fees increased $214 thousand or 21.8% during 2007. Service charges on deposit accounts grew $188 thousand to $2.2 million. The Company also benefited from an increase in income from mortgage loan sales of $193 thousand resulting from an increase in mortgage loan originations. During 2007, the Company sold investment securities realizing a loss of $76 thousand, while other income increased $108 thousand.

Noninterest Expense

Noninterest expense increased $1.4 million to $17.4 million in 2007 compared to $15.9 million in 2006. Salaries and employee benefits, the largest component of noninterest expense, increased $1.0 million, from $9.1 million in 2006 to $10.1 million in 2007. Additions at the executive and bank support staff levels together with normal salary increases, primarily account for this increase. Other noninterest expense increased $475 thousand for the year, including electronic banking expense, a major component of this category, which increased by $102 thousand. Increased usage of electronic banking products is the reason for the increase. Professional fees and services, another component of this category, also increased $102 thousand. This increase was primarily due to compliance with Sarbanes Oxley. At the end of 2006, the remaining costs associated with a core system conversion were amortized off, resulting in a decrease in data processing costs of $197 thousand. In relation to the aforementioned discussion on the subordinated debt, the Company expensed $126 thousand in remaining unamortized issue costs during third quarter contributing to the increase in other noninterest expense.

Income Tax Expense

The Company had income tax expense of $1.3 million for 2007 at an effective tax rate of 30.3% compared to income tax expense of $833 thousand in 2006 at an effective tax rate of 28.7%. Income taxes computed at the statutory rate are reduced primarily by the eligible amount of interest earned on state and municipal securities and income earned on bank owned life insurance. The growth in taxable income out paced the growth in nontaxable income resulting in the increase in the effective tax rate.

Results of Operations for the Years Ended December 31, 2006 and 2005

Earnings

The Company earned net income of $2.1 million, or $0.28 per basic share for 2006 as compared with net income of $1.5 million, or $0.20 per basic share, in 2005.

Net Interest Income

As with most financial institutions, the primary component of earnings for our banks, is net interest income. Net interest income is the difference between interest income, principally from loan and investment securities portfolios, and interest expense, principally on customer deposits and borrowings. Changes in net interest income result from changes in volume, spread and margin. For this purpose, volume refers to the average dollar level of interest-earning assets and interest-bearing liabilities, spread refers to the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities, and margin refers to net interest income divided by average interest-earning assets. Margin is influenced by the level and relative mix of interest-earning assets and interest-bearing liabilities, as well as by levels of noninterest bearing liabilities and capital.

Net interest income increased $1.1 million to $13.6 million for 2006 compared to the $12.5 million earned in 2005. During 2006 with the interest rates stabilizing the increase in net interest income resulted from growth in the loan and investment portfolio. The average yield on our interest-earning assets increased 87 basis points to 7.25%, while the average rate we paid for our interest-bearing liabilities increased 114 basis points. These increases resulted in a decrease of 27 basis points in our interest rate spread, from 3.84% in 2005 to 3.57% in 2006. Our net interest margin for 2006 was 4.10%, compared to 4.21% in 2005. Financial Table 1 on page 52 presents a detailed analysis of the components of the Company's net interest income while Financial Table 2 on page 53 summarizes the effects on net interest income from changes in interest rates and in the dollar volume of the components of interest-earning assets and interest bearing liabilities.

Provision and Allowance for Loan Losses

The provision for loan losses was $298 thousand and $755 thousand for the twelve months ended December 31, 2006 and 2005 respectively. There were net loan charge-offs of $1.6 million for the twelve months ended December 31, 2006 as compared with net loan charge-offs of $1.3 million during the same period of 2005. Refer to the Asset Quality discussion beginning on page 46 for further information.

Noninterest Income

The Company generates most of its revenue from net interest income; however, diversification of our earnings base is of major importance to our long term success. Noninterest income increased 25.7%, from $4.4 million in 2005 to $5.5 million in 2006, an increase of $1.1 million. Income generated from brokerage commissions and asset management fees increased $424 thousand to $1.3 million, while other banking fees increased $177 thousand or 21.9% during 2006. Service charges on deposit accounts grew $293 thousand to $2.0 million. During 2005, the Company implemented a new non-sufficient funds program. This new program along with the growth in demand deposit accounts resulted in a $348 thousand increase in NSF fees. The Company also benefited from an increase in income from mortgage loan sales of $210 thousand resulting in an increase in mortgage loan originations. During 2006, the Company sold investment securities realizing a gain of $60 thousand. These increases were offset by a decline in other income of $62 thousand.

Noninterest Expense

Noninterest expense increased $1.8 million to $15.9 million in 2006 compared to $14.1 million in 2005. Salaries and employee benefits, the largest component of noninterest expense, increased $1.1 million, from $8.0 million in 2005 to $9.1 million in 2006. Additions at the executive and bank support staff levels together with normal salary increases, primarily account for this increase. Data processing costs increased 11.4% or $96 thousand in 2006 with growth in loans and deposits. Other noninterest expense increased $560 thousand for the year, including electronic banking expense, a major component of this category, which increased by $276 thousand. Increased usage of electronic banking products is the reason for the increase. Marketing and donations another component of this category increased $235 thousand.

Income Tax Expense

The Company had income tax expense of $833 thousand for 2006 at an effective tax rate of 28.7% compared to income tax expense of $523 thousand in 2005 at an effective tax rate of 25.6%. Income taxes computed at the statutory rate are reduced primarily by the eligible amount of interest earned on state and municipal securities and income earned on bank owned life insurance. The growth in taxable income out paced the growth in nontaxable income resulting in the increase in the effective tax rate.

Asset Quality

The Company's allowance for loan losses is established through charges to earnings in the form of a provision for loan losses. The allowance is increased by provisions charged to operations and by recoveries of amounts previously charged off, and reduced by loans charged off. Management evaluates the adequacy of the allowance at least quarterly. In evaluating the adequacy of the allowance, management considers the growth, composition and industry diversification of the portfolio, historical loan loss experience, current delinquency levels, adverse situations that may affect a borrower's ability to repay, estimated value of any underlying collateral, prevailing economic conditions and other relevant factors. The Company's credit administration function, through a review process, validates the accuracy of the initial risk grade assessment. In addition, as a given loan's credit quality improves or deteriorates, the credit administration department has the responsibility to change the borrower's risk grade accordingly. For loans determined to be impaired, the allowance is based either on discounted cash flows using the loan's initial effective interest rate or on the fair value of the collateral for certain collateral dependent loans. This evaluation is inherently subjective, as it requires material estimates, including the amounts and timing of future cash flows expected to be received on impaired loans, which may be susceptible to significant change. In addition, regulatory agencies, as an integral part of their examination process, periodically review the allowance for loan losses and may require additions for estimated losses based upon judgments different from those of management.

Management uses the risk-grading program to facilitate the evaluation of probable inherent loan losses and the adequacy of the allowance for loan losses. In this program, risk grades are initially assigned by loan officers and reviewed and monitored by credit administration. The Company strives to maintain its loan portfolio in accordance with conservative loan underwriting policies that result in loans specifically tailored to the needs of its market area. Every effort is made to identify and minimize the credit risks associated with such lending strategies. The Company has no foreign loans and does not engage in significant lease financing or highly leveraged transactions. The Company follows a loan review program designed to evaluate the credit risk in the loan portfolio. This process includes the maintenance of an internally classified watch list that helps management assess the overall quality of the loan portfolio and the adequacy of the allowance for loan losses. In establishing the appropriate classification for specific assets, management considers, among other factors, the estimated value of the underlying collateral, the borrower's ability to repay, the borrower's payment history and the current delinquent status. As a result of this process, certain loans are categorized as substandard, doubtful or loss, and reserves are allocated based on management's judgment and historical experience.

The allowance for loan losses represents management's estimate of an amount adequate to provide for known and inherent losses in the loan portfolio in the normal course of business. While management believes that it uses the best information available to establish the allowance for loan losses, future adjustments to the allowance may be necessary and results of operations could be adversely affected if circumstances differ substantially from the assumptions used in making the determinations. Furthermore, while management believes it has established the allowance for loan losses in conformity with generally accepted accounting principles, there can be no assurance that regulators, in reviewing the Company's portfolio, will not require an adjustment to the allowance for loan losses. In addition, because future events affecting borrowers and collateral cannot be predicted with certainty, there can be no assurance that the existing allowance for loan losses is adequate or that increases will not be necessary should the quality of any loans deteriorate as a result of the factors discussed herein. Any material increase in the allowance for loan losses may adversely affect the Company's financial condition and results of operations.

The provision for loan losses declined from $298 thousand in 2006 to $15 thousand in 2007, a decrease of $283 thousand. This decline in the level of our provision in 2007 resulted primarily from recoveries totaling approximately $317 thousand on two loans charged off in prior years. Impaired loans, which include all loans in nonaccrual status and other loans deemed by management to be impaired, were $7.5 million at December 31, 2007 compared to $6.8 million at December 31, 2006 resulting in an increase of $701 thousand. Total nonaccrual, which are a

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component, increased from $1.2 million at December 31, 2006 to $1.8 million at December 31, 2007. The level of specific reserves identified for impaired loans decreased by $370 thousand. The decline in the level of specific reserves for impaired loans resulted from the Company's continued efforts in improving its collateral positions. The Company had net loan recoveries in 2007 of $324 thousand compared to net loan charge-offs of $1.6 million in 2006. Three loans which were impaired as of December 31, 2005 accounted for $1.4 million of the total $1.6 million in net charge-offs in 2006.

The allowance expressed as a percentage of gross loans held for investment decreased 1 basis point from 1.10% at December 31, 2006 to 1.09% at December 31, 2007. The allowance, as a percentage of total impaired loans, decreased from 51.2% at December 31, 2006 to 35.7% at December 31, 2007. Likewise, the portion of the allowance specifically allocable to impaired loans decreased from 24.0% at December 31, 2006 to 16.8% at December 31, 2007. Nonperforming loans, which consist solely of nonaccrual loans, were $1.8 million at December 31, 2007 as compared to $1.2 million at December 31, 2006. Nonperforming loans to total loans increased from 0.42% at December 31, 2006, to 0.56% at the end of 2007. The total allowance relative to non-performing loans decreased from 261.8% at the end of 2006 to 195.6% at this year end. Management believes the current level of allowance for loan losses to be adequate at this time.

The following nonperforming loan table shows the comparison for the past five years:

Nonperforming Assets
(dollars in thousands)

	At December 31,				
	2007	2006	2005	2004	2003
Nonperforming Assets:					
Nonaccrual loans	$ 1,795	$ 1,211	$ 1,875	$ 3,376	$ 1,577
Other real estate owned	163	203	169	481	108
Total nonperforming assets	$ 1,958	$ 1,414	$ 2,044	$ 3,857	$ 1,685
Accruing loans past due 90 days or more	$ —	$ 500	$ 339	$ 1,150	$ 607
Allowance for loan losses	3,510	3,171	4,482	4,983	3,224
Nonperforming loans to total loans	0.56%	0.42%	0.69%	1.30%	0.67%
Allowance for loan losses to total loans	1.09%	1.10%	1.64%	1.92%	1.37%
Nonperforming assets to total loans and other real estate	0.61%	0.49%	0.75%	1.47%	0.72%
Nonperforming assets to total assets	0.48%	0.37%	0.58%	1.17%	0.56%
Allowance for loan losses to nonperforming loans	195.57%	261.78%	239.09%	147.59%	204.44%

Capital Resources

The Company continues to maintain good capital ratios that support its asset growth. The capital position is maintained through the retention of earnings and controlled growth. Regulatory agencies divide capital into Tier I (consisting of shareholders' equity less ineligible intangible assets and accumulated other comprehensive income and allowable portions of trust preferred securities) and Tier II (consisting of the allowable portion of the reserve for loan losses and certain long-term debt) and measure capital adequacy by applying both capital levels to a banking company's risk-adjusted assets and off-balance sheet items. In addition to these capital ratios, regulatory agencies have established a Tier I leverage ratio that measures Tier I capital to average assets less ineligible intangible assets.

Regulatory guidelines require a minimum of total capital to risk-adjusted assets ratio of 8% with one-half consisting of tangible common shareholders' equity and a minimum Tier I leverage ratio of 4%. Banks which meet or exceed a Tier I ratio of 6%, a total capital ratio of 10% and a Tier I leverage ratio of 5% are considered well capitalized by regulatory standards. At December 31, 2007, the Company and its subsidiary banks were all well capitalized.

The Company expects to continue to exceed these minimums without altering current operations or strategy. The Company does however plan to do a private placement of subordinated debt during the first half of 2008 that will qualify as regulatory capital. Note 14 to the Consolidated Financial Statements presents additional information regarding the Company's and its subsidiary banks' capital ratios.

Dividends

The Board of Directors of Uwharrie Capital Corp declared a 3% stock dividend in 2007, 2006, and in 2005. All references in this Annual Report to net income per share and weighted average common and common equivalent shares outstanding reflect the effects of these stock dividends.

Liquidity

Liquidity, the ability to raise cash when needed without adversely impacting profits, is managed primarily by the selection of asset mix and the maturity mix of liabilities. Maturities and the marketability of securities and other funding sources provide a source of liquidity to meet deposit fluctuations. Maturities in the securities portfolio, presented in Financial Table 4 on page 55, are supported by cash flows from mortgage-backed securities that have longer-term contractual maturities.

Other funding sources at year-end 2007 included $14.3 million in federal funds lines of credit from correspondent banks and approximately $35.8 million of remaining credit availability from the Federal Home Loan Bank. The Company may also borrow from the Federal Reserve Bank discount window. Growth in deposits is typically the primary source of funding for loans, supported by long-term credit available from the Federal Home Loan Bank.

At December 31, 2007, borrowings from federal funds lines and securities sold under repurchase agreements amounted to $7.5 million, while other short-term borrowings totaled $24.4 million. Long-term debt at that date consisted of advances of $15.0 million from the Federal Home Loan Bank, a note payable of $6.6 million to another bank, and a mortgage payable of $91 thousand.

Management believes that the Company's current sources of funds provide adequate liquidity for its current cash flow needs.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Management's Discussion And Analysis of Financial Condition And Results of Operations

Contractual Obligations

The following table reflects the contractual obligations of the Company outstanding as of December 31, 2007.

	Payments Due by Period (in thousands)				
	Total	On Demand or less than 1 year	1-3 Years	4-5 Years	After 5 Years
Contractual Obligations					
Short-term debt	$ 31,928	$ 31,928	$ —	$ —	$ —
Long-term debt	21,691	—	20,626	1,018	47
Operating leases	804	121	233	157	293
Property purchase	255	255	—	—	—
Building construction	1,365	1,365	—	—	—
Total contractual cash obligations, excluding deposits	55,788	33,414	20,859	1,175	340
Deposits	324,657	309,258	13,802	1,597	—
Total contractual cash obligations, including deposits	$380,700	$ 342,927	$34,661	$ 2,772	$ 340

Critical Accounting Policy

The Company's most significant critical accounting policy is the determination of its allowance for loan losses. A critical accounting policy is one that is both very important to the portrayal of the Company's financial condition and results, and requires management's most difficult, subjective and/or complex judgments. What makes these judgments difficult, subjective and/or complex is the need to make estimates about the effects of matters that are inherently uncertain. Refer to the discussion within Allowance for Loan Losses and in Note 1 to the consolidated financial statements for a comprehensive discussion regarding this accounting policy.

Off-Balance Sheet Arrangements

The Company has various financial instruments (outstanding commitments) with off-balance sheet risk that are issued in the normal course of business to meet the financing needs of its customers. See Note 12 to the consolidated financial statements for more information regarding these commitments and contingent liabilities.

Interest Rate Sensitivity

The major component of income for the Company is net interest income, the difference between yield earned on assets and interest paid on liabilities. This differential or margin can vary over time as changes in interest rates occur. The volatility of changes in this differential can be measured by the timing (or repricing) difference between maturing assets and liabilities.

To identify interest rate sensitivity, a common measure is a gap analysis, which reflects the difference or gap between rate sensitive assets and liabilities over various time periods. Gap analysis at December 31, 2007 is reflected in Financial Table 3 on page 54. While management reviews this information, it has implemented the use of a simulation model which calculates expected net interest income based on projected interest-earning assets, interest-bearing liabilities and interest rates and provides a more relevant view of interest rate risk than traditional gap tables. The simulation allows comparison of flat, rising and falling rate scenarios to determine sensitivity of earnings to changes in interest rates.

The Company models immediate rising and declining rate shocks of 2% on its subsidiary banks as preferred by regulators. The most recent consolidated 2% rate shock projections from the asset liability model, measured over a twelve-month period, indicate a negative impact of 8.08% on net interest income in a rates down scenario and a negative impact of 1.71% on net interest income in a rates up environment. Two of the subsidiary banks are asset sensitive and typically have some negative impact when rates decline, since the majority of interest bearing assets will reprice more quickly than the interest bearing liabilities. The other bank is liability sensitive, with the opposite effect, and the blend provides some balance in the consolidated results.

The principal goals of the Company's asset liability management are the maintenance of adequate liquidity and the management of interest rate risk. Interest rate risk management attempts to balance the effects of interest rate changes on interest-sensitive assets and liabilities to protect net interest income from wide fluctuations that could result from changes in interest rates. The Company's Asset Liability Management Committee monitors market changes in interest rates and assists with pricing loan and deposit products consistent with funding source needs and asset growth projections.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Management's Discussion And Analysis of Financial Condition And Results of Operations

Financial Table 1

Average Balances and Net Interest Income Analysis
(dollars in thousands)

	2007 Average Balance	2007 Interest Income/ Expense	2007 Average Yield/ Rate (1)	2006 Average Balance	2006 Interest Income/ Expense	2006 Average Yield/ Rate (1)	2005 Average Balance	2005 Interest Income Expense	2005 Average Yield Rate (1)
Interest-earning assets									
Taxable securities	$ 30,364	$ 1,711	5.63%	$ 25,741	$ 1,266	4.92%	$ 19,363	$ 881	4.55%
Non-taxable securities (1)	12,847	549	6.95%	11,586	517	7.26%	11,962	533	7.25%
Short-term investments	14,219	733	5.16%	11,274	611	5.42%	8,740	302	3.46%
Taxable loans (2)	304,195	23,724	7.80%	289,194	21,758	7.52%	263,168	17,252	6.56%
Non-taxable loans (1)	3,954	192	7.90%	4,200	201	7.79%	3,996	193	7.86%
Total interest-earning assets	365,579	26,909	7.49%	341,995	24,353	7.25%	307,229	19,161	6.38%
Non-earning assets									
Cash and due from banks	11,253			11,833			11,904		
Premises and equipment, net	8,694			8,419			8,367		
Interest receivable and other	7,662			6,534			6,693		
Total non-earning assets	27,609			26,786			26,964		
Total assets	$393,188			$368,781			$334,193		
Interest-bearing liabilities									
Savings deposits	$ 26,635	$ 526	1.97%	$ 32,304	$ 734	2.27%	$ 37,987	$ 580	1.53%
Interest checking & MMDA	102,643	2,550	2.48%	89,174	2,342	2.63%	72,755	1,002	1.38%
Time deposits	136,217	6,454	4.74%	121,053	5,191	4.29%	99,704	2,891	2.90%
Total deposits	265,495	9,530	3.59%	242,531	8,267	3.41%	210,446	4,473	2.13%
Short-term borrowed funds	27,742	1,128	4.07%	17,928	758	4.23%	12,992	354	2.72%
Long-term debt	20,333	1,218	5.99%	30,582	1,677	5.48%	37,273	1,803	4.84%
Total interest-bearing Liabilities	313,570	11,876	3.79%	291,041	10,702	3.68%	260,711	6,630	2.54%
Noninterest liabilities									
Transaction deposits	46,766			47,210			44,145		
Interest payable and other	2,450			2,231			2,150		
Total liabilities	362,786			340,482			307,006		
Shareholders' equity	30,402			28,299			27,187		
Total liabilities and Shareholders equity	$393,188			$368,781			$334,193		
Interest rate spread			3.70%			3.57%			3.84%
Net interest income and net interest margin		$15,033	4.22%		$13,651	4.10%		$12,531	4.21%

1) Yields related to securities and loans exempt from federal and/or state income taxes are stated on a fully tax-equivalent basis, assuming a 38.55% tax rate.
2) Nonaccrual loans are included in loans, net of unearned income.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Management's Discussion And Analysis of Financial Condition And Results of Operations

Financial Table 2

Volume and Rate Variance Analysis
(dollars in thousands)

	2007 Versus 2006			2006 Versus 2005		
	Volume	Rate	Net Change	Volume	Rate	Net Change
Interest-earning assets						
Taxable securities	$ 244	$ 201	$ 445	$ 302	$ 83	$ 385
Non-taxable securities	55	(23)	32	(17)	1	(16)
Short-term investments	156	(34)	122	112	197	309
Taxable loans	1,149	817	1,966	1,832	2,674	4,506
Non-taxable loans	(12)	3	(9)	10	(2)	8
Total interest-earning assets	1,592	964	2,556	2,239	2,953	5,192
Interest-bearing liabilities						
Savings deposits	(120)	(88)	(208)	(108)	262	154
Transaction and MMDA deposits	344	(136)	208	329	1,011	1,340
Other time deposits	684	579	1,263	767	1,533	2,300
Short-term borrowed funds	407	(37)	370	172	232	404
Long-term debt	(588)	129	(459)	(345)	219	(126)
Total interest-bearing liabilities	727	447	1,174	815	3,257	4,072
Net interest income	$ 865	$ 517	$ 1,382	$1,424	$ (304)	$ 1,120

The above table analyzes the dollar amount of changes in interest income and interest expense for major components of interest-earning assets and interest-bearing liabilities. The table distinguishes between (i) changes attributable to volume (changes in volume multiplied by the prior period's rate), (ii) changes attributable to rate (changes in rate multiplied by the prior period's volume), and (iii) net change (the sum of the previous columns). The change attributable to both rate and volume (changes in rate multiplied by changes in volume) has been allocated equally to the change attributable to volume and the change attributable to rate.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
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Financial Table 3

Interest Rate Sensitivity Analysis
(dollars in thousands)

	1-90 Day Position	3-6 Month Position	6-12 Month Position	1-5 Year Position	> 5 Year Position	Total Position
Interest-earning assets						
Interest-earning deposits with banks	$ 2,432	$ —	$ —	—	$ —	$ 2,432
Investment securities	166	103	7,272	4,042	39,422	51,005
FHLB and other stock	—	—	—	—	2,209	2,209
Loans held for sale	2,916	—	—	—	—	2,916
Loans held for investment	189,858	6,822	13,721	76,133	35,453	321,987
Total interest-earning assets	195,372	6,925	20,993	80,175	77,084	380,549
Interest-bearing liabilities						
Deposits	42,567	60,318	72,353	93,517	9,305	278,060
Short-term borrowed funds	31,928	—	—	—	—	31,928
Long-term debt	—	—	—	21,635	56	21,691
Total interest-bearing liabilities	74,995	60,318	72,353	115,152	9,361	331,679
Interest sensitivity GAP per period	$120,877	$(53,393)	$(51,360)	$ (34,977)	$67,723	$ 48,870
Cumulative interest sensitivity GAP	$120,877	$ 67,484	$ 16,124	$ (18,853)	$48,870	$ 48,870
Ratios						
Cumulative gap as a percentage of total interest-earning assets	31.76%	17.73%	4.24%	(4.95)%	12.84%	12.84%
Cumulative interest-earning assets as a percentage of interest-bearing liabilities	262.26%	150.06%	107.78%	94.15%	114.73%	114.73%

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
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Financial Table 4

Investment Securities Portfolio Analysis
(dollars in thousands)

	December 31, 2007		
	Amortized Cost	Estimated Fair Value	Book Yield(1)
Securities available for sale			
U.S. Treasury			
Due within one year	$ 2,997	$ 2,995	3.11%
U.S. Government agencies			
Due within one year	3,995	4,017	3.94%
Due after one but within five years	2,511	2,551	4.34%
	6,506	6,568	4.09%
Mortgage-backed securities			
Due within one year	2	2	6.50%
Due after five but within ten year	2,617	2,642	5.28%
Due after ten years	25,560	25,648	5.74%
	28,179	28,292	5.70%
State and political			
Due within one year	503	511	8.84%
Due after one but within five years	1,440	1,492	8.58%
Due after five but within ten year	3,647	3,775	7.79%
Due after ten years	6,597	6,856	8.49%
	12,187	12,634	8.31%
Corporate Bond			
Due after ten years	501	500	3.23%
Equity Securities			
Due within one year	8	16	9.61%
Total Securities available for sale			
Due within one year	7,505	7,541	3.94%
Due after one but within five years	3,951	4,043	5.89%
Due after five but within ten year	6,264	6,417	6.74%
Due after ten years	32,658	33,004	6.26%
	$ 50,378	$ 51,005	5.94%

1) Yields on securities and investments exempt from federal and/or state income taxes are stated on a fully tax- equivalent basis, assuming a 38.55% tax rate.

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Management's Discussion And Analysis of Financial Condition And Results of Operations

Financial Table 5

Noninterest Income
(dollars in thousands)

	Year Ended December 31,		
	2007	2006	2005
Service charges on deposit accounts	$2,188	$2,000	$1,707
Other banking fees	1,198	984	807
Asset management fees	1,473	974	497
Brokerage commissions	426	371	424
Other noninterest income	400	348	290
Core noninterest income	5,685	4,677	3,725
Income from mortgage loan sales	957	764	554
Security gains (losses)	(76)	60	(16)
Gains (losses) from sale of OREO	(2)	(23)	12
Other gains (losses) from sale of assets	26	(9)	76
Total noninterest income	$6,590	$5,469	$4,351

Financial Table 6

Other Noninterest Expense
(dollars in thousands)

	Year Ended December 31,		
	2007	2006	2005
Professional fees and services	$ 720	$ 618	$ 456
Marketing and donations	639	669	434
Office supplies and printing	277	280	260
Postage	173	192	167
Telephone and data lines	232	212	200
Electronic banking expense	706	604	328
Software amortization and maintenance	448	372	257
Loan collection cost	140	172	299
Subordinated debt issue costs	130	5	5
Other	1,660	1,396	1,554
Total other noninterest expense	$4,995	$4,520	$3,960

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Management's Discussion And Analysis of Financial Condition And Results of Operations

Financial Table 7

Loan Portfolio Composition
(dollars in thousands)

	At December 31,					
	2007		2006		2005	
	Amount	% of Total Loans	Amount	% of Total Loans	Amount	% of Total Loans
Loan type:						
Commercial	$ 37,724	11.72%	$ 36,406	12.64%	$ 37,299	13.68%
Real estate - construction	46,546	14.46%	27,342	9.49%	21,206	7.78%
Real estate - residential	135,842	42.21%	126,111	43.79%	116,715	42.81%
Real estate - commercial	86,593	26.90%	84,744	29.43%	83,861	30.76%
Consumer	15,022	4.67%	13,262	4.60%	13,479	4.94%
Other	143	0.04%	133	0.05%	72	0.03%
Total loans	321,870	100.00%	287,998	100.00%	272,632	100.00%
Less:						
Allowance for loan losses	(3,510)		(3,171)		(4,482)	
Unearned net loan fees	117		137		210	
Net loans	$318,477		$284,964		$268,360	

	At December 31,			
	2004		2003	
	Amount	% of Total Loans	Amount	% of Total Loans
Loan type:				
Commercial	$37,718	14.47%	$ 38,517	16.38%
Real estate - construction	25,480	9.77%	21,813	9.28%
Real estate - residential	102,627	39.38%	76,933	32.72%
Real estate - commercial	81,283	31.18%	84,920	36.12%
Consumer	13,488	5.17%	12,741	5.42%
Other	90	0.03%	187	0.08%
Total loans	$260,686	100.00%	235,111	100.00%
Less:				
Allowance for loan losses	(4,983)		(3,224)	
Unearned net loan fees	149		40	
Net loans	$255,852		$231,927	

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Management's Discussion And Analysis of Financial Condition And Results of Operations

Financial Table 8

Selected Loan Maturities
(dollars in thousands)

	December 31, 2007			
	One Year or Less	One to Five Years	Over Five Years	Total
Commercial and agricultural	$ 17,202	$ 15,365	$ 5,157	$ 37,724
Real estate – construction	32,034	12,629	1,883	46,546
Total selected loans	$ 49,236	$ 27,994	$ 7,040	$ 84,270
Fixed rate loans	$ 32,396	$ 76,133	$35,453	$143,982
Sensitivity to rate changes:				
Variable interest rates	$178,005	$ —	$ —	$178,005

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Management's Discussion And Analysis of Financial Condition And Results of Operations

Financial Table 9

Activity in the Allowance for Loan Loss
(dollars in thousands)

	At or for the Year Ended December 31,				
	2007	2006	2005	2004	2003
Allowance for loan losses at beginning of year	$3,171	$4,482	$4,983	$3,224	$2,755
Provision for loan losses	15	298	755	2,092	593
Loan charge-offs:					
Commercial	—	1,533	1,124	224	10
Real estate	—	14	—	—	45
Consumer	224	140	254	149	95
Total charge-offs	224	1,687	1,378	373	150
Recoveries of loans previously charged off:					
Commercial	440	34	3	1	—
Real estate	—	—	—	—	1
Consumer	108	44	119	39	25
Total recoveries	548	78	122	40	26
Net charge-offs (recoveries)	(324)	1,609	1,256	333	124
Allowance for loan losses at end of year	$3,510	$3,171	$4,482	$4,983	$3,224
Net (charge-offs) recoveries as a percent of average loans	0.11%	(0.55)%	(0.47)%	(0.13)%	(0.06)%

UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Management's Discussion And Analysis of Financial Condition And Results of Operations

Financial Table 10

Allocation of the Allowance for Loan Losses
(dollars in thousands)

	At December 31,					
	2007		2006		2005	
	Amount	% of Total Loans (1)	Amount	% of Total Loans (1)	Amount	% of Total Loans (1)
Commercial	$ 326	11.72%	$ 356	12.64%	$2,474	13.68%
Real estate - construction	325	14.46%	255	9.49%	101	7.78%
Real estate - residential	922	42.21%	1,235	43.79%	323	42.81%
Real estate - commercial	1,715	26.90%	1,123	29.43%	1,159	30.76%
Consumer loans	222	4.67%	202	4.60%	369	4.94%
Other	—	0.04%	—	0.05%	—	— %
Unallocated	—	— %	—	— %	56	0.03%
Total loans	$3,510	100.00%	$3,171	100.00%	$4,482	100.00%

	At December 31,			
	2004		2003	
	Amount	% of Total Loans (1)	Amount	% of Total Loans (1)
Commercial	$ 897	14.47%	$1,204	16.38%
Real estate - construction	185	9.77%	171	9.28%
Real estate - residential	509	39.38%	472	32.72%
Real estate - commercial	2,965	31.18%	877	36.12%
Consumer	359	5.17%	450	5.42%
Other	—	— %	—	— %
Unallocated	68	0.03%	50	0.08%
Total loans	$4,983	100.00%	$3,224	100.00%

(1) Represents total of all outstanding loans in each category as a percent of total loans outstanding.

Financial Table 11

Maturities of Time Deposits of $100,000 or More
(dollars in thousands)

	3 Months or Less	Over 3 Months to 6 Months	Over 6 Months to 12 Months	Over 12 Months	Total
Time Deposits of $100,000 or more	$12,292	$15,806	$ 21,940	$ 4,691	$54,729

Financial Table 12

Securities Performance Ratios

	At December 31,				
	2007	2006	2005	2004	2003
Return on average assets	0.75%	0.56%	0.45%	0.08%	0.57%
Return on average equity	9.73%	7.32%	5.58%	0.91%	5.78%
Equity to average assets ratio	7.73%	7.67%	8.14%	8.64%	9.86%

UWHARRIE CAPITAL CORP
Board of Directors

Joe S. Brooks
Owner and Manager
Brothers Precision Tool Co.

Henry E. Farmer, Sr.
President and Owner
Henry E. Farmer, Inc.

Charles F. Geschickter, III
President and Chief Executive Officer
ST Motorsports, Inc.;
JTG Racing, Inc. and
Wood / JTG Racing, Inc.

Thomas M. Hearne, Jr.
Geopavement Engineer
NC Department of Transportation

Charles D. Horne
President
Hornwood, Inc.

Joseph R. Kluttz, Jr.
President
Albemarle Insurance Agency, Inc.

B. Franklin Lee
Owner and Manager
Franklin Lee Farm

W. Chester Lowder
Director of Livestock Program
Public Policy Division
NC Farm Bureau Federation, Inc.

John P. Murray, MD
Board Vice Chairman
Retired – Physician and Owner
Albemarle Ear, Nose and Throat

James E. Nance
President
Confederate Motors, Inc.

Emmett S. Patterson
Retired – General Manager and Executive Vice President
Pee Dee Electric Membership Corporation

Timothy J. Propst
Executive Vice President
Propst Construction Co., Inc.

Susan J. Rourke
President and Owner
U.S. Land Management Co.

Donald P. Scarborough
President and Owner
Plank Road Realty, Inc.

John W. Shealy, Jr.
President
Capital Concrete Co.

Michael E. Snyder, Sr.
Board Chairman
Vice President
EJS and Sons, LLC

Douglas L. Stafford
Principal
Griffin Stafford, LLC

Emily M. Thomas
Vice President - Administration and Finance
CMH Flooring Products, Inc.

Executive Officers

Roger L. Dick
President and Chief Executive Officer
Uwharrie Capital Corp

Brendan P. Duffey
Executive Vice President and Chief Operating Officer
Uwharrie Capital Corp

Patricia K. Horton
Chief Executive Officer
Cabarrus Bank & Trust
Company

W.D. "Bill" Lawhon, Jr.
President and Chief Executive Officer
Bank of Stanly

Christy D. Stoner
President and Chief Executive Officer
The Strategic Alliance Corporation, BOS Agency, Inc.
Chief Executive Officer
Strategic Investment Advisors, Inc.
Executive Vice President Marketing
Uwharrie Capital Corp

Jimmy L. Strayhorn
President and Chief Executive Officer
Anson Bank & Trust Co.

Jeffrey M. Talley
President
Strategic Investment
Advisors, Inc.

Barbara S. Williams
Executive Vice President and
Controller
Uwharrie Capital Corp

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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 March 31, 2008

OR

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

For the transition period from ______ to ______.

COMMISSION FILE NUMBER 000-22062

UWHARRIE CAPITAL CORP
(Exact name of registrant as specified in its charter)

NORTH CAROLINA **(State or Other Jurisdiction of Incorporation or Organization)**	**56-1814206** **(I.R.S. Employer Identification No.)**
132 NORTH FIRST STREET **ALBEMARLE, NORTH CAROLINA** **(Address of Principal Executive Offices)**	**28001** **(Zip Code)**

Registrant's Telephone number, including area code: (704) 983-6181

N/A
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. ☒ Yes ☐ No

Indicate by check mark 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.

Large accelerated filer ☐ Accelerated filer ☐

Non-accelerated filer ☐ (Do not check if a smaller reporting company) Smaller reporting company ☒

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

Indicate the number of shares outstanding of each of the classes of common stock issuer's as of the latest practicable date: 7,413,278 shares of common stock outstanding as of May 1, 2008.

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Uwharrie Capital Corp and Subsidiaries
Consolidated Balance Sheets

Part I. FINANCIAL INFORMATION
Item 1 - Financial Statements

	March 31, 2008 (Unaudited)	December 31, 2007*
	(dollars in thousands)	
ASSETS		
Cash and due from banks	$ 12,292	$ 13,765
Interest-earning deposits with banks	1,761	2,432
Federal funds sold	1,425	—
Securities available for sale, at fair value	49,552	51,005
Loans held for sale	818	2,916
Loans:		
Loans held for investment	325,397	321,987
Less allowance for loan losses	(3,583)	(3,510)
Net loans held for investment	321,814	318,477
Premises and equipment, net	8,899	8,751
Interest receivable	2,088	2,055
Federal Home Loan Bank stock	2,256	2,137
Bank owned life insurance	5,364	5,318
Goodwill	987	987
Other assets	4,181	4,101
Total assets	$ 411,437	$ 411,944
LIABILITIES		
Deposits:		
Demand noninterest-bearing	$ 45,673	$ 46,597
Interest checking and money market accounts	101,441	102,411
Savings deposits	26,201	26,200
Time deposits, $100,000 and over	56,305	54,729
Other time deposits	97,142	94,720
Total deposits	326,762	324,657
Short-term borrowed funds	25,383	31,928
Long-term debt	24,690	21,691
Interest payable	486	596
Other liabilities	2,185	1,498
Total liabilities	379,506	380,370
Off balance sheet items, commitments and contingencies (Note 5)		
SHAREHOLDERS' EQUITY		
Common stock, $1.25 par value: 20,000,000 shares authorized; shares issued and outstanding 7,405,449 and 7,414,707 shares, respectively	9,257	9,268
Additional paid-in capital	13,418	13,453
Unearned ESOP compensation	(784)	(800)
Undivided profits	9,768	9,266
Accumulated other comprehensive income	272	387
Total shareholders' equity	31,931	31,574
Total liabilities and shareholders' equity	$ 411,437	$ 411,944

(*) Derived from audited consolidated financial statements

See accompanying notes

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Uwharrie Capital Corp and Subsidiaries
Consolidated Statements of Operations (Unaudited)

	Three Months Ended March, 2008	Three Months Ended March, 2007
	(in thousands, except share and per share data)	
Interest Income		
Loans, including fees	$ 5,969	$ 5,654
Investment securities		
US Treasury	24	24
US Government agencies and corporations	487	280
State and political subdivisions	158	163
Other	34	37
Interest-earning deposits with banks and federal funds sold	25	384
Total Interest income	6,697	6,542
Interest Expense		
Interest checking and money market accounts	435	710
Savings deposits	95	146
Time deposits, $100,000 and over	682	606
Other time deposits	1,093	990
Short-term borrowed funds	188	244
Long-term borrowed funds	311	362
Total interest expense	2,804	3,058
Net interest income	3,893	3,484
Provision for loan losses	86	—
Net interest income after provision for loan losses	3,807	3,484
Noninterest Income		
Service charges on deposit accounts	530	503
Other service fees and commissions	748	698
Income from mortgage loan sales	441	255
Other income	146	86
Total noninterest income	1,865	1,542
Noninterest Expense		
Salaries and employee benefits	2,637	2,445
Net occupancy expense	223	217
Equipment expense	140	159
Data processing costs	188	178
Other noninterest expense	1,335	1,084
Total noninterest expenses	4,523	4,083
Income before income taxes	1,149	943
Income taxes	374	285
Net income	$ 775	$ 658
Net income per common share		
Basic	$ 0.11	$ 0.09
Diluted	$ 0.11	$ 0.09
Weighted average shares outstanding		
Basic	7,272,006	7,469,051
Diluted	7,328,525	7,561,498

See accompanying notes

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Uwharrie Capital Corp and Subsidiaries
Consolidated Statement of Changes in Shareholders' Equity

	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Unearned ESOP Compensation	Undivided Profits	Accumulated Other Comprehensive Income	Total
		(in thousands, except share data)					
Balance, December 31, 2007	7,414,707	$9,268	$ 13,453	$ (800)	$ 9,266	$ 387	$31,574
Net income	—	—	—	—	775	—	775
Other comprehensive loss	—	—	—	—	—	(115)	(115)
Release of ESOP shares	—	—	7	16	—	—	23
Common stock issued pursuant to:							
Stock options exercised	13,048	16	40	—	—	—	56
Tax benefit of stock options exercised	—	—	6	—	—	—	6
Repurchase of common stock	(22,306)	(27)	(94)	—	—	—	(121)
Stock compensation expense	—	—	6	—	—	—	6
Adjustment to initially apply EITF 06-4	—	—	—	—	(273)	—	(273)
Balance, March 31, 2008	7,405,449	$9,257	$ 13,418	$ (784)	$ 9,768	$ 272	$31,931

See accompanying notes

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Uwharrie Capital Corp and Subsidiaries
Consolidated Statements of Cash Flows (Unaudited)

	Three Months Ended March 31, 2008	2007
	(dollars in thousands)	
Cash flows from operating activities		
Net income	$ 775	$ 658
Adjustments to reconcile net income to net cash		
Provided by operating activities:		
Depreciation	153	151
Net amortization of security premiums/discounts	(57)	(39)
Net amortization of mortgage servicing rights	124	99
Provision for loan losses	86	—
Stock based compensation	6	11
Income from mortgage loan sales	(441)	(255)
Proceeds from sales of loans held for sale	23,030	10,122
Origination of loans held for sale	(20,721)	(8,453)
Loss on sale of premises, equipment and other assets	5	—
Increase in cash surrender value of life insurance	(46)	(43)
Release of ESOP shares	23	24
Net change in interest receivable	(33)	(61)
Net change in other assets	258	(37)
Net change in interest payable	(110)	71
Net change in other liabilities	414	245
Net cash provided by operating activities	3,466	2,493
Cash flows from investing activities		
Proceeds from sales, maturities and calls of securities available for sale	2,397	1,006
Purchase of securities available for sale	(1,073)	(2,325)
Net increase in loans	(3,584)	(8,880)
Purchase of premises and equipment	(306)	(192)
Proceeds from sales of foreclosed real estate	—	39
Net change in Federal Home Loan Bank stock	(119)	8
Net cash used by investing activities	(2,685)	(10,344)
Cash flows from financing activities		
Net increase in deposit accounts	2,105	5,385
Net increase (decrease) in short-term borrowed funds	(6,545)	7,307
Net increase (decrease) in long-term debt	2,999	(3,838)
Repurchase of common stock	(121)	(566)
Net proceeds from issuance of common stock	56	36
Tax benefit of stock options exercised	6	—
Net cash provided by (used in) financing activities	(1,500)	8,324
Increase (decrease) in cash and cash equivalents	(719)	473
Cash and cash equivalents, beginning of period	16,197	34,760
Cash and cash equivalents, end of period	$ 15,478	$ 35,233

See accompanying notes

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UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements (Unaudited)

Note 1 - Basis of Presentation

The financial statements and accompanying notes are presented on a consolidated basis including Uwharrie Capital Corp (the "Company") and its subsidiaries, Bank of Stanly ("Stanly"), Anson Bank & Trust Co. ("Anson"), Cabarrus Bank & Trust Company ("Cabarrus"), Strategic Investment Advisors, Inc., ("SIA"), and Uwharrie Mortgage Inc. Stanly consolidates its subsidiaries, the Strategic Alliance Corporation, BOS Agency, Inc. and Gateway Mortgage, Inc., each of which is wholly-owned by Stanly.

The information contained in the consolidated financial statements is unaudited. In the opinion of management, the consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America and material adjustments necessary for a fair presentation of results of interim periods, all of which are of a normal recurring nature, have been made. The results of operations for the interim periods are not necessarily indicative of the results that may be expected for an entire year. Management is not aware of economic events, outside influences or changes in concentrations of business that would require additional clarification or disclosure in the consolidated financial statements. Certain prior period amounts have been reclassified to conform to current period classifications. These reclassifications had no effect on net income or shareholders' equity as previously reported.

The organization and business of the Company, accounting policies followed by the Company and other information are contained in the notes to consolidated financial statements filed as part of the Company's 2007 Annual Report on Form 10-K. This Quarterly report should be read in conjunction with such Annual Report.

Note 2 – Comprehensive Income

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available for sale securities, are reported as a separate component of the equity section of the balance sheet, such items, along with net income, are components of comprehensive income.

	Three Months Ended March 31, 2008	2007
	(in thousands)	
Net income	$ 775	$ 658
Other comprehensive income (loss)		
Unrealized gains (losses) on available for sale securities	(187)	73
Related tax effect	72	(28)
Total other comprehensive income (loss)	(115)	45
Comprehensive income	$ 660	$ 703

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Note 3 – Per Share Data

On October 30, 2007, the Company's Board of Directors declared a 3% stock dividend payable on December 7, 2007 to shareholders of record on November 13, 2007. All information presented in the accompanying interim consolidated financial statements regarding earnings per share and weighted average number of shares outstanding has been computed giving effect to this stock dividend.

Basic and diluted net income per common share is computed based on the weighted average number of shares outstanding during each period after retroactively adjusting for stock dividends. Diluted net income per common share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the net income of the Company.

Basic and diluted net income per common share have been computed based upon net income as presented in the accompanying consolidated statements of operations divided by the weighted average number of common shares outstanding or assumed to be outstanding. The computation of basic and dilutive earnings per share is summarized below:

	Three Months Ended March 31, 2008	2007
Weighted average number of common shares used in computing basic net income per common share	7,410,270	7,623,099
Effect of ESOP shares	(138,264)	(154,048)
Adjusted weighted average number of common shares used in computing basic net income per common share	7,272,006	7,469,051
Effect of dilutive stock options	56,519	92,447
Weighted average number of common shares and dilutive potential common shares used in computing diluted net income per common share	7,328,525	7,561,498

Note 4 – Loans

	March 31, 2008	December 31, 2007
	(in thousands)	
Loans outstanding at period end:		
Commercial	$ 40,234	$ 37,724
Real estate-construction	49,493	46,546
Real estate-residential	133,498	135,959
Real estate-commercial	86,458	86,593
Consumer loans	15,569	15,022
All other loans	145	143
Total	$325,397	$ 321,987

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	Three Months Ended March 31, 2008	2007
	(in thousands)	
Analysis of the allowance for loan losses:		
Balance at beginning of period	$ 3,510	$ 3,171
Provision charged to operations	86	—
Charge-offs	(30)	(147)
Recoveries	17	10
Net charge-offs	(13)	(137)
Balance at end of period	$ 3,583	$ 3,034

Note 5 - Commitments and Contingencies

The subsidiary banks are party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of their customers. These financial instruments include commitments to extend credit, lines of credit and standby letters of credit. These instruments involve elements of credit risk in excess of amounts recognized in the accompanying financial statements.

The banks' risk of loss with the unfunded loans and lines of credit or standby letters of credit is represented by the contractual amount of these instruments. The banks use the same credit policies in making commitments under such instruments as they do for on-balance sheet instruments. The amount of collateral obtained, if any, is based on management's credit evaluation of the borrower. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Credit card commitments are unsecured. At March 31, 2008, outstanding financial instruments whose contract amounts represent credit risk were approximately:

(in thousands)	
Commitments to extend credit	$ 91,443
Credit card commitments	9,469
Standby letters of credit	877
Total commitments	$101,789

Note 6 – Fair Value Disclosures

The Company adopted the provisions of Statement of Financial Accounting Statements (SFAS) No. 157 *Fair Value Measurements* (SFAS 157) and SFAS No. 159, *The Fair Value Option for Financial Assets and Liabilities* (SFAS 159) on January 1, 2008.

SFAS 157 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. SFAS 157 does not require any new fair value measurements, but clarifies and standardizes some divergent practices that have emerged since prior guidance was issued. SFAS 157 creates a three-level hierarchy under which individual fair value estimates are to be ranked based on the relative reliability of the inputs used in the valuation.

SFAS 157 defines fair value as the price that would be received to sell an asset or transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities, the Company considers the principal or most advantageous market in which those assets or liabilities are sold and

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considers assumptions that market participants would use when pricing those assets or liabilities. Fair values determined using level 1 inputs rely on active and observable markets to price identical assets or liabilities. In situations where identical assets and liabilities are not traded in active markets, fair values may be determined based on level 2 inputs, which exist when observable data exists for similar assets and liabilities. Fair values for assets and liabilities for which identical or similar assets and liabilities are not actively traded in observable markets are based on level 3 inputs, which are considered to be unobservable.

Among the Company's assets and liabilities, investment securities available for sale are reported at their fair values on a recurring basis. Certain other assets are adjusted to their fair value on a nonrecurring basis, including loans held for sale, which are carried at the lower of cost or market, loan servicing rights, where fair value is determined using similar assets with similar characteristics, when available, or based upon discounted cash flows using market-based assumptions, foreclosed real estate, which is carried at lower of cost or fair market value and goodwill, which is periodically tested for impairment. Deposits, short-term borrowings and long-term obligations are not reported at fair value.

The Company does not record loans at fair value on a recurring basis. However, from time to time, a loan is considered impaired and an allowance for loan losses is established. Loans for which it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement are considered impaired. Once a loan is identified as individually impaired, management measures impairment in accordance with SFAS 114, *Accounting by Creditors for Impairment of a Loan,* (SFAS 114). The fair value of impaired loans is estimated using one of several methods, including collateral value, market value of similar debt, enterprise value, liquidation value and discounted cash flows. Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceed the recorded investments in such loans. At March 31, 2008, substantially all of the total impaired loans were evaluated based on the fair value of the collateral. In accordance with SFAS 157, impaired loans where an allowance is established based on the fair value of collateral require classification in the fair value hierarchy. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company records the impaired loan as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company records the impaired loan as nonrecurring Level 3.

For assets and liabilities carried at fair value, the following table provides fair value information as of March 31, 2008:

	Total	Level 1	Level 2	Level 3
		(dollars in thousands)		
Investment securities available for sale	$49,552	$9,666	$39,886	$ —
Total assets at fair value	$49,552	$9,666	$39,886	$ —
Total liabilities at fair value	$ —	$ —	$ —	$ —

Prices for US Treasury and government agency securities are readily available in the active markets in which those securities are traded, and the resulting fair values are shown in the 'Level 1 input' column. Prices for mortgage-backed securities and for state, county and municipal securities are obtained for similar securities, and the resulting fair values are shown in the 'Level 2 input' column. Prices for all other non-marketable investments are determined based on various assumptions that are not observable. The fair values for these investment

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securities are shown in the 'Level 3 input' column. Non-marketable investment securities, which are carried at their purchase price, include those that may only be redeemed by the issuer.

The Company may be required, from time to time, to measure certain assets at fair value on a nonrecurring basis in accordance with U.S. generally accepted accounting principles. These include assets that are measured at the lower of cost or market that were recognized at fair value below cost at the end of the period. Assets measured at fair value on a nonrecurring basis are included in the table below as of March 31, 2008:

	Total	Level 1	Level 2	Level 3
	(dollars in thousands)			
Loans	$8,591	$ —	$8,591	$ —
Total assets at fair value	$8,591	$ —	$8,591	$ —
Total liabilities at fair value	$ —	$ —	$ —	$ —

SFAS 159 allows an entity to elect to measure certain financial assets and liabilities at fair value with changes in fair value recognized in the income statement each period. The statement also requires additional disclosures to identify the effects of an entity's fair value election on its earnings. Upon the adoption of SFAS 159, the Company did not elect to report any assets and liabilities at fair value.

Note 7 – Recent Accounting Pronouncements

SAB 109

Staff Accounting Bulletin No. 109 ("SAB 109"**),** "Written Loan Commitments Recorded at Fair Value Through Earnings," supersedes Staff Accounting Bulletin No. 105 by requiring the expected net future cash flows related to servicing a loan to be included in the measurement of all written loan commitments that are accounted for at fair value through earnings. The adoption of SAB 109 on January 1, 2008, did not have a significant impact on the Company's consolidated financial statements.

SFAS 157

Statement of Financial Accounting Standards No. 157 ("SFAS 157"), *Fair Value Measurements*, defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. The Company adopted the provisions of SFAS 157 on January 1, 2008 as discussed in Note 6 above.

SFAS 159

Statement of Financial Accounting Standards No. 159 ("SFAS 159"), *The Fair Value Option for Financial Assets and Financial Liabilities*, permits entities to choose to measure many financial instruments and certain other items at fair value. The objective of this standard is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This statement is effective for fiscal years beginning after November 15, 2007, with early adoption permitted under certain circumstances. The adoption of SFAS 159 did not have any impact on the Company's consolidated financial statements. See Note 6 above.

EITF 06-4

The Emerging Issues Task Force (EITF) reached a consensus at its September 2006 meeting regarding EITF 06-4, *Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements*. The scope of EITF 06-4 is

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limited to the recognition of a liability and related compensation costs for endorsement split-dollar life insurance policies that provide a benefit to an employee that extends to postretirement periods. Therefore, this EITF would not apply to a split-dollar life insurance arrangement that provides a specified benefit to an employee that is limited to the employee's active service period with an employer. This EITF 06-4 is effective for fiscal years beginning after December 15, 2007, with earlier application permitted. The Company adopted EITF 06-4 on January 1, 2008 and it had the effect of reducing beginning consolidated undivided profits by approximately $273,000.

From time to time, the FASB issues exposure drafts of proposed statements of financial accounting standards. Such exposure drafts are subject to comment from the public, to revisions by the FASB and to final issuance by the FASB as statements of financial accounting standards. Management considers the effect of the proposed statements on the consolidated financial statements of the Company and monitors the status of changes to and proposed effective dates of exposure drafts.

Reclassification

Certain amounts in the 2007 consolidated financial statements have been reclassified to conform to the 2008 presentation. The reclassifications had no effect on net income or shareholders' equity as previously reported.

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

This Quarterly Report on Form 10-Q may contain certain forward-looking statements consisting of estimates with respect to the financial condition, results of operations and business of the Company that are subject to various factors which could cause actual results to differ materially from these estimates. These factors include, but are not limited to, general economic conditions, changes in interest rates, deposit flows, loan demand, real estate values, and competition; changes in accounting principles, policies, or guidelines; changes in legislation or regulation; and other economic, competitive, governmental, regulatory, and technological factors affecting the Company's operations, pricing, products and services.

Comparison of Financial Condition at March 31, 2008 and December 31, 2007.

During the three months ended March 31, 2008, the Company's total assets decreased $507 thousand, from $411.9 million to $411.4 million. During the three months, loans held for investment increased $3.4 million or 1.1%, from $322.0 million at December 31, 2007 to $325.4 million at March 31, 2008. This increase, however, was offset by a decline in investment securities of $1.5 million and a decrease in loans held for sale of $2.1 million during the period.

Cash and cash equivalents decreased $719 thousand during the three months ended March 31, 2008. Cash and due from banks declined $1.5 million, while interest-earning deposits with banks decreased $671 thousand. These decreases were offset by an increase in federal funds sold of $1.4 million. The Company made the decision to continue to keep a portion of their investments in short-term federal funds during the first quarter of 2008.

Investment securities decreased $1.5 million or 2.9% for the three months. The decrease resulted primarily from normal mortgage backed securities pay down activity during the period.

As previously stated, loans held for investment increased $3.4 million to $325.4 million during the period ended March 31, 2008. The Company has experienced positive growth trends in its residential construction, commercial and consumer areas of the loan portfolio. These positive trends were impacted by a decrease in our one to four family residential real estate loan

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portfolio. Loans held for sale decreased 71.9% or $2.1 million during the period. The allowance for loan losses was $3.6 million at March 31, 2008 which represents 1.10% of the loan portfolio.

Other changes in our consolidated assets related to premises and equipment, interest receivable, Federal Home Loan Bank stock, bank owned life insurance and other assets. Fixed assets increased $148 thousand, interest receivable grew $33 thousand, bank owned life insurance increased $46 thousand and other assets increased $80 thousand. Federal Home Loan Bank stock increased $119 thousand. Federal Home Loan Bank stock ownership is a requirement for member banks that utilize Federal Home Loan Bank for borrowing funds. The amount of stock owned by each member bank is based primarily on the amount of borrowings outstanding.

Customer deposits, our primary funding source, experienced a $2.1 million increase during the three months ended March 31, 2008, increasing from $324.7 million to $326.8 million. Time deposits $100,000 and over grew by $1.6 million and other time deposits increased $2.4 million during the period. These increases were offset by declines in interest checking and money market accounts of $970 thousand and demand deposits of $924 thousand.

The growth in deposits allowed the Company to reduce net borrowings by $3.5 million during the first quarter of 2008. Borrowings consist of both short-term and long-term borrowed funds. The Company utilizes both short-term and long-term advances from the Federal Home Loan Bank. At March 31, 2008, $32.0 million of the total borrowings of $50.1 million were comprised of Federal Home Loan Bank advances.

Other liabilities increased from $ 1.5 million at December 31, 2007 to $2.2 million at March 31, 2008, an increase of $687 thousand. The Company has a supplemental retirement plan in place for four executive officers. The Company has purchased life insurance policies in order to provide future funding of benefit payments. As discussed in Note 7, with the adoption of EITF 06-4, *Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements*, the Company recorded a $273 thousand liability. This adjustment coupled with an increase in the reserve for income taxes were the primary factors associated with the increase in other liabilities.

At March 31, 2008, total shareholders’ equity was $31.9 million, an increase of $357 thousand from December 31, 2007. Net income for the period was $775 thousand and the Company received $56 thousand from the exercise of stock options. These increases were offset by the repurchase of 22,306 shares of the Company’s common stock at a cost of $121 thousand and unrealized losses on investment securities, net of tax, of $115 thousand. The Company also recorded a $273 thousand one-time cumulative adjustment to undivided profits for the adoption of EITF 06-4. At March 31, 2008, the Company and its subsidiary banks exceeded all applicable regulatory capital requirements.

Comparison of Results of Operations For the Three Months Ended March 31, 2008 and 2007.

Net Income

Uwharrie Capital Corp reported net income of $775 thousand, or $0.11 per basic share, for the three months ended March 31, 2008, as compared to $658 thousand, or $0.09 per basic share, for the three months ended March 31, 2007, an increase of $117 thousand, or $0.02 per share.

Net Interest Income

As with most financial institutions, the primary component of earnings for our banks, is net interest income. Net interest income is the difference between interest income, principally from

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loan and investment securities portfolios, and interest expense, principally on customer deposits and borrowings. Changes in net interest income result from changes in volume, spread and margin. For this purpose, volume refers to the average dollar level of interest-earning assets and interest-bearing liabilities, spread refers to the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities, and margin refers to net interest income divided by average interest-earning assets. Margin is influenced by the level and relative mix of interest-earning assets and interest-bearing liabilities, as well as by levels of noninterest-bearing liabilities and capital.

Net interest income for the three months ended March 31, 2008 was $3.9 million as compared with $3.5 million during the quarter ending March 31, 2007, resulting in an increase of $409 thousand, or 11.7%. During the quarter ending March 31, 2008 our growth in the volume of interest-earning assets outpaced the growth in interest-bearing liabilities by $296 thousand. The average yield on our interest–earning assets decreased 22 basis points to 7.20%, while the average rate we paid for our interest-bearing liabilities decreased 51 basis points. The Company’s assets that are interest rate sensitive adjust at the time the Federal Reserve adjusts interest rates, while, interest-bearing time deposits adjust at the time of maturity. The fore mentioned decreases resulted in an increase of 29 basis points in our interest rate spread, from 3.52% in 2007 to 3.81% in 2008. Our net interest margin was 4.22% and 4.00% for the comparable periods in 2008 and 2007.

The following table presents average balance sheets and a net interest income analysis for the three months ended March 31, 2008 and 2007:

Average Balance Sheet and Net Interest Income Analysis
For the Three Months Ended March 31,

(in thousands)

	Average Balance		Income/Expenses		Rate/Yield	
	2008	2007	2008	2007	2008	2007
Interest-earning assets:						
Taxable securities	$ 37,864	$ 27,540	$ 548	$ 341	5.81%	4.97%
Nontaxable securities (1)	12,861	12,865	155	163	7.85%	8.38%
Short-term investments	3,022	29,679	25	384	3.32%	5.19%
Taxable loans	322,504	290,650	5,924	5,607	7.37%	7.74%
Non-taxable loans (1)	3,795	3,992	45	47	7.36%	7.85%
Total interest-earning assets	380,046	364,726	6,697	6,542	7.20%	7.42%
Interest-bearing liabilities:						
Interest-bearing deposits	279,931	265,518	2,305	2,452	3.30%	3.70%
Short-term borrowed funds	25,381	22,841	188	244	2.97%	4.28%
Long-term debt	26,509	25,843	311	362	4.71%	5.62%
Total interest bearing liabilities	331,821	314,202	2,804	3,058	3.39%	3.90%
Net interest spread	$ 48,225	$ 50,524	$3,893	$3,484	3.81%	3.52%
Net interest margin (1) (% of earning assets)					4.22%	4.00%

(1) Yields related to securities and loans exempt from income taxes are stated on a fully tax-equivalent basis, assuming a 38.55% tax rate.

Provision and Allowance for Loan Losses

The provision for loan losses was $86 thousand for the three months ending March 31, 2008. There was no provision required for the same period in 2007. There were net loan charge-offs of $13 thousand for the three months ended March 2008 as compared with net loan charge-offs of $137 thousand during the same period of 2007. Refer to the Asset Quality discussion on page 16 for further information.

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Noninterest Income

The Company generates most of its revenue from net interest income; however, like all financial institutions, diversification of our earnings base is of major importance in our long term success. Total noninterest income increased $323 thousand, from $1.5 million for the quarter ended March 31, 2007 to $1.9 million for the same period in 2008. Service charges on deposit accounts produced earnings of $530 thousand for the three months ended March 31, 2008, an increase of $27 thousand, or 5.4%. Other service fees and commissions experienced a 7.2% increase for the comparable three month period. Growth in ATM fees of $35 thousand and investment fees on managed accounts of $58 thousand enhanced this increase. Income from mortgage loan sales increased $186 thousand from $255 thousand for the quarter ended March 31, 2007 to $441 thousand for the same period in 2008. The interest rate reductions during the first quarter attributed to the increase in mortgage loan sales. The Company also owns shares of VISA stock. VISA redeemed a portion of this stock during the first quarter of 2008 resulting in other income of $59 thousand. This income was the primary reason for the increase in other income for the comparable periods.

Noninterest Expense

Noninterest expense for the quarter ended March 31, 2008 was $4.5 million compared to $4.1 million for the same period of 2007, an increase of $440 thousand. Salaries and employee benefits, the largest component of noninterest expense, increased $192 thousand, from $2.4 million for the quarter ending March 31, 2007 to $2.6 million for the same period in 2008. The Company has a non-qualifying deferred compensation plan for certain executive officers. The costs associated with this plan increased $82 thousand for the comparable periods. This increase coupled with normal salary increases contributed to the overall increase in noninterest expense. Other noninterest expense increased $251 thousand for the comparable three month periods. The table below reflects the composition of other noninterest expense.

Other noninterest expense

	Three Months Ended March 31,	
	2008	2007
	(in thousands)	
Professional fees and services	$ 165	$ 158
Marketing and donations	172	125
Office supplies, printing and postage	116	110
Telephone and data lines	60	56
Electronic banking expense	186	162
Software amortization and maintenance	99	104
Loan collection expense	71	25
Shareholder relations expense	58	45
Deposit/other charge-offs	28	6
Other	380	293
Total	$ 1,335	$ 1,084

Income Tax Expense

The Company had income tax expense of $374 thousand for the three months ended March 31, 2008 resulting in an effective tax rate of 32.6% compared to income tax expense of $285 thousand and an effective rate of 30.2% in the 2007 period. Income taxes computed at the statutory rate are reduced primarily by the eligible amount of interest earned on state and municipal securities, tax free municipal loans and income earned on bank owned life insurance. The increase in the effective tax rate resulted primarily from the decrease in the level of such

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tax free income as a percentage income before income taxes in the current year quarter compared to the 2007 quarter.

Asset Quality

The Company's allowance for loan losses is established through charges to earnings in the form of a provision for loan losses. The allowance is increased by provisions charged to operations and by recoveries of amounts previously charged off, and reduced by loans charged off. Management evaluates the adequacy of the allowance at least quarterly. In evaluating the adequacy of the allowance, management considers the growth, composition and industry diversification of the portfolio; historical loan loss experience; current delinquency levels; adverse situations that may affect a borrower's ability to repay; estimated value of any underlying collateral; prevailing economic conditions and other relevant factors. The Company's credit administration function, through a review process, validates the accuracy of the initial risk grade assessment. In addition, as a given loan's credit quality improves or deteriorates, the credit administration department has the responsibility to change the borrower's risk grade accordingly. For loans determined to be impaired, the allowance is based either on discounted cash flows using the loan's initial effective interest rate or on the fair value of the collateral for certain collateral dependent loans. This evaluation is inherently subjective, as it requires material estimates, including the amounts and timing of future cash flows expected to be received on impaired loans, which may be susceptible to significant change. In addition, regulatory agencies, as an integral part of their examination process, periodically review the allowance for loan losses and may require additions for estimated losses based upon judgments different from those of management.

Management uses the risk-grading program to facilitate the evaluation of probable inherent loan losses and the adequacy of the allowance for loan losses. In this program, risk grades are initially assigned by loan officers and reviewed and monitored by credit administration. The Company strives to maintain its loan portfolio in accordance with conservative loan underwriting policies that result in loans specifically tailored to the needs of its market area. Every effort is made to identify and minimize the credit risks associated with such lending strategies. The Company has no foreign loans and does not engage in significant lease financing or highly leveraged transactions. The Company follows a loan review program designed to evaluate the credit risk in the loan portfolio. This process includes the maintenance of an internally classified watch list that helps management assess the overall quality of the loan portfolio and the adequacy of the allowance for loan losses. In establishing the appropriate classification for specific assets, management considers, among other factors, the estimated value of the underlying collateral, the borrower's ability to repay, the borrower's payment history and the current delinquent status. As a result of this process, certain loans are categorized as substandard, doubtful or loss and reserves are allocated based on management's judgment and historical experience.

The allowance for loan losses represents management's estimate of an appropriate amount to provide for known and inherent losses in the loan portfolio in the normal course of business. While management believes that it uses the best information available to establish the allowance for loan losses, future adjustments to the allowance may be necessary and results of operations could be adversely affected if circumstances differ substantially from the assumptions used in making the determinations. Furthermore, while management believes it has established the allowance for loan losses in conformity with generally accepted accounting principles, there can be no assurance that regulators, in reviewing the Company's portfolio, will not require an adjustment to the allowance for loan losses. In addition, because future events affecting borrowers and collateral cannot be predicted with certainty, there can be no assurance that the existing allowance for loan losses is adequate or that increases will not be necessary, should the quality of any loans deteriorate as a result of the factors discussed herein. Any

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material increase in the allowance for loan losses may adversely affect the Company's financial condition and results of operations.

The provision for loan losses was $86 thousand for the three months ended March 31, 2008 as compared to $0 for the same period in 2007 when no provisions were required. Additionally, the allowance expressed as a percentage of loans held for investment was 1.10% at March 31, 2008, an increase from 1.09% at December 31, 2007. During the first three months of 2008 the levels of our impaired loans, which includes all loans in nonaccrual status and other loans deemed by management to be impaired, were $10.4 million compared to $7.5 million at December 31, 2007 an increase of $2.9 million. Of the $10.4 million in impaired loans at March 31, 2008, $8.6 million carried an allowance of $1.4 million while $1.8 million were evaluated and required no specific allowance. The level of specific reserves identified for impaired loans increased by $111 thousand for the same period. These increases were due primarily to the impairment of a loan relationship with one customer of $2.6 million, for which a $50 thousand specific reserve has been provided. Net loan charge-offs for the three months ending March 31, 2007 were $137 thousand, while the same period in 2008 experienced net loan charge-offs of $13 thousand.

The allowance as a percentage of total impaired loans has increased from 35.7% at December 31, 2007 to 38.0% at March 31, 2008. The portion of the allowance specifically allocable to impaired loans decreased from 16.8% at December 31, 2007 to 13.2% at March 31, 2008. Management believes the current level of allowance for loan losses to be adequate at this time.

The following nonperforming loan table shows the comparison for the three months ended March 31, 2008 to December 31, 2007:

Nonperforming Assets
(dollars in thousands)

	March 31, 2008	December 31, 2007
Nonperforming assets:		
Non accrual loans	$ 1,686	$ 1,795
Other real estate owned	321	163
Total nonperforming assets	$ 2,007	$ 1,958
Accruing loans past due 90 days or more	$ 27	$ —
Allowance for loans losses	3,583	3,510
Nonperforming loans to total loans	0.52%	0.56%
Allowance for loan losses to total loans	1.10%	1.09%
Nonperforming assets to total loans and other real estate	0.62%	0.61%
Nonperforming assets to total assets	0.49%	0.48%
Allowance for loan losses to Nonperforming loans	212.57%	195.57%

Liquidity and Capital Resources

The objective of the Company's liquidity management policy is to ensure the availability of sufficient cash flows to meet all financial commitments and to capitalize on any opportunities for expansion. Liquidity management addresses the ability to meet deposit withdrawals on demand

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or at contractual maturity, to repay borrowings as they mature, and to fund new loans and investments as opportunities arise.

The Company's primary sources of internally generated funds are principal and interest payments on loans, cash flows generated from operations and cash flow generated by investments. Growth in deposits is typically the primary source of funds for loan growth. The Company and its subsidiary banks have multiple funding sources in addition to deposits that can be used to increase liquidity and provide additional financial flexibility. These sources are the subsidiary banks' established federal funds lines with correspondent banks aggregating $20.1 million at March 31, 2008, with available credit of $19.6 million, established borrowing relationships with the Federal Home Loan Bank, with available credit of $38.3 million, access to borrowings from the Federal Reserve Bank discount window, and the sale of securities under agreements to repurchase. In addition, the Company issues commercial paper and has secured long-term debt from other sources. Total debt from these sources aggregated $50.1 million at March 31, 2008, compared to $53.6 million at December 31, 2007.

Banks and bank holding companies, as regulated institutions, must meet required levels of capital. The FDIC and the Federal Reserve, the primary federal regulators of the Company and its subsidiary banks, have adopted minimum capital regulations or guidelines that categorize components and the level of risk associated with various types of assets.

Regulatory guidelines require a minimum of total capital to risk-adjusted assets ratio of 8 percent and a Tier I leverage ratio of 4 percent. Banks, which meet or exceed a Tier I ratio of 6 percent, a total capital ratio of 10 percent and a Tier I leverage ratio of 5 percent are considered "well capitalized" by regulatory standards. Financial institutions are expected to maintain a level of capital commensurate with the risk profile assigned to their assets in accordance with those guidelines.

Both the Company and its subsidiary banks have maintained capital levels exceeding minimum levels for "well capitalized" banks and bank holding companies. The Company expects to continue to exceed these minimums without altering current operations or strategy. The Company does however plan to effect a private placement of subordinated debt during the second quarter of 2008 that will qualify as regulatory capital.

Accounting and Regulatory Matters

Management is not aware of any known trends, events, uncertainties or current recommendations by regulatory authorities that will have or that are reasonably likely to have a material effect on the Company's liquidity, capital resources, or other operations.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

The Company's primary market risk is interest rate risk. Interest rate risk is the result of differing maturities or repricing intervals of interest-earning assets and interest-bearing liabilities and the fact that rates on these financial instruments do not change uniformly. These conditions may impact the earnings generated by the Company's interest earning assets or the cost of its interest-bearing liabilities, thus directly impacting the Company's overall earnings. The Company's management actively monitors and manages interest rate risk. One way this is accomplished is through the development of and adherence to the Company's asset/liability policy. This policy sets forth management's strategy for matching the risk characteristics of the Company's interest-earning assets and liabilities so as to mitigate the effect of changes in the rate environment. The Company's market risk profile has not changed significantly since December 31, 2007.

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Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

At the end of the period covered by this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's principal executive officer and principal financial officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Securities Exchange Act Rule 13a-14.

Based upon that evaluation, the principal executive officer and principal financial officer concluded that the Company's disclosure controls and procedures were effective (1) to provide reasonable assurance that information required to be disclosed by the Company in the reports filed or submitted by it under the Securities Exchange Act was recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and (2) to provide reasonable assurance that information required to be disclosed by the Company in such reports is accumulated and communicated to the Company's management, including its principal executive officer and principal financial officer, as appropriate to allow for timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

Management of the Company has evaluated, with the participation of the Company's principal executive officer and principal financial officer, changes in the Company's internal controls over financial reporting (as defined in Rule 13a -15(f) and 15d – 15(f) of the Exchange Act) during the first quarter of 2008. In connection with such evaluation, the Company has determined that there were no changes in the Company's internal control over financial reporting during the period covered by this report that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting. The Company reviews its disclosure controls and procedures, which may include its internal control over financial reporting, on an ongoing basis, and may from time to time make changes aimed at enhancing their effectiveness and to ensure that the Company's systems evolve with its business.

Part II. OTHER INFORMATION

Item 1. Legal Proceedings

Neither the Company nor its subsidiaries, nor any of their properties are subject to any legal proceedings other than ordinary routine litigation incidental to their business.

Item 1A. Risk Factors

Not applicable.

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

The following table sets forth information with respect to shares of common stock repurchased by the Company during the three months ended March 31, 2008.

	(a) Total Number of Shares Purchased	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Program (1)	(d) Maximum Dollar Value of Shares that May Yet Be Purchased Under the Plans (2)
January 1, 2008 Through January 31, 2008	3,935	$ 5.40	—	$ —
February 1, 2008 Through February 28, 2008	1,000	$ 5.50	—	$ —
March 1, 2008 Through March 31, 2008	17,371	$ 5.44	—	$ —
Total	22,306	$ 5.43	—	$ —

(1) Trades of the Company's stock occur in the Over-the-Counter marketplace from time to time. The Company also has in place a Stock Repurchase Plan that provides liquidity to its shareholders in the event a willing buyer is not available to purchase shares that are offered for sale. The Company is under no obligation to purchase shares offered; however, it will accommodate such offers as its Stock Repurchase Plan allows. This plan was initially adopted in 1995 and is approved annually by resolution of the Board of Directors or the Executive Committee of the Board.

(2) On January 9, 2007, the Executive Committee of Uwharrie Capital Corp mandated by resolution that the Company could repurchase 3,935 shares of its common stock at a cost of $21,249.

(3) On January 22, 2008, the Board of Directors of Uwharrie Capital Corp mandated by resolution that the Company could repurchase up to $50,000 of its common stock during first quarter of 2008. This resolution is under a Stock Repurchase Plan that is contingent upon maintaining a well capitalized regulatory capital ratio. The purchase price under the plan is set on a quarterly basis, based on an independent valuation of the Company's stock price, and is approved by the Board. The Board individually approves stock repurchases that exceed $50,000 in any one transaction.

(4) On March 18, 2008, the Board of Directors of Uwharrie Capital Corp mandated by resolution that the Company could repurchase up to an additional $50,000 of its common stock during the first quarter.

Item 3. Defaults Upon Senior Securities

None

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

None

Item 5. Other Information

None

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EXHIBIT INDEX

Exhibit Number	Description of Exhibit
3.1	Registrant's Articles of Incorporation *
3.2	Registrant's By-laws *
4	Form of stock certificate*
10.1	Incentive Stock Option Plan, as amended *
10.2	Employee Stock Ownership Plan and Trust *
10.3	2006 Incentive Stock Option Plan *
10.4	2006 Employee Stock Purchase Plan *
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith)
31.2	Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith)
32	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith)

* Incorporated by reference

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Item 6. Exhibits

Exhibit Number	Description of Exhibit
3.1	Registrant's Articles of Incorporation *
3.2	Registrant's By-laws *
4	Form of stock certificate *
10.1	Incentive Stock Option Plan, as amended *
10.2	Employee Stock Ownership Plan and Trust **
10.3	2006 Incentive Stock Option Plan ***
10.4	2006 Employee Stock Purchase Plan ***
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith)
31.2	Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith)
32	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith)

* Incorporated by reference from exhibits to Registrant's Registration Statement on Form S-4 (Reg. No. 33-58882).
** Incorporated by reference to Registrant's Annual Report on Form 10-KSB for the fiscal year ended 1999.
*** Incorporated by reference to Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2006.

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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 who is thereunto duly authorized.

	UWHARRIE CAPITAL CORP (Registrant)
Date: May 12, 2008	By: /s/ Roger L. Dick Roger L. Dick President and Chief Executive Officer
Date: May 12, 2008	By: /s/ Barbara S. Williams Barbara S. Williams Principal Financial Officer

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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, 2008

OR

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

For the transition period from ______ to ______.

COMMISSION FILE NUMBER 000-22062

UWHARRIE CAPITAL CORP
(Exact name of registrant as specified in its charter)

NORTH CAROLINA **(State or Other Jurisdiction of Incorporation or Organization)**	**56-1814206** **(I.R.S. Employer Identification No.)**
132 NORTH FIRST STREET **ALBEMARLE, NORTH CAROLINA** **(Address of Principal Executive Offices)**	**28001** **(Zip Code)**

Registrant's Telephone number, including area code: (704) 983-6181

N/A
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. ☒ Yes ☐ No

Indicate by check mark 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.

Large accelerated filer ☐	Accelerated filer ☐
Non-accelerated filer ☐ (Do not check if a smaller reporting company)	Smaller reporting company ☒

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

Indicate the number of shares outstanding of each of the classes of common stock issuer's as of the latest practicable date: 7,407,851 shares of common stock outstanding as of August 1, 2008.

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Uwharrie Capital Corp and Subsidiaries
Consolidated Balance Sheets

Part I. FINANCIAL INFORMATION

Item 1 - Financial Statements

	June 30, 2008 (Unaudited)	December 31, 2007*
	(dollars in thousands)	
ASSETS		
Cash and due from banks	$ 13,585	$ 13,765
Interest-earning deposits with banks	1,381	2,432
Securities available for sale, at fair value	48,748	51,005
Loans held for sale	1,919	2,916
Loans:		
Loans held for investment	336,735	321,987
Less allowance for loan losses	(3,657)	(3,510)
Net loans held for investment	333,078	318,477
Premises and equipment, net	9,323	8,751
Interest receivable	1,925	2,055
Federal Home Loan Bank stock	2,369	2,137
Bank owned life insurance	5,411	5,318
Goodwill	987	987
Other real estate owned	590	163
Other assets	4,852	3,938
Total assets	$ 424,168	$ 411,944
LIABILITIES		
Deposits:		
Demand noninterest-bearing	$ 46,362	$ 46,597
Interest checking and money market accounts	110,454	102,411
Savings deposits	26,947	26,200
Time deposits, $100,000 and over	56,723	54,729
Other time deposits	94,616	94,720
Total deposits	335,102	324,657
Short-term borrowed funds	20,251	31,928
Long-term debt	34,195	21,691
Interest payable	538	596
Other liabilities	2,004	1,498
Total liabilities	392,090	380,370
Off balance sheet items, commitments and contingencies (Note 5)		
SHAREHOLDERS' EQUITY		
Common stock, $1.25 par value: 20,000,000 shares authorized; shares issued and outstanding 7,407,851 and 7,414,707 shares respectively	9,259	9,268
Additional paid-in capital	13,398	13,453
Unearned ESOP compensation	(769)	(800)
Undivided profits	10,540	9,266
Accumulated other comprehensive income (loss)	(350)	387
Total shareholders' equity	32,078	31,574
Total liabilities and shareholders' equity	$ 424,168	$ 411,944

(*) Derived from audited consolidated financial statements

See accompanying notes

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Uwharrie Capital Corp and Subsidiaries
Consolidated Statements of Operations (Unaudited)

	Three Months Ended June 30, 2008	Three Months Ended June 30, 2007	Six Months Ended June 30, 2008	Six Months Ended June 30, 2007
‘	(in thousands, except share and per share data)			
Interest Income				
Loans, including fees	$ 5,669	$ 5,865	$ 11,638	$ 11,519
Investment securities				
US Treasury	25	24	49	48
US Government agencies and corporations	468	316	955	596
State and political subdivisions	170	157	328	320
Other	32	37	66	74
Interest-earning deposits with banks and federal funds sold	18	251	43	635
Total interest income	6,382	6,650	13,079	13,192
Interest Expense				
Interest checking and money market accounts	312	666	747	1,376
Savings deposits	74	134	169	280
Time deposits, $100,000 and over	604	566	1,286	1,172
Other time deposits	985	1,009	2,078	1,999
Short-term borrowed funds	146	396	334	640
Long-term debt	308	201	619	563
Total interest expense	2,429	2,972	5,233	6,030
Net interest income	3,953	3,678	7,846	7,162
Provision for loan losses	171	(138)	257	(138)
Net interest income after provision for loan losses	3,782	3,816	7,589	7,300
Noninterest Income				
Service charges on deposit accounts	537	556	1,067	1,059
Other service fees and commissions	754	721	1,502	1,419
Loss on sale of securities	—	(76)	—	(76)
Income from mortgage loan sales	357	188	798	443
Other income	247	103	393	189
Total noninterest income	1,895	1,492	3,760	3,034
Noninterest Expense				
Salaries and employee benefits	2,664	2,476	5,301	4,921
Net occupancy expense	236	209	459	426
Equipment expense	156	147	296	306
Data processing costs	204	185	392	363
Other noninterest expense	1,272	1,256	2,607	2,340
Total noninterest expense	4,532	4,273	9,055	8,356
Income before income taxes	1,145	1,035	2,294	1,978
Income taxes	373	318	747	603
Net income	$ 772	$ 717	$ 1,547	$ 1,375
Net income per common share				
Basic	$ 0.11	$ 0.10	$ 0.21	$ 0.18
Diluted	$ 0.11	$ 0.10	$ 0.21	$ 0.18
Weighted average shares outstanding				
Basic	7,231,869	7,411,526	7,251,938	7,440,060
Diluted	7,263,199	7,513,197	7,293,310	7,537,143

See accompanying notes

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Uwharrie Capital Corp and Subsidiaries
Consolidated Statement of Changes in Shareholders' Equity

	Common Stock		Additional Paid-in	Unearned ESOP	Undivided	Other Comprehensive	
	Shares	Amount	Capital	Compensation	Profits	Income(Loss)	Total
			(in thousands, except share data)				
Balance, December 31, 2007	7,414,707	$9,268	$ 13,453	$ (800)	$ 9,266	$ 387	$31,574
Net income	—	—	—	—	1,547	—	1,547
Other comprehensive loss	—	—	—	—	—	(737)	(737)
Release of ESOP shares	—	—	9	31	—	—	40
Common stock issued pursuant to:							
Stock options exercised	69,742	87	213	—	—	—	300
Tax benefit of stock options exercised	—	—	26	—	—	—	26
Repurchase of common stock	(76,598)	(96)	(316)	—	—	—	(412)
Stock compensation expense	—	—	13	—	—	—	13
Adjustment to initially apply EITF 06-4	—	—	—	—	(273)	—	(273)
Balance, June 30, 2008	7,407,851	$9,259	$ 13,398	$ (769)	$ 10,540	$ (350)	$32,078

See accompanying notes

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Uwharrie Capital Corp and Subsidiaries
Consolidated Statements of Cash Flows (Unaudited)

	Six Months Ended June 30, 2008	2007
	(dollars in thousands)	
Cash flows from operating activities		
Net income	$ 1,547	$ 1,375
Adjustments to reconcile net income to net cash		
Provided by operating activities:		
Depreciation	319	312
Net amortization of security premiums/discounts	(116)	(90)
Amortization of mortgage servicing rights	237	200
Provision for loan losses	257	(138)
Stock based compensation	13	23
Net realized loss on available sale securities	—	76
Income from mortgage loan sales	(798)	(443)
Proceeds from sales of loans held for sale	36,614	19,565
Origination of loans held for sale	(35,187)	(21,680)
Loss on sale of premises, equipment and other assets	5	—
Increase in cash surrender value of life insurance	(93)	(86)
Gain on sales of other assets	—	(20)
Release of ESOP shares	40	44
Net change in interest receivable	130	(61)
Net change in other assets	(324)	(908)
Net change in interest payable	(58)	(85)
Net change in other liabilities	233	307
Net cash provided (used) by operating activities	2,819	(1,609)
Cash flows from investing activities		
Proceeds from sales, maturities and calls of securities available for sale	4,361	6,874
Purchase of securities available for sale	(3,184)	(11,129)
Net change in Federal Home Loan Bank stock	(232)	8
Net increase in loans	(15,285)	(15,366)
Proceeds from sales of premises, equipment and other assets	—	65
Purchase of premises and equipment	(896)	(223)
Proceeds from sales of foreclosed real estate	—	39
Net cash used in investing activities	(15,236)	(19,732)
Cash flows from financing activities		
Net increase (decrease) in deposit accounts	10,445	(3,560)
Net increase (decrease) in short-term borrowed funds	(11,677)	26,233
Net increase (decrease) in long-term debt	12,504	(12,840)
Repurchase of common stock	(412)	(566)
Net proceeds from issuance of common stock	300	36
Tax benefit of stock options exercised	26	3
Net cash provided by financing activities	11,186	9,306
Decrease in cash and cash equivalents	(1,231)	(12,035)
Cash and cash equivalents, beginning of period	16,197	34,760
Cash and cash equivalents, end of period	$ 14,966	$ 22,725

See accompanying notes

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UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements (Unaudited)

Note 1 – Basis of Presentation

The financial statements and accompanying notes are presented on a consolidated basis including Uwharrie Capital Corp (the "Company") and its subsidiaries, Bank of Stanly ("Stanly"), Anson Bank & Trust Co. ("Anson"), Cabarrus Bank & Trust Company ("Cabarrus"), Strategic Investment Advisors, Inc., ("SIA"), and Uwharrie Mortgage Inc. Stanly consolidates its subsidiaries, the Strategic Alliance Corporation, BOS Agency, Inc. and Gateway Mortgage, Inc., each of which is wholly-owned by Stanly.

The information contained in the consolidated financial statements is unaudited. In the opinion of management, the consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America and material adjustments necessary for a fair presentation of results of interim periods, all of which are of a normal recurring nature, have been made. The results of operations for the interim periods are not necessarily indicative of the results that may be expected for an entire year. Management is not aware of economic events, outside influences or changes in concentrations of business that would require additional clarification or disclosure in the consolidated financial statements. Certain prior period amounts have been reclassified to conform to current period classifications. These reclassifications had no effect on net income or shareholders' equity as previously reported.

The organization and business of the Company, accounting policies followed by the Company and other information are contained in the notes to consolidated financial statements filed as part of the Company's 2007 Annual Report on Form 10-K. This Quarterly report should be read in conjunction with such Annual Report.

Note 2 – Comprehensive Income

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available for sale securities, are reported as a separate component of the equity section of the balance sheet, such items, along with net income, are components of comprehensive income.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
	(in thousands)			
Net Income	$ 772	$ 717	$ 1,547	$1,375
Other comprehensive loss				
Unrealized losses on available for sale securities	(1,009)	(344)	(1,196)	(271)
Related tax effect	386	133	459	105
Reclassification of loss recognized in net income	—	76	—	76
Related tax effect	—	(29)	—	(29)
Total other comprehensive loss	(623)	(164)	(737)	(119)
Comprehensive income	$ 149	$ 553	$ 810	$1,256

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Note 3 – Per Share Data

On October 30, 2007, the Company's Board of Directors declared a 3% stock dividend payable on December 7, 2007 to shareholders of record on November 13, 2007. All information presented in the accompanying interim consolidated financial statements regarding earnings per share and weighted average number of shares outstanding has been computed giving effect to this stock dividend.

Basic and diluted net income per common share is computed based on the weighted average number of shares outstanding during each period after retroactively adjusting for stock dividends. Diluted net income per common share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the net income of the Company. On June 30, 2008 the Company had 89,798 shares that were anti-dilutive and were excluded from the diluted net income per common share computation.

Basic and diluted net income per common share have been computed based upon net income as presented in the accompanying consolidated statements of operations divided by the weighted average number of common shares outstanding or assumed to be outstanding. The computation of basic and dilutive earnings per share is summarized below:

	Three Months Ended June, 30		Six Months Ended June 30,	
	2008	2007	2008	2007
Weighted average number of common shares outstanding	7,366,060	7,561,533	7,386,129	7,590,067
Effect of ESOP shares	(134,191)	(150,007)	(134,191)	(150,007)
Adjusted weighted average number of common shares used in computing basic net income per common share	7,231,869	7,411,526	7,251,938	7,440,060
Effect of dilutive stock options	31,330	101,671	41,372	97,083
Weighted average number of common shares and dilutive potential common shares used in computing diluted net income per common share	7,263,199	7,513,197	7,293,310	7,537,143

Note 4 – Investment Securities

Securities available for sale are summarized below:

	June 30, 2008	December 31, 2007
	(dollars in thousands)	
Amortized Cost	$49,317	$ 50,378
Gross unrealized losses	(1,131)	(92)
Gross unrealized gains	562	719
Fair Value	$48,748	$ 51,005

Management has evaluated these securities to determine whether they should be considered other-than-temporarily impaired at June 30, 2008. This evaluation considered, among other things, the extent and duration of the impairment, current and expected future yields, the

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Company's ability to continue to hold these securities in its portfolio and the issuers' credit ratings. The majority of the gross unrealized losses are related mortgage-backed securities portfolio. Further evaluations were made on these investments including analyzing prepayment rates, general market data, delinquency rates on the underlying mortgage loans and current and anticipated losses in foreclosure.

Based on these evaluations, the Company does not consider these investments to be other-than-temporarily impaired at June 30, 2008. Management expects to collect all contractual interest and principal payments and that recovery of these temporarily impaired securities will occur within a reasonable time frame. Management will continue to evaluate these securities on an ongoing basis, and if it is subsequently determined that an other than temporary impairment has occurred, the Company will record any such impairment as a charge to earnings.

Note 5 – Loans

	June 30, 2008	December 31, 2007
	(in thousands)	
Loans outstanding at period end:		
Commercial	$ 44,085	$ 37,724
Real estate-construction	53,607	46,546
Real estate-residential	134,975	135,959
Real estate-commercial	88,242	86,593
Consumer loans	15,610	15,022
All other loans	216	143
Total	$336,735	$ 321,987

	Three Months Ended June 30, 2008	Three Months Ended June 30, 2007	Six Months Ended June 30, 2008	Six Months Ended June 30, 2007
	(in thousands)			
Analysis of the allowance for loan losses				
Balance at beginning of period	$3,583	$3,034	$3,510	$3,171
Provision charged to operations	171	(138)	257	(138)
Charge-offs	(137)	(16)	(167)	(163)
Recoveries	40	457	57	467
Net recoveries (charge-offs)	(97)	441	(110)	304
Balance at end of period	$3,657	$3,337	$3,657	$3,337

Note 6 – Commitments and Contingencies

The subsidiary banks are party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of their customers. These financial instruments include commitments to extend credit, lines of credit and standby letters of credit. These instruments involve elements of credit risk in excess of amounts recognized in the accompanying financial statements.

The banks' risk of loss with the unfunded loans and lines of credit or standby letters of credit is represented by the contractual amount of these instruments. The banks use the same credit policies in making commitments under such instruments as they do for on-balance sheet instruments. The amount of collateral obtained, if any, is based on management's credit

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evaluation of the borrower. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Credit card commitments are unsecured. At June 30, 2008, outstanding financial instruments whose contract amounts represent credit risk were approximately:

(in thousands)	
Commitments to extend credit	$81,946
Credit card commitments	9,737
Standby letters of credit	1,022
Total commitments	$92,705

Note 7 – Fair Value Disclosures

The Company adopted the provisions of Statement of Financial Accounting Statements (SFAS) No. 157 *Fair Value Measurements* (SFAS 157) and SFAS No. 159, *The Fair Value Option for Financial Assets and Liabilities* (SFAS 159) on January 1, 2008.

SFAS 157 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. SFAS 157 does not require any new fair value measurements, but clarifies and standardizes some divergent practices that have emerged since prior guidance was issued. SFAS 157 creates a three-level hierarchy under which individual fair value estimates are to be ranked based on the relative reliability of the inputs used in the valuation.

SFAS 157 defines fair value as the price that would be received to sell an asset or transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities, the Company considers the principal or most advantageous market in which those assets or liabilities are sold and considers assumptions that market participants would use when pricing those assets or liabilities. Fair values determined using Level 1 inputs rely on active and observable markets to price identical assets or liabilities. In situations where identical assets and liabilities are not traded in active markets, fair values may be determined based on Level 2 inputs, which exist when observable data exists for similar assets and liabilities. Fair values for assets and liabilities for which identical or similar assets and liabilities are not actively traded in observable markets are based on Level 3 inputs, which are considered to be unobservable.

Among the Company's assets and liabilities, investment securities available for sale are reported at their fair values on a recurring basis. Certain other assets are adjusted to their fair value on a nonrecurring basis, including loans held for sale, which are carried at the lower of cost or market, loan servicing rights, where fair value is determined using similar assets with similar characteristics, when available, or based upon discounted cash flows using market-based assumptions, foreclosed real estate, which is carried at lower of cost or fair market value and goodwill, which is periodically tested for impairment. Deposits, short-term borrowings and long-term obligations are not reported at fair value.

The Company does not record loans at fair value on a recurring basis. However, from time to time, a loan is considered impaired and an allowance for loan losses is established. Loans for which it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement are considered impaired. Once a loan is identified as individually impaired, management measures impairment in accordance with SFAS 114, *Accounting by Creditors for Impairment of a Loan,* (SFAS 114). The fair value of impaired loans is estimated using one of several methods, including collateral value, market value of similar debt, enterprise value, liquidation value and discounted cash flows. Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceed the recorded investments in such loans. At June 30, 2008, substantially all of

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the total impaired loans were evaluated based on the fair value of the collateral. In accordance with SFAS 157, impaired loans where an allowance is established based on the fair value of collateral require classification in the fair value hierarchy. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company records the impaired loan as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company records the impaired loan as nonrecurring Level 3.

For assets and liabilities carried at fair value, the following table provides fair value information as of June 30, 2008:

	Total	Level 1	Level 2	Level 3
		(dollars in thousands)		
Investment securities available for sale	$48,748	$9,578	$39,170	$ —
Total assets at fair value	$48,748	$9,578	$39,170	$ —
Total liabilities at fair value	$ —	$ —	$ —	$ —

Prices for US Treasury and government agency securities are readily available in the active markets in which those securities are traded, and the resulting fair values are shown in the ‘Level 1 input’ column. Prices for mortgage-backed securities and for state, county and municipal securities are obtained for similar securities, and the resulting fair values are shown in the ‘Level 2 input’ column. Prices for all other non-marketable investments are determined based on various assumptions that are not observable. The fair values for these investment securities are shown in the ‘Level 3 input’ column. Non-marketable investment securities, which are carried at their purchase price, include those that may only be redeemed by the issuer.

The Company may be required, from time to time, to measure certain assets at fair value on a nonrecurring basis in accordance with U.S. generally accepted accounting principles. These include assets that are measured at the lower of cost or market that were recognized at fair value below cost at the end of the period. Assets measured at fair value on a nonrecurring basis are included in the table below as of June 30, 2008:

	Total	Level 1	Level 2	Level 3
		(dollars in thousands)		
Loans	$6,913	$ —	$6,913	$ —
Total assets at fair value	$6,913	$ —	$6,913	$ —
Total liabilities at fair value	$ —	$ —	$ —	$ —

SFAS 159 allows an entity to elect to measure certain financial assets and liabilities at fair value with changes in fair value recognized in the income statement each period. The statement also requires additional disclosures to identify the effects of an entity’s fair value election on its earnings. Upon the adoption of SFAS 159, the Company did not elect to report any assets and liabilities at fair value.

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Note 8 – Recent Accounting Pronouncements

SAB 109

Staff Accounting Bulletin No. 109 ("SAB 109"), "Written Loan Commitments Recorded at Fair Value Through Earnings," supersedes Staff Accounting Bulletin No. 105 by requiring the expected net future cash flows related to servicing a loan to be included in the measurement of all written loan commitments that are accounted for at fair value through earnings. The adoption of SAB 109 on January 1, 2008, did not have a significant impact on the Company's consolidated financial statements.

SFAS 157

Statement of Financial Accounting Standards No. 157 ("SFAS 157"), *Fair Value Measurements*, defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. The Company adopted the provisions of SFAS 157 on January 1, 2008 as discussed in Note 7 above.

SFAS 159

Statement of Financial Accounting Standards No. 159 ("SFAS 159"), *The Fair Value Option for Financial Assets and Financial Liabilities*, permits entities to choose to measure many financial instruments and certain other items at fair value. The objective of this standard is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This statement is effective for fiscal years beginning after November 15, 2007, with early adoption permitted under certain circumstances. The adoption of SFAS 159 did not have any impact on the Company's consolidated financial statements. See Note 7 above.

EITF 06-4

The Emerging Issues Task Force (EITF) reached a consensus at its September 2006 meeting regarding EITF 06-4, *Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements*. The scope of EITF 06-4 is limited to the recognition of a liability and related compensation costs for endorsement split-dollar life insurance policies that provide a benefit to an employee that extends to postretirement periods. Therefore, this EITF would not apply to a split-dollar life insurance arrangement that provides a specified benefit to an employee that is limited to the employee's active service period with an employer. This EITF 06-4 is effective for fiscal years beginning after December 15, 2007, with earlier application permitted. The Company adopted EITF 06-4 on January 1, 2008 and it had the effect of reducing beginning consolidated undivided profits by approximately $273,000.

From time to time, the FASB issues exposure drafts of proposed statements of financial accounting standards. Such exposure drafts are subject to comment from the public, to revisions by the FASB and to final issuance by the FASB as statements of financial accounting standards. Management considers the effect of the proposed statements on the consolidated financial statements of the Company and monitors the status of changes to and proposed effective dates of exposure drafts.

Reclassification

Certain amounts in the 2007 consolidated financial statements have been reclassified to conform to the 2008 presentation. The reclassifications had no effect on net income or shareholders' equity as previously reported.

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

This Quarterly Report on Form 10-Q may contain certain forward-looking statements consisting of estimates with respect to the financial condition, results of operations and business of the Company that are subject to various factors which could cause actual results to differ materially from these estimates. These factors include, but are not limited to, general economic conditions, changes in interest rates, deposit flows, loan demand, real estate values, and competition; changes in accounting principles, policies, or guidelines; changes in legislation or regulation; and other economic, competitive, governmental, regulatory, and technological factors affecting the Company's operations, pricing, products and services.

Comparison of Financial Condition at June 30, 2008 and December 31, 2007.

During the six months ended June 30, 2008, the Company's total assets increased $12.3 million, from $411.9 million to $424.2 million. During the six months, loans held for investment increased $14.7 million or 4.6%, from $322.0 million at December 31, 2007 to $336.7 million at June 30, 2008. This increase, however, was offset by a decline in investment securities of $2.3 million and a decrease in loans held for sale of $1.0 million during the period.

Cash and cash equivalents decreased $1.2 million during the six months ended June 30, 2008. Cash and due from banks declined $180 thousand, while interest-earning deposits with banks decreased $1.0 million.

Investment securities decreased $2.3 million or 4.4% for the six months. Market values have declined $1.2 million due to the recent downturn in the investment markets. Management believes this decline in investment market values is only temporary and does not expect to incur a loss at this time. The remainder of the decrease resulted primarily from normal mortgage backed securities pay down activity during the period.

As previously stated, loans held for investment increased $14.7 million to $336.7 million during the period ended June 30, 2008. The Company has experienced positive growth trends in its residential construction, commercial and consumer areas of the loan portfolio. These positive trends were impacted by a decrease in our one to four family residential real estate loan portfolio. Loans held for sale decreased 34.2% or $1.0 million during the period. The allowance for loan losses was $3.7 million at June 30, 2008 which represents 1.09% of the loan portfolio.

Other changes in our consolidated assets related to premises and equipment, interest receivable, Federal Home Loan Bank stock, bank owned life insurance and other assets. Fixed assets increased $572 thousand, interest receivable declined $130 thousand, bank owned life insurance increased $93 thousand and other assets increased $1.3 million. Federal Home Loan Bank stock increased $232 thousand. Federal Home Loan Bank stock ownership is a requirement for member banks that utilize Federal Home Loan Bank for borrowing funds. The amount of stock owned by each member bank is based primarily on the amount of borrowings outstanding.

Customer deposits, our primary funding source, experienced a $10.4 million increase during the six months ended June 30, 2008, increasing from $324.7 million to $335.1 million. Time deposits $100,000 and over grew by $2.0 million, interest checking and money market accounts increased $8.0 million and savings accounts grew $747 thousand. These increases were offset by declines in other time deposits of $104 thousand and demand deposits of $235 thousand.

Total borrowings increased $827 thousand for the period. Borrowings consist of both short-term and long-term borrowed funds. The Company utilizes both short-term and long-term advances from the Federal Home Loan Bank. At June 30, 2008, $33.7 million of the total borrowings of $54.4 million were comprised of Federal Home Loan Bank advances.

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Other liabilities increased from $1.5 million at December 31, 2007 to $2.0 million at June 30, 2008, an increase of $506 thousand. The Company has a supplemental retirement plan in place for four executive officers. The Company has purchased life insurance policies in order to provide future funding of benefit payments. As discussed in Note 7, with the adoption of EITF 06-4, *Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements*, the Company recorded a $273 thousand liability. This adjustment coupled with an increase in the reserve for income taxes were the primary factors associated with the increase in other liabilities.

At June 30, 2008, total shareholders' equity was $32.1 million, an increase of $504 thousand from December 31, 2007. Net income for the period was $1.5 million and the Company received $300 thousand from the exercise of stock options. These increases were offset by the repurchase of 76,598 shares of the Company's common stock at a cost of $412 thousand and unrealized losses on investment securities, net of tax, of $737 thousand. The Company also recorded a $273 thousand one-time cumulative adjustment to undivided profits for the adoption of EITF 06-4. At June 30, 2008, the Company and its subsidiary banks exceeded all applicable regulatory capital requirements.

Comparison of Results of Operations For the Three Months Ended June 30, 2008 and 2007.

Net Income

Uwharrie Capital Corp reported net income of $772 thousand, or $0.11 per basic share, for the three months ended June 30, 2008, as compared to $717 thousand, or $0.10 per basic share, for the three months ended June 30, 2007, an increase of $55 thousand, or $0.01 per share.

Net Interest Income

The Company's primary source of income, net interest income, increased $275 thousand or 7.5% for the three months ended June 30, 2008, as compared to the same period for 2007. Refer to the six month discussion on page 16 for further information.

Provision and Allowance for Loan Losses

The provision for loan losses was $171 thousand for the three months ending June 30, 2008 compared to ($138) thousand for the same period in 2007. There were net loan charge-offs of $97 thousand for the three months ended June 30, 2008 as compared with net loan recoveries of $441 thousand during the same period of 2007. Refer to the Asset Quality discussion on page 18 for further information.

Noninterest Income

The Company generates most of its revenue from net interest income; however, like all financial institutions, diversification of our earnings base is of major importance in our long term success. Total noninterest income increased $403 thousand, from $1.5 million for the quarter ended June 30, 2007 to $1.9 million for the same period in 2008. Service charges on deposit accounts produced earnings of $537 thousand for the three months ended June 30, 2008. Other service fees and commissions experienced a 4.6% increase for the comparable three month period. Growth in ATM fees of $25 thousand and investment fees on managed accounts of $34 thousand enhanced this increase. Income from mortgage loan sales increased $169 thousand from $188 thousand for the quarter ended June 30, 2007 to $357 thousand for the

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same period in 2008. The interest rate reductions during the first quarter attributed to the increase in mortgage loan sales. The Company also owned shares of MasterCard stock and redeemed this stock during the second quarter of 2008 resulting in other income of $162 thousand. This income was the primary reason for the increase in other income over the comparable period.

Noninterest Expense

Noninterest expense for the quarter ended June 30, 2008 was $4.5 million compared to $4.3 million for the same period of 2007, an increase of $259 thousand. Salaries and employee benefits, the largest component of noninterest expense, increased $188 thousand, from $2.5 million for the quarter ending June 30, 2007 to $2.7 million for the same period in 2008. The Company has a non-qualifying deferred compensation plan for certain executive officers. The costs associated with this plan increased $83 thousand for the comparable periods. This increase coupled with normal salary increases contributed to the overall increase in noninterest expense. Other noninterest expense increased $16 thousand for the comparable three month periods. The table below reflects the composition of other noninterest expense.

Other noninterest expense

	Three Months Ended June 30,	
	2008	2007
	(in thousands)	
Professional fees and services	$ 173	$ 218
Marketing and donations	145	152
Office supplies and printing	19	30
Telephone and data lines	62	60
Electronic banking expense	200	167
Software amortization and maintenance	124	118
Loan collection expense	56	43
Shareholder relations expense	43	55
Dues and subscriptions	40	38
Postage	49	46
Other	361	329
Total	$ 1,272	$ 1,256

Income Tax Expense

The Company had income tax expense of $373 thousand for the three months ended June 30, 2008 resulting in an effective tax rate of 32.58% compared to income tax expense of $318 thousand and an effective rate of 30.72% in the 2007 period. Income taxes computed at the statutory rate are reduced primarily by the eligible amount of interest earned on state and municipal securities, tax free municipal loans and income earned on bank owned life insurance. The increase in the effective tax rate resulted primarily from the decrease in the level of such tax free income as a percentage of income before income taxes in the current year quarter compared to the 2007 quarter.

Comparison of Results of Operations For the Six Months Ended June 30, 2008 and 2007.

Net Income

Uwharrie Capital Corp reported net income of $1.5 million or $0.21 per basic share, for the six months ended June 30, 2008, as compared to $1.4 million, or $0.18 per basic share, for the six months ended June 30, 2007, an increase of $172 thousand, or $0.03 per share.

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Net Interest Income

As with most financial institutions, the primary component of earnings for our banks, is net interest income. Net interest income is the difference between interest income, principally from loan and investment securities portfolios, and interest expense, principally on customer deposits and borrowings. Changes in net interest income result from changes in volume, spread and margin. For this purpose, volume refers to the average dollar level of interest-earning assets and interest-bearing liabilities, spread refers to the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities, and margin refers to net interest income divided by average interest-earning assets. Margin is influenced by the level and relative mix of interest-earning assets and interest-bearing liabilities, as well as by levels of noninterest-bearing liabilities and capital.

Net interest income for the six months ended June 30, 2008 was $7.8 million as compared with $7.2 million during the six months ended June 30, 2007, resulting in an increase of $684 thousand, or 9.6%. During the six months ended June 30, 2008 our growth in the volume of interest-earning assets outpaced the growth in interest-bearing liabilities by $947 thousand. The average yield on our interest–earning assets decreased 50 basis points to 6.94%, while the average rate we paid for our interest-bearing liabilities decreased 75 basis points. The Company’s assets that are interest rate sensitive adjust at the time the Federal Reserve Open Market Committee adjusts interest rates, while, interest-bearing time deposits adjust at the time of maturity. The fore mentioned decreases resulted in an increase of 25 basis points in our interest rate spread, from 3.55% in 2007 to 3.80% in 2008. Our net interest margin was 4.22% and 4.10% for the comparable periods in 2008 and 2007.

The following table presents average balance sheets and a net interest income analysis for the six months ended June 30, 2008 and 2007:

Average Balance Sheet and Net Interest Income Analysis
For the Six Months Ended June 30,

	Average Balance		Income/Expenses		Rate/Yield	
(in thousands)	**2008**	**2007**	**2008**	**2007**	**2008**	**2007**
Interest-earning assets:						
Taxable securities	$ 38,537	$ 27,831	$ 1,075	$ 724	5.61%	5.23%
Nontaxable securities (1)	13,726	13,138	323	314	7.70%	7.85%
Short-term investments	3,487	24,482	43	635	2.48%	5.22%
Taxable loans	326,770	295,136	11,550	11,424	7.11%	7.78%
Non-taxable loans (1)	3,895	3,952	88	95	7.44%	7.85%
Total interest-earning assets	386,415	364,539	13,079	13,192	6.94%	7.44%
Interest-bearing liabilities:						
Interest-bearing deposits	283,537	264,086	4,280	4,827	3.04%	3.68%
Short-term borrowed funds	18,493	23,944	334	640	3.63%	5.38%
Long-term debt	32,755	23,932	619	563	3.80%	4.73%
Total interest bearing liabilities	334,785	311,962	5,233	6,030	3.14%	3.89%
Net interest spread	$ 51,630	$ 52,577	$ 7,846	$ 7,162	3.80%	3.55%
Net interest margin (1) (% of earning assets)					4.22%	4.10%

(1) Yields related to securities and loans exempt from income taxes are stated on a fully tax-equivalent basis, assuming a 38.55% tax rate.

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Provision and Allowance for Loan Losses

The provision for loan losses was $257 thousand for the six months ending June 30, 2008 compared to ($138) thousand for the same period in 2007. There were net loan charge-offs of $110 thousand for the six months ended June 2008 as compared with net loan recoveries of $304 thousand during the same period of 2007. Refer to the Asset Quality discussion on page 18 for further information.

Noninterest Income

The Company generates most of its revenue from net interest income; however, like all financial institutions, diversification of our earnings base is of major importance in our long term success. Total noninterest income increased $726 thousand, from $3.0 million for the six months ended June 30, 2007 to $3.8 million for the same period in 2008. Service charges on deposit accounts produced earnings of $1.1 million for the six months ended June 30, 2008. Other service fees and commissions experienced a 5.8% increase for the comparable six month period. Growth in ATM fees of $60 thousand and investment fees on managed accounts of $91 thousand enhanced this increase. Income from mortgage loan sales increased $355 thousand from $443 thousand for the six months ended June 30, 2007 to $798 thousand for the same period in 2008. The interest rate reductions during the period attributed to the increase in mortgage loan sales. The Company owns shares of VISA stock and MasterCard stock. VISA redeemed a portion of this stock during the first quarter of 2008 resulting in other income of $59 thousand. We sold all of the shares of MasterCard during second quarter of 2008 producing other income of $162 thousand. This income was the primary reason for the increase in other income for the comparable periods.

Noninterest Expense

Noninterest expense for the six months ended June 30, 2008 was $9.1 million compared to $8.4 million for the same period of 2007, an increase of $699 thousand. Salaries and employee benefits, the largest component of noninterest expense, increased $380 thousand, from $4.9 million for the six months ended June 30, 2007 to $5.3 million for the same period in 2008. The Company has a non-qualifying deferred compensation plan for certain executive officers. The costs associated with this plan increased $167 thousand for the comparable periods. This increase coupled with normal salary increases contributed to the overall increase in noninterest expense. Other noninterest expense increased $267 thousand for the comparable six month periods. The table below reflects the composition of other noninterest expense.

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Other noninterest expense

	Six Months Ended June 30, 2008	Six Months Ended June 30, 2007
	(in thousands)	
Professional fees and services	$ 338	$ 376
Marketing and donations	317	277
Office supplies and printing	135	140
Telephone and data lines	122	116
Electronic banking expense	386	329
Software amortization and maintenance	223	222
Loan collection expense	127	68
Shareholder relations expense	101	100
Dues and subscriptions	77	70
Postage	96	79
Other	685	563
Total	$2,607	$2,340

Income Tax Expense

The Company had income tax expense of $747 thousand for the six months ended June 30, 2008 resulting in an effective tax rate of 32.56% compared to income tax expense of $603 thousand and an effective rate of 30.49% in the 2007 period. Income taxes computed at the statutory rate are reduced primarily by the eligible amount of interest earned on state and municipal securities, tax free municipal loans and income earned on bank owned life insurance. The increase in the effective tax rate resulted primarily from the decrease in the level of such tax free income as a percentage income before income taxes in the current year period compared to the 2007 period.

Asset Quality

The Company's allowance for loan losses is established through charges to earnings in the form of a provision for loan losses. The allowance is increased by provisions charged to operations and by recoveries of amounts previously charged off, and reduced by loans charged off. Management evaluates the adequacy of the allowance at least quarterly. In evaluating the adequacy of the allowance, management considers the growth, composition and industry diversification of the portfolio; historical loan loss experience; current delinquency levels; adverse situations that may affect a borrower's ability to repay; estimated value of any underlying collateral; prevailing economic conditions and other relevant factors. The Company's credit administration function, through a review process, validates the accuracy of the initial risk grade assessment. In addition, as a given loan's credit quality improves or deteriorates, the credit administration department has the responsibility to change the borrower's risk grade accordingly. For loans determined to be impaired, the allowance is based either on discounted cash flows using the loan's initial effective interest rate or on the fair value of the collateral for certain collateral dependent loans. This evaluation is inherently subjective, as it requires material estimates, including the amounts and timing of future cash flows expected to be received on impaired loans, which may be susceptible to significant change. In addition, regulatory agencies, as an integral part of their examination process, periodically review the allowance for loan losses and may require additions for estimated losses based upon judgments different from those of management.

Management uses the risk-grading program to facilitate the evaluation of probable inherent loan losses and the adequacy of the allowance for loan losses. In this program, risk grades are initially assigned by loan officers and reviewed and monitored by credit administration. The Company strives to maintain its loan portfolio in accordance with conservative loan underwriting

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policies that result in loans specifically tailored to the needs of its market area. Every effort is made to identify and minimize the credit risks associated with such lending strategies. The Company has no foreign loans and does not engage in significant lease financing or highly leveraged transactions. The Company follows a loan review program designed to evaluate the credit risk in the loan portfolio. This process includes the maintenance of an internally classified watch list that helps management assess the overall quality of the loan portfolio and the adequacy of the allowance for loan losses. In establishing the appropriate classification for specific assets, management considers, among other factors, the estimated value of the underlying collateral, the borrower's ability to repay, the borrower's payment history and the current delinquent status. As a result of this process, certain loans are categorized as substandard, doubtful or loss and reserves are allocated based on management's judgment and historical experience.

The allowance for loan losses represents management's estimate of an appropriate amount to provide for known and inherent losses in the loan portfolio in the normal course of business. While management believes that it uses the best information available to establish the allowance for loan losses, future adjustments to the allowance may be necessary and results of operations could be adversely affected if circumstances differ substantially from the assumptions used in making the determinations. Furthermore, while management believes it has established the allowance for loan losses in conformity with generally accepted accounting principles, there can be no assurance that regulators, in reviewing the Company's portfolio, will not require an adjustment to the allowance for loan losses. In addition, because future events affecting borrowers and collateral cannot be predicted with certainty, there can be no assurance that the existing allowance for loan losses is adequate or that increases will not be necessary, should the quality of any loans deteriorate as a result of the factors discussed herein. Any material increase in the allowance for loan losses may adversely affect the Company's financial condition and results of operations.

The provision for loan losses was $257 thousand for the six months ended June 30, 2008 as compared to ($138) thousand for the same period in 2007. Additionally, the allowance expressed as a percentage of loans held for investment was 1.09% at both June 30, 2008 and December 31, 2007. During the first six months of 2008 the levels of our impaired loans, which includes all loans in nonaccrual status and other loans deemed by management to be impaired, were $9.7 million compared to $7.5 million at December 31, 2007, an increase of $2.2 million. Of the $9.7 million in impaired loans at June 30, 2008, $6.9 million carried an allowance of $1.3 million while $2.8 million were evaluated and required no specific allowance. The level of specific reserves identified for impaired loans increased by $62 thousand for the same period. These increases were due primarily to the impairment of a loan relationship with one customer of $2.6 million, for which a $50 thousand specific reserve has been provided. Net loan recoveries for the six months ending June 30, 2007 were $304 thousand, while the same period in 2008 experienced net loan charge-offs of $110 thousand.

The allowance as a percentage of total impaired loans has increased from 35.7% at December 31, 2007 to 35.9% at June 30, 2008. The portion of the allowance specifically allocable to impaired loans decreased from 16.8% at December 31, 2007 to 13.6% at June 30, 2008. Management believes the current level of allowance for loan losses to be appropriate given the risk inherence in the loan portfolio at this time.

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The following nonperforming loan table shows the comparison for the six months ended June 30, 2008 to December 31, 2007:

Nonperforming Assets
(dollars in thousands)

	June 30, 2008	December 31, 2007
Nonperforming assets:		
Nonaccrual loans	$ 1,539	$ 1,795
Other real estate owned	590	163
Total nonperforming assets	$ 2,129	$ 1,958
Accruing loans past due 90 days or more	$ 11	$ —
Allowance for loans losses	3,657	3,510
Nonperforming loans to total loans	0.46%	0.56%
Allowance for loan losses to total loans	1.09%	1.09%
Nonperforming assets to total loans and other real estate	0.63%	0.61%
Nonperforming assets to total assets	0.50%	0.48%
Allowance for loan losses to Nonperforming loans	237.62%	195.57%

Liquidity and Capital Resources

The objective of the Company's liquidity management policy is to ensure the availability of sufficient cash flows to meet all financial commitments and to capitalize on any opportunities for expansion. Liquidity management addresses the ability to meet deposit withdrawals on demand or at contractual maturity, to repay borrowings as they mature and to fund new loans and investments as opportunities arise.

The Company's primary sources of internally generated funds are principal and interest payments on loans, cash flows generated from operations and cash flow generated by investments. Growth in deposits is typically the primary source of funds for loan growth. The Company and its subsidiary banks have multiple funding sources in addition to deposits that can be used to increase liquidity and provide additional financial flexibility. These sources are the subsidiary banks' established federal funds lines with correspondent banks aggregating $20.4 million at June 30, 2008, with available credit of $14.4 million, established borrowing relationships with the Federal Home Loan Bank, with available credit of $33.1 million, access to borrowings from the Federal Reserve Bank discount window, and the sale of securities under agreements to repurchase. In addition, the Company issues commercial paper and has secured long-term debt from other sources. Total debt from these sources aggregated $54.4 million at June 30, 2008, compared to $53.6 million at December 31, 2007.

Banks and bank holding companies, as regulated institutions, must meet required levels of capital. The FDIC and the Federal Reserve, the primary federal regulators of the Company and its subsidiary banks, have adopted minimum capital regulations or guidelines that categorize components and the level of risk associated with various types of assets.

Regulatory guidelines require a minimum of total capital to risk-adjusted assets ratio of 8 percent and a Tier I leverage ratio of 4 percent. Banks, which meet or exceed a Tier I ratio of 6 percent, a total capital ratio of 10 percent and a Tier I leverage ratio of 5 percent are considered "well capitalized" by regulatory standards. Financial institutions are expected to maintain a level of capital commensurate with the risk profile assigned to their assets in accordance with those guidelines.

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Both the Company and its subsidiary banks have maintained capital levels exceeding minimum levels for “well capitalized” banks and bank holding companies. The Company expects to continue to exceed these minimums without altering current operations or strategy. The Company began a private placement of subordinated debt during the second quarter of 2008 that will qualify as regulatory capital. At June 30, 2008, the Company had $2.5 million in subordinated debt. The placement will continue into the third quarter.

Accounting and Regulatory Matters

Management is not aware of any known trends, events, uncertainties or current recommendations by regulatory authorities that will have or that are reasonably likely to have a material effect on the Company’s liquidity, capital resources, or other operations.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

The Company’s primary market risk is interest rate risk. Interest rate risk is the result of differing maturities or repricing intervals of interest-earning assets and interest-bearing liabilities and the fact that rates on these financial instruments do not change uniformly. These conditions may impact the earnings generated by the Company’s interest earning assets or the cost of its interest-bearing liabilities, thus directly impacting the Company’s overall earnings. The Company’s management actively monitors and manages interest rate risk. One way this is accomplished is through the development of and adherence to the Company’s asset/liability policy. This policy sets forth management’s strategy for matching the risk characteristics of the Company’s interest-earning assets and liabilities so as to mitigate the effect of changes in the rate environment. The Company’s market risk profile has not changed significantly since December 31, 2007.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

At the end of the period covered by this report, the Company carried out an evaluation, under the supervision and with the participation of the Company’s management, including the Company’s principal executive officer and principal financial officer, of the effectiveness of the design and operation of the Company’s disclosure controls and procedures pursuant to Securities Exchange Act Rule 13a-15.

Based upon that evaluation, the principal executive officer and principal financial officer concluded that the Company’s disclosure controls and procedures were effective (1) to provide reasonable assurance that information required to be disclosed by the Company in the reports filed or submitted by it under the Securities Exchange Act was recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms, and (2) to provide reasonable assurance that information required to be disclosed by the Company in such reports is accumulated and communicated to the Company’s management, including its principal executive officer and principal financial officer, as appropriate to allow for timely decisions regarding required disclosure.

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Changes in Internal Control over Financial Reporting

Management of the Company has evaluated, with the participation of the Company's principal executive officer and principal financial officer, changes in the Company's internal controls over financial reporting (as defined in Rule 13a -15(f) and 15d – 15(f) of the Exchange Act) during the second quarter of 2008. In connection with such evaluation, the Company has determined that there were no changes in the Company's internal control over financial reporting during the period covered by this report that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting. The Company reviews its disclosure controls and procedures, which may include its internal control over financial reporting, on an ongoing basis, and may from time to time make changes aimed at enhancing their effectiveness and to ensure that the Company's systems evolve with its business.

Part II. OTHER INFORMATION

Item 1. Legal Proceedings

Neither the Company nor its subsidiaries, nor any of their properties are subject to any legal proceedings other than ordinary routine litigation incidental to their business.

Item 1A. Risk Factors

Not applicable.

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

The following table sets forth information with respect to shares of common stock repurchased by the Company during the three months ended June 30, 2008.

	(a) Total Number of Shares Purchased	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Program (1)	(d) Maximum Dollar Value of Shares that May Yet Be Purchased Under the Plans (2)(3)
April 1, 2008 Through April 30, 2008	48,865	$ 5.35	—	$ —
May 1, 2008 Through May 31, 2008	—	$ —	—	$ —
June 1, 2008 Through June 30, 2008	5,427	$ 5.42	—	$ —
Total	54,292	$ 5.36	—	$ —

(1) Trades of the Company's stock occur in the Over-the-Counter marketplace from time to time. The Company also has in place a Stock Repurchase Plan that provides liquidity to its shareholders in the event a willing buyer is not available to purchase shares that are offered for sale. The Company is under no obligation to purchase shares offered; however, it will accommodate such offers as its Stock Repurchase Plan allows. This plan was initially adopted in 1995 and is approved annually by resolution of the Board of Directors or the Executive Committee of the Board.

(2) On April 15, 2008, the Executive Committee of Uwharrie Capital Corp mandated by resolution that the Company could repurchase 48,865 shares of its common stock at a cost of $261,428.

(3) On June 30, 2008, the Executive Committee of Uwharrie Capital Corp mandated by resolution that the Company could repurchase 5,427 shares of its common stock at a cost of $29,431.

Item 3. Defaults Upon Senior Securities

None

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

The Company's annual meeting of shareholders was held on Tuesday, May 13, 2008 in Albemarle, North Carolina. Proposals listed in the Proxy Statement dated March 28, 2008, (1) to elect six (6) directors of the Company to three (3) year terms and (2) to ratify the appointment of the Company's independent public accountants for 2008, were approved by the shareholders as listed below. There were no other matters submitted for vote of the shareholders at this meeting.

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Proposal (1) To elect six (6) directors to three (3) year terms. Votes for each nominee were as follows:

Nominee	For	Withheld
Joe S. Brooks	4,686,516	20,019
Ronald T. Burleson	4,682,339	24,196
Charles F. Geschickter	4,660,254	46,290
W. Chester Lowder	4,679,620	26,915
John P. Murray	4,686,286	20,249
Susan J. Rourke	4,674,627	31,908

The following twelve directors continued in office: Henry E. Farmer, Sr., Thomas M. Hearne, Jr., Charles D. Horne, Joseph R. Kluttz, Jr., James E. Nance, Emmett S. Patterson, Timothy J. Propst, Donald P. Scarborough, John W. Shealy, Jr., Michael E. Snyder, Sr., Douglas L Stafford, and Emily M. Thomas.

Proposal (2) To ratify the appointment of Dixon Hughes PLLC as the Company's independent registered public accounting firm for 2008.

For	4,660,560
Against	5,535
Abstain	40,440

Item 5. Other Information

None

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Item 6. Exhibit

Exhibit Number	Description of Exhibit
3.1	Registrant's Articles of Incorporation *
3.2	Registrant's By-laws *
4	Form of stock certificate *
10.1	Incentive Stock Option Plan, as amended *
10.2	Employee Stock Ownership Plan and Trust **
10.3	2006 Incentive Stock Option Plan ***
10.4	2006 Employee Stock Purchase Plan ***
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith)
31.2	Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith)
32	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith)

* Incorporated by reference from exhibits to Registrant's Registration Statement on Form S-4 (Reg. No. 33-58882).
** Incorporated by reference to Registrant's Annual Report on Form 10-KSB for the Fiscal year ended 1999.
*** Incorporated by reference to Registrant's Quarterly Report on Form 10-Q for the Quarter ended June 30, 2006.

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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 who is thereunto duly authorized.

	UWHARRIE CAPITAL CORP (Registrant)
Date: August 8, 2008	By: /s/ Roger L. Dick Roger L. Dick President and Chief Executive Officer
Date: August 8, 2008	By: /s/ Barbara S. Williams Barbara S. Williams Principal Financial Officer

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EXHIBIT INDEX

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* Incorporated by reference

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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 September 30, 2008

OR

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

For the transition period from ______ to ______.

COMMISSION FILE NUMBER 000-22062

UWHARRIE CAPITAL CORP
(Exact name of registrant as specified in its charter)

NORTH CAROLINA **(State or Other Jurisdiction of Incorporation or Organization)**	**56-1814206** **(I.R.S. Employer Identification No.)**
132 NORTH FIRST STREET **ALBEMARLE, NORTH CAROLINA** **(Address of Principal Executive Offices)**	**28001** **(Zip Code)**

Registrant's Telephone number, including area code: (704) 983-6181

N/A
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. ☒ Yes ☐ No

Indicate by check mark 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.

Large accelerated filer ☐	Accelerated filer ☐
Non-accelerated filer ☐ (Do not check if a smaller reporting company)	Smaller reporting company ☒

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange

Act). ☐ Yes ☒ No

Indicate the number of shares outstanding of each of the classes of common stock issuer's as of the latest practicable date: 7,407,851 shares of common stock outstanding as of November 1, 2008.

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Uwharrie Capital Corp and Subsidiaries
Consolidated Balance Sheets

Part I. FINANCIAL INFORMATION
Item 1 - Financial Statements

	September 30, 2008 (Unaudited)	December 31, 2007*
	(dollars in thousands)	
ASSETS		
Cash and due from banks	$ 13,318	$ 13,765
Interest-earning deposits with banks	2,808	2,432
Securities available for sale, at fair value	43,009	51,005
Loans held for sale	1,073	2,916
Loans:		
Loans held for investment	341,830	321,987
Less allowance for loan losses	(4,143)	(3,510)
Net loans held for investment	337,687	318,477
Premises and equipment, net	10,297	8,751
Interest receivable	2,041	2,055
Federal Home Loan Bank stock	2,092	2,137
Bank owned life insurance	5,459	5,318
Goodwill	987	987
Other real estate owned	752	163
Other assets	5,801	3,938
Total assets	$ 425,324	$ 411,944
LIABILITIES		
Deposits:		
Demand noninterest-bearing	$ 48,437	$ 46,597
Interest checking and money market accounts	115,196	102,411
Savings deposits	25,886	26,200
Time deposits, $100,000 and over	57,409	54,729
Other time deposits	97,683	94,720
Total deposits	344,611	324,657
Short-term borrowed funds	9,461	31,928
Long-term debt	36,753	21,691
Interest payable	498	596
Other liabilities	2,222	1,498
Total liabilities	393,545	380,370
Off balance sheet items, commitments and contingencies (Note 6)		
SHAREHOLDERS' EQUITY		
Common stock, $1.25 par value: 20,000,000 shares authorized; shares issued and outstanding 7,407,851 and 7,414,707 shares respectively	9,259	9,268
Additional paid-in capital	13,408	13,453
Unearned ESOP compensation	(752)	(800)
Undivided profits	10,883	9,266
Accumulated other comprehensive income (loss)	(1,019)	387
Total shareholders' equity	31,779	31,574
Total liabilities and shareholders' equity	$ 425,324	$ 411,944

(*) Derived from audited consolidated financial statements

See accompanying notes

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Uwharrie Capital Corp and Subsidiaries
Consolidated Statements of Operations (Unaudited)

	Three Months Ended September 30, 2008	Three Months Ended September 30, 2007	Nine Months Ended September 30, 2008	Nine Months Ended September 30, 2007
	(in thousands, except share and per share data)			
Interest Income				
Loans, including fees	$ 5,652	$ 6,174	$ 17,290	$ 17,693
Investment securities				
US Treasury	24	25	73	73
US Government agencies and corporations	376	376	1,331	972
State and political subdivisions	182	157	510	477
Other	17	38	83	112
Interest-earning deposits with banks and federal funds sold	16	76	59	711
Total interest income	6,267	6,846	19,346	20,038
Interest Expense				
Interest checking and money market accounts	345	639	1,092	2,015
Savings deposits	68	132	237	412
Time deposits, $100,000 and over	578	529	1,864	1,701
Other time deposits	888	1,052	2,966	3,051
Short-term borrowed funds	73	352	407	843
Long-term debt	395	260	1,014	972
Total interest expense	2,347	2,964	7,580	8,994
Net interest income	3,920	3,882	11,766	11,044
Provision for loan losses	529	18	786	(120)
Net interest income after provision for loan losses	3,391	3,864	10,980	11,164
Noninterest Income				
Service charges on deposit accounts	599	550	1,666	1,609
Other service fees and commissions	737	750	2,239	2,169
Loss on sale of securities	—	—	—	(76)
Gain on sale fixed assets/other assets	11	6	6	26
Income from mortgage loan sales	206	235	1,004	678
Other income	97	119	495	288
Total noninterest income	1,650	1,660	5,410	4,694
Noninterest Expense				
Salaries and employee benefits	2,620	2,493	7,921	7,414
Net occupancy expense	250	219	709	645
Equipment expense	178	150	474	456
Data processing costs	194	188	586	551
Other noninterest expense	1,300	1,364	3,907	3,704
Total noninterest expense	4,542	4,414	13,597	12,770
Income before income taxes	499	1,110	2,793	3,088
Income taxes	156	336	903	939
Net income	$ 343	$ 774	$ 1,890	$ 2,149
Net income per common share				
Basic	$ 0.05	$ 0.10	$ 0.25	$ 0.29
Diluted	$ 0.05	$ 0.10	$ 0.25	$ 0.29
Weighted average shares outstanding				
Basic	7,495,903	7,566,368	7,481,606	7,631,112
Diluted	7,541,820	7,703,672	7,525,329	7,743,681

See accompanying notes

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Uwharrie Capital Corp and Subsidiaries
Consolidated Statement of Changes in Shareholders' Equity (Unaudited)

	Common Stock		Additional Paid-in	Unearned ESOP	Undivided	Other Comprehensive	
	Shares	Amount	Capital	Compensation	Profits	Income(Loss)	Total
			(in thousands, except share data)				
Balance, December 31, 2007	7,414,707	$9,268	$ 13,453	$ (800)	$ 9,266	$ 387	$ 31,574
Net income	—	—	—	—	1,890	—	1,890
Other comprehensive loss	—	—	—	—	—	(1,406)	(1,406)
Release of ESOP shares	—	—	12	48	—	—	60
Common stock issued pursuant to:							
Stock options exercised	69,742	87	213	—	—	—	300
Tax benefit of stock options exercised	—	—	26	—	—	—	26
Repurchase of common stock	(76,598)	(96)	(316)	—	—	—	(412)
Stock compensation expense	—	—	20	—	—	—	20
Adjustment to initially apply EITF 06-4	—	—	—	—	(273)	—	(273)
Balance, September 30, 2008	7,407,851	$9,259	$ 13,408	$ (752)	$ 10,883	$ (1,019)	$31,779

See accompanying notes

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Uwharrie Capital Corp and Subsidiaries
Consolidated Statements of Cash Flows (Unaudited)

	Nine Months Ended September 30, 2008	2007
	(dollars in thousands)	
Cash flows from operating activities		
Net income	$ 1,890	$ 2,149
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	486	471
Net amortization of security premiums/discounts	(158)	(158)
Amortization of mortgage servicing rights	352	294
Provision for loan losses	786	(120)
Stock based compensation	20	34
Net realized loss on available sale securities	—	76
Income from mortgage loan sales	(1,004)	(678)
Proceeds from sales of loans held for sale	46,180	32,652
Origination of loans held for sale	(43,804)	(32,354)
(Gain) loss on sale of premises, equipment and other assets	5	(26)
Increase in cash surrender value of life insurance	(141)	(123)
Gain on sales of other assets	(11)	—
Release of ESOP shares	60	69
Net change in interest receivable	14	(335)
Net change in other assets	(1,583)	(612)
Net change in interest payable	(98)	(63)
Net change in other liabilities	451	401
Net cash provided by operating activities	3,445	1,677
Cash flows from investing activities		
Proceeds from sales, maturities and calls of securities available for sale	9,792	9,146
Purchase of securities available for sale	(3,920)	(15,542)
Net change in Federal Home Loan Bank stock	45	188
Net increase in loans	(19,994)	(21,399)
Proceeds from sales of premises, equipment and other assets	—	87
Purchase of premises and equipment	(2,037)	(586)
Proceeds from sales of foreclosed real estate	135	39
Net cash used in investing activities	(15,979)	(28,067)
Cash flows from financing activities		
Net increase in deposit accounts	19,954	7,950
Net increase (decrease) in short-term borrowed funds	(22,467)	12,665
Net increase (decrease) in long-term debt	15,062	(12,597)
Repurchase of common stock	(412)	(1,065)
Net proceeds from issuance of common stock	300	36
Tax benefit of stock options exercised	26	3
Net cash provided by financing activities	12,463	6,992
Decrease in cash and cash equivalents	(71)	(19,398)
Cash and cash equivalents, beginning of period	16,197	34,760
Cash and cash equivalents, end of period	$ 16,126	$ 15,362

See accompanying notes

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UWHARRIE CAPITAL CORP AND SUBSIDIARIES
Notes to Consolidated Financial Statements (Unaudited)

Note 1 - Basis of Presentation

The financial statements and accompanying notes are presented on a consolidated basis including Uwharrie Capital Corp (the "Company") and its subsidiaries, Bank of Stanly ("Stanly"), Anson Bank & Trust Co. ("Anson"), Cabarrus Bank & Trust Company ("Cabarrus"), Strategic Investment Advisors, Inc., ("SIA"), and Uwharrie Mortgage Inc. Stanly consolidates its subsidiaries, the Strategic Alliance Corporation, BOS Agency, Inc. and Gateway Mortgage, Inc., each of which is wholly-owned by Stanly.

The information contained in the consolidated financial statements is unaudited. In the opinion of management, the consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America and material adjustments necessary for a fair presentation of results of interim periods, all of which are of a normal recurring nature, have been made. The results of operations for the interim periods are not necessarily indicative of the results that may be expected for an entire year. Management is not aware of economic events, outside influences or changes in concentrations of business that would require additional clarification or disclosure in the consolidated financial statements.

The organization and business of the Company, accounting policies followed by the Company and other information are contained in the notes to consolidated financial statements filed as part of the Company's 2007 Annual Report on Form 10-K. This Quarterly report should be read in conjunction with such Annual Report.

Note 2 – Comprehensive Income

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available for sale securities, are reported as a separate component of the equity section of the balance sheet, such items, along with net income, are components of comprehensive income.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
	(in thousands)			
Net Income	$ 343	$ 774	$ 1,890	$2,149
Other comprehensive gain (loss)				
Unrealized gain (losses) on available for sale securities	(1,087)	397	(2,283)	126
Related tax effect	418	(153)	877	(48)
Reclassification of loss recognized in net income	—	—	—	76
Related tax effect	—	—	—	(29)
Total other comprehensive income (loss)	(669)	244	(1,406)	125
Comprehensive income (loss)	$ (326)	$ 1,018	$ 484	$2,274

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Note 3 – Per Share Data

On November 3, 2008, the Company's Board of Directors declared a 3% stock dividend payable on December 4, 2008 to shareholders of record on November 17, 2008. All information presented in the accompanying interim consolidated financial statements regarding earnings per share and weighted average number of shares outstanding has been computed giving effect to this stock dividend.

Basic and diluted net income per common share is computed based on the weighted average number of shares outstanding during each period after retroactively adjusting for stock dividends. Diluted net income per common share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the net income of the Company. On September 30, 2008 the Company had 89,798 shares that were anti-dilutive and were excluded from the diluted net income per common share computation.

Basic and diluted net income per common share have been computed based upon net income as presented in the accompanying consolidated statements of operations divided by the weighted average number of common shares outstanding or assumed to be outstanding. The computation of basic and dilutive earnings per share is summarized below:

	Three Months Ended September, 30		Nine Months Ended September 30,	
	2008	2007	2008	2007
Weighted average number of common shares outstanding	7,630,292	7,717,047	7,615,995	7,781,791
Effect of ESOP shares	(134,389)	(150,679)	(134,389)	(150,679)
Adjusted weighted average number of common shares used in computing basic net income per common share	7,495,903	7,566,368	7,481,606	7,631,112
Effect of dilutive stock options	45,917	137,304	43,723	112,569
Weighted average number of common shares and dilutive potential common shares used in computing diluted net income per common share	7,541,820	7,703,672	7,525,329	7,743,681

Note 4 – Investment Securities

Securities available for sale are summarized below:

	September 30, 2008	December 31, 2007
	(dollars in thousands)	
Amortized cost	$ 44,663	$ 50,378
Gross unrealized losses	(2,045)	(92)
Gross unrealized gains	391	719
Fair value	$ 43,009	$ 51,005

Management has evaluated these securities to determine whether they should be considered other-than-temporarily impaired at September 30, 2008. This evaluation considered, among other things, the extent and duration of the impairment, current and expected future yields, the

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Company's ability to continue to hold these securities in its portfolio and the issuers' credit ratings. The majority of the gross unrealized losses are related mortgage-backed securities portfolio. Further evaluations were made on these investments including analyzing prepayment rates, general market data, delinquency rates on the underlying mortgage loans and current and anticipated losses in foreclosure.

Based on these evaluations, the Company does not consider these investments to be other-than-temporarily impaired at September 30, 2008. Management expects to collect all contractual interest and principal payments and that recovery of these temporarily impaired securities will occur within a reasonable time frame. Management will continue to evaluate these securities on an ongoing basis, and if it is subsequently determined that an other than temporary impairment has occurred, the Company will record any such impairment as a charge to earnings.

Note 5 – Loans

	September 30, 2008	December 31, 2007
	(in thousands)	
Loans outstanding at period end:		
Commercial	$ 46,278	$ 37,724
Real estate-construction	51,971	46,546
Real estate-residential	137,253	135,959
Real estate-commercial	90,472	86,593
Consumer loans	15,697	15,022
All other loans	159	143
Total	$ 341,830	$ 321,987

	Three Months Ended September 30, 2008	Three Months Ended September 30, 2007	Nine Months Ended September 30, 2008	Nine Months Ended September 30, 2007
	(in thousands)			
Analysis of the allowance for loan losses				
Balance at beginning of period	$ 3,657	$ 3,337	$ 3,510	$ 3,171
Provision charged (credited) to operations	529	18	786	(120)
Charge-offs	(63)	(31)	(230)	(194)
Recoveries	20	70	77	537
Net recoveries(charge-offs)	(43)	39	(153)	343
Balance at end of period	$ 4,143	$ 3,394	$ 4,143	$ 3,394

Note 6 - Commitments and Contingencies

The subsidiary banks are party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of their customers. These financial instruments include commitments to extend credit, lines of credit and standby letters of credit. These instruments involve elements of credit risk in excess of amounts recognized in the accompanying financial statements.

The banks' risk of loss with the unfunded loans and lines of credit or standby letters of credit is represented by the contractual amount of these instruments. The banks use the same credit policies in making commitments under such instruments as they do for on-balance sheet instruments. The amount of collateral obtained, if any, is based on management's credit evaluation of the borrower. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Credit card commitments are unsecured. At September 30, 2008, outstanding financial instruments whose contract amounts represent credit risk were approximately:

(in thousands)	
Commitments to extend credit	$72,878
Credit card commitments	10,527
Standby letters of credit	871
Total commitments	$84,276

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Note 7 – Fair Value Disclosures

The Company adopted the provisions of Statement of Financial Accounting Statements (SFAS) No. 157 *Fair Value Measurements* (SFAS 157) and SFAS No. 159, *The Fair Value Option for Financial Assets and Liabilities* (SFAS 159) on January 1, 2008.

SFAS 157 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. SFAS 157 does not require any new fair value measurements, but clarifies and standardizes some divergent practices that have emerged since prior guidance was issued. SFAS 157 creates a three-level hierarchy under which individual fair value estimates are to be ranked based on the relative reliability of the inputs used in the valuation.

SFAS 157 defines fair value as the price that would be received to sell an asset or transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities, the Company considers the principal or most advantageous market in which those assets or liabilities are sold and considers assumptions that market participants would use when pricing those assets or liabilities. Fair values determined using Level 1 inputs rely on active and observable markets to price identical assets or liabilities. In situations where identical assets and liabilities are not traded in active markets, fair values may be determined based on Level 2 inputs, which exist when observable data exists for similar assets and liabilities. Fair values for assets and liabilities for which identical or similar assets and liabilities are not actively traded in observable markets are based on Level 3 inputs, which are considered to be unobservable.

Among the Company's assets and liabilities, investment securities available for sale are reported at their fair values on a recurring basis. Certain other assets are adjusted to their fair value on a nonrecurring basis, including loans held for sale, which are carried at the lower of cost or market, loan servicing rights, where fair value is determined using similar assets with similar characteristics, when available, or based upon discounted cash flows using market-based assumptions, foreclosed real estate, which is carried at lower of cost or fair market value and goodwill, which is periodically tested for impairment. Deposits, short-term borrowings and long-term obligations are not reported at fair value.

The Company does not record loans at fair value on a recurring basis. However, from time to time, a loan is considered impaired and an allowance for loan losses is established. Loans for which it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement are considered impaired. Once a loan is identified as individually impaired, management measures impairment in accordance with SFAS 114, *Accounting by Creditors for Impairment of a Loan,* (SFAS 114). The fair value of impaired loans is estimated using one of several methods, including collateral value, market value of similar debt, enterprise value, liquidation value and discounted cash flows. Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceed the recorded investments in such loans. At September 30, 2008, substantially all of the total impaired loans were evaluated based on the fair value of the collateral. In accordance with SFAS 157, impaired loans where an allowance is established based on the fair

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value of collateral require classification in the fair value hierarchy. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company records the impaired loan as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company records the impaired loan as nonrecurring Level 3.

For assets and liabilities carried at fair value, the following table provides fair value information as of September 30, 2008:

	Total	Level 1	Level 2	Level 3
	(dollars in thousands)			
Investment securities available for sale	$43,009	$5,543	$37,466	$ —
Total assets at fair value	$43,009	$5,543	$37,466	$ —
Total liabilities at fair value	$ —	$ —	$ —	$ —

Prices for US Treasury and government agency securities are readily available in the active markets in which those securities are traded, and the resulting fair values are shown in the ‘Level 1 input’ column. Prices for mortgage-backed securities and for state, county and municipal securities are obtained for similar securities, and the resulting fair values are shown in the ‘Level 2 input’ column. Prices for all other non-marketable investments are determined based on various assumptions that are not observable. The fair values for these investment securities are shown in the ‘Level 3 input’ column. Non-marketable investment securities, which are carried at their purchase price, include those that may only be redeemed by the issuer.

The Company may be required, from time to time, to measure certain assets at fair value on a nonrecurring basis in accordance with U.S. generally accepted accounting principles. These include assets that are measured at the lower of cost or market that were recognized at fair value below cost at the end of the period. Assets measured at fair value on a nonrecurring basis are included in the table below as of September 30, 2008:

	Total	Level 1	Level 2	Level 3
	(dollars in thousands)			
Loans	$10,834	$ —	$10,834	$ —
Other real estate owned	752	—	752	—
Total assets at fair value	$11,586	$ —	$11,586	$ —
Total liabilities at fair value	$ —	$ —	$ —	$ —

SFAS 159 allows an entity to elect to measure certain financial assets and liabilities at fair value with changes in fair value recognized in the income statement each period. The statement also requires additional disclosures to identify the effects of an entity’s fair value election on its earnings. Upon the adoption of SFAS 159, the Company did not elect to report any assets and liabilities at fair value.

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Note 8 – Recent Accounting Pronouncements

SAB 109

Staff Accounting Bulletin No. 109 (“SAB 109”), *Written Loan Commitments Recorded at Fair Value Through Earnings* supersedes Staff Accounting Bulletin No. 105 by requiring the expected net future cash flows related to servicing a loan to be included in the measurement of all written loan commitments that are accounted for at fair value through earnings. The adoption of SAB 109 on January 1, 2008, did not have a significant impact on the Company’s consolidated financial statements.

SFAS 157

Statement of Financial Accounting Standards No. 157 (“SFAS 157”), *Fair Value Measurements*, defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. The Company adopted the provisions of SFAS 157 on January 1, 2008 as discussed in Note 7 above.

SFAS 159

Statement of Financial Accounting Standards No. 159 (“SFAS 159”), *The Fair Value Option for Financial Assets and Financial Liabilities*, permits entities to choose to measure many financial instruments and certain other items at fair value. The objective of this standard is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This statement is effective for fiscal years beginning after November 15, 2007, with early adoption permitted under certain circumstances. The adoption of SFAS 159 did not have any impact on the Company’s consolidated financial statements. See Note 7 above.

SFAS 161

In March of 2008, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 161, *“Disclosures about Derivative Instruments and Hedging Activities—an amendment of FASB Statement No. 133” (“SFAS 161”).* SFAS 161 amends and expands the disclosure requirement of Statement No. 133 for derivative instruments and hedging activities to provide users of financial statements with an enhanced understanding of the derivative instrument’s purpose, how it is accounted for, and its impact on the financial statements. This statement is effective for fiscal years beginning after November 15, 2008, with early adoption encouraged. The Company has chosen not to early adopt the provisions of SFAS 161. The Company has evaluated this statement and does not believe it will have a material effect on the Company’s consolidated financial statements.

EITF 06-4

The Emerging Issues Task Force (EITF) reached a consensus at its September 2006 meeting regarding EITF 06-4, *Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements*. The scope of EITF 06-4 is limited to the recognition of a liability and related compensation costs for endorsement split-dollar life insurance policies that provide a benefit to an employee that extends to postretirement periods. Therefore, this EITF would not apply to a split-dollar life insurance arrangement that provides a specified benefit to an employee that is limited to the employee’s active service period with an employer. This EITF 06-4 is effective for fiscal years beginning after December 15, 2007, with earlier application permitted. The Company adopted EITF 06-4 on January 1, 2008 and it had the effect of reducing beginning consolidated undivided profits by approximately $273,000.

From time to time, the FASB issues exposure drafts of proposed statements of financial accounting standards. Such exposure drafts are subject to comment from the public, to revisions by the FASB and to final issuance by the FASB as statements of financial accounting

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standards. Management considers the effect of the proposed statements on the consolidated financial statements of the Company and monitors the status of changes to and proposed effective dates of exposure drafts.

Reclassification

Certain amounts in the 2007 consolidated financial statements have been reclassified to conform to the 2008 presentation. The reclassifications had no effect on net income or shareholders' equity as previously reported.

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

This Quarterly Report on Form 10-Q may contain certain forward-looking statements consisting of estimates with respect to the financial condition, results of operations and business of the Company that are subject to various factors which could cause actual results to differ materially from these estimates. These factors include, but are not limited to, general economic conditions, changes in interest rates, deposit flows, loan demand, real estate values, and competition; changes in accounting principles, policies, or guidelines; changes in legislation or regulation; and other economic, competitive, governmental, regulatory, and technological factors affecting the Company's operations, pricing, products and services.

Comparison of Financial Condition at September 30, 2008 and December 31, 2007.

During the nine months ended September 30, 2008, the Company's total assets increased $13.4 million, from $411.9 million to $425.3 million. During the nine months, loans held for investment increased $19.8 million or 6.2%, from $322.0 million at December 31, 2007 to $341.8 million at September 30, 2008. This increase, however, was offset by a decline in investment securities of $8.0 million and a decrease in loans held for sale of $1.8 million during the period.

Cash and cash equivalents decreased $71 thousand during the nine months ended September 30, 2008. Cash and due from banks declined $447 thousand, while interest-earning deposits with banks increased $376 thousand.

Investment securities decreased $8.0 million or 15.7% for the nine months. Market values have declined $2.3 million due to the recent downturn in the investment markets. Management believes this decline in investment market values is only temporary and does not expect to incur a loss at this time. The Company had $4.7 million in securities that matured during the period and $3.9 million in new securities purchased. The Company did have an $8 thousand investment in 400 shares of FNMA stock that were written off at the end of the period. The remainder of the decrease resulted primarily from normal mortgage backed securities pay down activity during the period.

As previously stated, loans held for investment increased $19.8 million to $341.8 million during the period ended September 30, 2008. The Company has experienced positive growth trends in all areas of its loan portfolio. The commercial and residential construction areas of the loan portfolio lead the way with growth of 22.7% and 11.7%, respectively. Loans held for sale decreased 63.2% or $1.8 million during the period. The allowance for loan losses was $4.1 million at September 30, 2008 which represents 1.21% of the loan portfolio.

Other changes in our consolidated assets related to premises and equipment, interest receivable, Federal Home Loan Bank stock, bank owned life insurance, other real estate owned and other assets. The Company has been renovating an office building to gain some much needed office space. These renovations were the leading factor in the increase of $1.5 million in fixed assets. Interest receivable declined $14 thousand, bank owned life insurance increased $141 thousand and other real estate owned increased $589 thousand. Other assets increased $1.9 million, resulting primarily from increases in the income tax benefit of $309 thousand and deferred income taxes of $877 thousand. Federal Home Loan Bank stock decreased $45 thousand. Federal Home Loan Bank stock ownership is a requirement for member banks that utilize Federal Home Loan Bank for borrowing funds. The amount of stock owned by each member bank is based primarily on the amount of borrowings outstanding.

Customer deposits, our primary funding source, experienced a $19.9 million increase during the nine months ended September 30, 2008, increasing from $324.7 million to $344.6 million.

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Interest checking and money market accounts increased $12.8 million, while demand noninterest-bearing grew $1.8 million. Time deposits over $100,000 and other deposits experienced positive growth of $2.7 million and $3.0 million, respectively. These increases were offset by a decline in savings deposits of $314 thousand.

Total borrowings decreased $7.4 million for the period. Borrowings consist of both short-term and long-term borrowed funds. The Company utilizes both short-term and long-term advances from the Federal Home Loan Bank. At September 30, 2008, $28.0 million of the total borrowings of $46.2 million were comprised of Federal Home Loan Bank advances. The Company has also been conducting a private placement of junior subordinated debt during the period ending September 30, 2008. At the end of the period, the Company had placed $7.1 million.

Other liabilities increased from $1.5 million at December 31, 2007 to $2.2 million at September 30, 2008, an increase of $724 thousand. The Company has a supplemental retirement plan in place for four executive officers. The Company has purchased life insurance policies in order to provide future funding of benefit payments. As discussed in Note 8, with the adoption of EITF 06-4, *Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements*, the Company recorded a $273 thousand liability. This adjustment coupled with an increase in the reserve for income taxes were the primary factors associated with the increase in other liabilities.

At September 30, 2008, total shareholders' equity was $31.8 million, an increase of $205 thousand from December 31, 2007. Net income for the period was $1.9 million and the Company received $300 thousand from the exercise of stock options. These increases were offset by the repurchase of 76,598 shares of the Company's common stock at a cost of $412 thousand and unrealized losses on investment securities, net of tax, of $1.4 million. The Company also recorded a $273 thousand one-time cumulative adjustment to undivided profits for the adoption of EITF 06-4. At September 30, 2008, the Company and its subsidiary banks exceeded all applicable regulatory capital requirements.

Comparison of Results of Operations For the Three Months Ended September 30, 2008 and 2007.

Net Income

Uwharrie Capital Corp reported net income of $343 thousand, or $0.05 per basic share, for the three months ended September 30, 2008, as compared to $774 thousand, or $0.10 per basic share, for the three months ended September 30, 2007, a decrease of $431 thousand, or $0.05 per share.

Net Interest Income

The Company's primary source of income, net interest income, increased $38 thousand or 1.0% for the three months ended September 30, 2008, as compared to the same period for 2007. Refer to the nine month discussion on page 18 for further information.

Provision and Allowance for Loan Losses

The provision for loan losses was $529 thousand for the three months ending September 30, 2008 compared to $18 thousand for the same period in 2007. There were net loan charge-offs of $43 thousand for the three months ended September 30, 2008 as compared with net loan recoveries of $39 thousand during the same period of 2007. Refer to the Asset Quality discussion on page 19 for further information.

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Noninterest Income

The Company generates most of its revenue from net interest income; however, like all financial institutions, diversification of our earnings base is of major importance in our long term success. Total noninterest income decreased $10 thousand for the three month period ending September 30, 2008 as compared to the same period in 2007. Service charges on deposit accounts produced earnings of $599 thousand for the three months ended September 30, 2008. Other service fees and commissions experienced a 1.7% decrease for the comparable three month period. Growth in ATM fees of $24 thousand was offset by a decrease in investment fees of $28 thousand. Income from mortgage loan sales decreased $29 thousand from $235 thousand for the quarter ended September 30, 2007 to $206 thousand for the same period in 2008. The slow down in the economy and the current problems in the mortgage industry attributed to the decrease in mortgage loan sales.

Noninterest Expense

Noninterest expense for the quarter ended September 30, 2008 was $4.5 million compared to $4.4 million for the same period of 2007, an increase of $128 thousand. Salaries and employee benefits, the largest component of noninterest expense, increased $127 thousand, from $2.5 million for the quarter ending September 30, 2007 to $2.6 million for the same period in 2008. The Company has a non-qualifying deferred compensation plan for certain executive officers. The costs associated with this plan increased $106 thousand for the comparable periods. This increase coupled with normal salary increases contributed to the overall increase in noninterest expense. Net occupancy expense and equipment expense had a combined increase of $59 thousand related to the aforementioned renovations to a new office building. Other noninterest expense decreased $64 thousand for the comparable three month periods. The table below reflects the composition of other noninterest expense.

Other noninterest expense

	Three Months Ended September 30,	
	2008	2007
	(in thousands)	
Professional fees and services	$ 179	$ 212
Marketing and donations	146	136
Office supplies and printing	62	60
Telephone and data lines	57	58
Electronic banking expense	220	182
Software amortization and maintenance	104	96
Loan collection expense	46	36
Shareholder relations expense	43	50
Dues and subscriptions	32	30
Postage	45	44
Subordinated debt issue cost	7	127
Other	359	333
Total	$ 1,300	$ 1,364

Income Tax Expense

The Company had income tax expense of $156 thousand for the three months ended September 30, 2008 resulting in an effective tax rate of 31.3% compared to income tax expense of $336 thousand and an effective rate of 30.3% in the 2007 period. Income taxes computed at the statutory rate are reduced primarily by the eligible amount of interest earned on state and municipal securities, tax free municipal loans and income earned on bank owned

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life insurance. The increase in the effective tax rate resulted primarily from the decrease in the level of such tax free income as a percentage of income before income taxes in the current year quarter compared to the 2007 quarter.

Comparison of Results of Operations For the Nine Months Ended September 30, 2008 and 2007.

Net Income

Uwharrie Capital Corp reported net income of $1.9 million or $0.25 per basic share, for the nine months ended September 30, 2008, as compared to $2.1 million, or $0.29 per basic share, for the nine months ended September 30, 2007, a decrease of $259 thousand, or $0.04 per share.

Net Interest Income

As with most financial institutions, the primary component of earnings for our banks is net interest income. Net interest income is the difference between interest income, principally from loan and investment securities portfolios, and interest expense, principally on customer deposits and borrowings. Changes in net interest income result from changes in volume, spread and margin. For this purpose, volume refers to the average dollar level of interest-earning assets and interest-bearing liabilities, spread refers to the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities, and margin refers to net interest income divided by average interest-earning assets. Margin is influenced by the level and relative mix of interest-earning assets and interest-bearing liabilities, as well as by levels of noninterest-bearing liabilities and capital.

Net interest income for the nine months ended September 30, 2008 was $11.8 million as compared with $11.0 million during the nine months ended September 30, 2007, resulting in an increase of $722 thousand, or 6.5%. During the nine months ended September 30, 2008 our growth in the volume of interest-earning assets outpaced the growth in interest-bearing liabilities by $897 thousand. The average yield on our interest–earning assets decreased 72 basis points to 6.77%, while the average rate we paid for our interest-bearing liabilities decreased 85 basis points. The Company’s assets that are interest rate sensitive adjust at the time the Federal Reserve Open Market Committee adjusts interest rates, while, interest-bearing time deposits adjust at the time of maturity. The fore mentioned decreases resulted in an increase of 13 basis points in our interest rate spread, from 3.64% in 2007 to 3.77% in 2008. Our net interest margin was 4.17% and 4.19% for the comparable periods in 2008 and 2007.

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The following table presents average balance sheets and a net interest income analysis for the nine months ended September 30, 2008 and 2007:

Average Balance Sheet and Net Interest Income Analysis
For the Nine Months Ended September 30,

(in thousands)

	Average Balance		Income/Expenses		Rate/Yield	
	2008	2007	2008	2007	2008	2007
Interest-earning assets:						
Taxable securities	$ 36,763	$ 29,044	$ 1,493	$ 1,165	5.42%	5.36%
Nontaxable securities (1)	14,298	12,932	504	469	7.66%	7.88%
Short-term investments	3,801	18,789	59	711	2.07%	5.06%
Taxable loans	330,286	299,894	17,201	17,550	6.96%	7.82%
Non-taxable loans (1)	3,909	3,955	89	143	7.45%	7.87%
Total interest-earning assets	389,057	364,614	19,346	20,038	6.77%	7.49%
Interest-bearing liabilities:						
Interest-bearing deposits	286,882	263,537	6,159	7,179	2.87%	3.64%
Short-term borrowed funds	17,589	27,075	407	843	3.09%	4.16%
Long-term debt	33,117	21,671	1,014	972	4.09%	6.00%
Total interest bearing liabilities	337,588	312,283	7,580	8,994	3.00%	3.85%
Net interest spread	$ 51,469	$ 52,331	$11,766	$11,044	3.77%	3.64%
Net interest margin (1) (% of earning assets)					4.17%	4.19%

(1) Yields related to securities and loans exempt from income taxes are stated on a fully tax-equivalent basis, assuming a 38.55% tax rate.

Provision and Allowance for Loan Losses

The provision for loan losses was $786 thousand for the nine months ending September 30, 2008 compared to ($120) thousand for the same period in 2007. There were net loan charge-offs of $153 thousand for the nine months ended September 2008 as compared with net loan recoveries of $343 thousand during the same period of 2007. Refer to the Asset Quality discussion on page 19 for further information.

Noninterest Income

The Company generates most of its revenue from net interest income; however, like all financial institutions, diversification of our earnings base is of major importance in our long term success. Total noninterest income increased $716 thousand, from $4.7 million for the nine months ended September 30, 2007 to $5.4 million for the same period in 2008. Service charges on deposit accounts produced earnings of $1.7 million for the nine months ended September 30, 2008. Other service fees and commissions experienced a 3.2% increase for the comparable nine month period. Growth in both ATM fees and investment fees on managed accounts of $85 thousand enhanced this increase. Income from mortgage loan sales increased $326 thousand from $678 thousand for the nine months ended September 30, 2007 to $1.0 million for the same period in 2008. The interest rate reductions during the period attributed to the increase in mortgage loan sales. The Company owns shares of VISA stock and MasterCard stock. VISA redeemed a portion of this stock during the first quarter of 2008 resulting in other income of $59 thousand. We sold all of the shares of MasterCard during second quarter of 2008 producing other income of $162 thousand. This income was the primary reason for the increase in other income for the comparable periods.

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Noninterest Expense

Noninterest expense for the nine months ended September 30, 2008 was $13.6 million compared to $12.8 million for the same period of 2007, an increase of $827 thousand. Salaries and employee benefits, the largest component of noninterest expense, increased $507 thousand, from $7.4 million for the nine months ended September 30, 2007 to $7.9 million for the same period in 2008. The Company has a non-qualifying deferred compensation plan for certain executive officers. The costs associated with this plan increased $272 thousand for the comparable periods. This increase coupled with normal salary increases contributed to the overall increase in noninterest expense. Other noninterest expense increased $203 thousand for the comparable nine month periods. The table below reflects the composition of other noninterest expense.

Other noninterest expense

	Nine Months Ended September 30,	
	2008	2007
	(in thousands)	
Professional fees and services	$ 517	$ 588
Marketing and donations	463	413
Office supplies and printing	197	200
Telephone and data lines	179	174
Electronic banking expense	606	511
Software amortization and maintenance	327	318
Loan collection expense	173	104
Shareholder relations expense	144	150
Dues and subscriptions	109	100
Postage	141	123
Subordinated debt issue cost	132	130
Other	919	893
Total	$3,907	$3,704

Income Tax Expense

The Company had income tax expense of $903 thousand for the nine months ended September 30, 2008 resulting in an effective tax rate of 32.3% compared to income tax expense of $939 thousand and an effective rate of 30.4% in the 2007 period. Income taxes computed at the statutory rate are reduced primarily by the eligible amount of interest earned on state and municipal securities, tax free municipal loans and income earned on bank owned life insurance. The increase in the effective tax rate resulted primarily from the decrease in the level of such tax free income as a percentage income before income taxes in the current year period compared to the 2007 period.

Asset Quality

The Company’s allowance for loan losses is established through charges to earnings in the form of a provision for loan losses. The allowance is increased by provisions charged to operations and by recoveries of amounts previously charged off, and reduced by loans charged off. Management evaluates the adequacy of the allowance at least quarterly. In evaluating the adequacy of the allowance, management considers the growth, composition and industry diversification of the portfolio; historical loan loss experience; current delinquency levels; adverse situations that may affect a borrower’s ability to repay; estimated value of any underlying collateral; prevailing economic conditions and other relevant factors. The Company’s credit administration function, through a review process, validates the accuracy of the initial risk

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grade assessment. In addition, as a given loan's credit quality improves or deteriorates, the credit administration department has the responsibility to change the borrower's risk grade accordingly. For loans determined to be impaired, the allowance is based either on discounted cash flows using the loan's initial effective interest rate or on the fair value of the collateral for certain collateral dependent loans. This evaluation is inherently subjective, as it requires material estimates, including the amounts and timing of future cash flows expected to be received on impaired loans, which may be susceptible to significant change. In addition, regulatory agencies, as an integral part of their examination process, periodically review the allowance for loan losses and may require additions for estimated losses based upon judgments different from those of management.

Management uses the risk-grading program to facilitate the evaluation of probable inherent loan losses and the adequacy of the allowance for loan losses. In this program, risk grades are initially assigned by loan officers and reviewed and monitored by credit administration. The Company strives to maintain its loan portfolio in accordance with conservative loan underwriting policies that result in loans specifically tailored to the needs of its market area. Every effort is made to identify and minimize the credit risks associated with such lending strategies. The Company has no foreign loans and does not engage in significant lease financing or highly leveraged transactions. The Company follows a loan review program designed to evaluate the credit risk in the loan portfolio. This process includes the maintenance of an internally classified watch list that helps management assess the overall quality of the loan portfolio and the adequacy of the allowance for loan losses. In establishing the appropriate classification for specific assets, management considers, among other factors, the estimated value of the underlying collateral, the borrower's ability to repay, the borrower's payment history and the current delinquent status. As a result of this process, certain loans are categorized as substandard, doubtful or loss and reserves are allocated based on management's judgment and historical experience.

The allowance for loan losses represents management's estimate of an appropriate amount to provide for known and inherent losses in the loan portfolio in the normal course of business. While management believes that it uses the best information available to establish the allowance for loan losses, future adjustments to the allowance may be necessary and results of operations could be adversely affected if circumstances differ substantially from the assumptions used in making the determinations. Furthermore, while management believes it has established the allowance for loan losses in conformity with generally accepted accounting principles, there can be no assurance that regulators, in reviewing the Company's portfolio, will not require an adjustment to the allowance for loan losses. In addition, because future events affecting borrowers and collateral cannot be predicted with certainty, there can be no assurance that the existing allowance for loan losses is adequate or that increases will not be necessary, should the quality of any loans deteriorate as a result of the factors discussed herein. Any material increase in the allowance for loan losses may adversely affect the Company's financial condition and results of operations.

The provision for loan losses was $786 thousand for the nine months ended September 30, 2008 as compared to ($120) thousand for the same period in 2007. Additionally, the allowance expressed as a percentage of loans held for investment was 1.21% at September 30, 2008 compared to 1.09% December 31, 2007. During the first nine months of 2008 the levels of our impaired loans, which includes all loans in nonaccrual status and other loans deemed by management to be impaired, were $14.0 million compared to $7.5 million at December 31, 2007, an increase of $6.5 million. Of the $14.0 million in impaired loans at September 30, 2008, $10.8 million carried an allowance of $2.0 million while $3.2 million were evaluated and required no specific allowance. The level of specific reserves identified for impaired loans increased by $772 thousand for the same period. These increases were due primarily to the impairment of loan relationships with two customers of $5.1 million, for which a $646 thousand specific reserve has been provided. Net loan recoveries for the nine months ending September 30, 2007 were $343 thousand, while the same period in 2008 experienced net loan charge-offs of $152 thousand.

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The allowance as a percentage of total impaired loans has increased from 35.7% at December 31, 2007 to 48.9% at September 30, 2008. The portion of the allowance specifically allocable to impaired loans decreased from 16.8% at December 31, 2007 to 14.4% at September 30, 2008. Management believes the current level of allowance for loan losses to be appropriate given the risk inherence in the loan portfolio at this time.

The following nonperforming loan table shows the comparison for the nine months ended September 30, 2008 to December 31, 2007:

Nonperforming Assets
(dollars in thousands)

	September 30, 2008	December 31, 2007
Nonperforming assets:		
Nonaccrual loans	$ 5,828	$ 1,795
Other real estate owned	752	163
Total nonperforming assets	$ 6,580	$ 1,958
Accruing loans past due 90 days or more	$ 10	$ —
Allowance for loans losses	4,143	3,510
Nonperforming loans to total loans	1.70%	0.56%
Allowance for loan losses to total loans	1.21%	1.09%
Nonperforming assets to total loans and other real estate	1.92%	0.61%
Nonperforming assets to total assets	1.55%	0.48%
Allowance for loan losses to Nonperforming loans	71.10%	195.57%

Liquidity and Capital Resources

The objective of the Company's liquidity management policy is to ensure the availability of sufficient cash flows to meet all financial commitments and to capitalize on any opportunities for expansion. Liquidity management addresses the ability to meet deposit withdrawals on demand or at contractual maturity, to repay borrowings as they mature and to fund new loans and investments as opportunities arise.

The Company's primary sources of internally generated funds are principal and interest payments on loans, cash flows generated from operations and cash flow generated by investments. Growth in deposits is typically the primary source of funds for loan growth. The Company and its subsidiary banks have multiple funding sources in addition to deposits that can be used to increase liquidity and provide additional financial flexibility. These sources are the subsidiary banks' established federal funds lines with correspondent banks aggregating $20.9 million at September 30, 2008, with available credit of $20.9 million, established borrowing relationships with the Federal Home Loan Bank, with available credit of $29.1 million, access to borrowings from the Federal Reserve Bank discount window, and the sale of securities under agreements to repurchase. In addition, the Company issues commercial paper and has secured long-term debt from other sources. Total debt from these sources aggregated $46.2 million at September 30, 2008, compared to $53.6 million at December 31, 2007.

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Banks and bank holding companies, as regulated institutions, must meet required levels of capital. The FDIC and the Federal Reserve, the primary federal regulators of the Company and its subsidiary banks, have adopted minimum capital regulations or guidelines that categorize components and the level of risk associated with various types of assets.

Regulatory guidelines require a minimum of total capital to risk-adjusted assets ratio of 8 percent and a Tier I leverage ratio of 4 percent. Banks, which meet or exceed a Tier I ratio of 6 percent, a total capital ratio of 10 percent and a Tier I leverage ratio of 5 percent are considered “well capitalized” by regulatory standards. Financial institutions are expected to maintain a level of capital commensurate with the risk profile assigned to their assets in accordance with those guidelines.

Both the Company and its subsidiary banks have maintained capital levels exceeding minimum levels for “well capitalized” banks and bank holding companies. The Company expects to continue to exceed these minimums without altering current operations or strategy. The Company began a private placement of subordinated debt during the second quarter of 2008 that will qualify as regulatory capital. At September 30, 2008, the Company had $7.1 million in subordinated debt. The placement will continue into the fourth quarter

Accounting and Regulatory Matters

Management is not aware of any known trends, events, uncertainties or current recommendations by regulatory authorities that will have or that are reasonably likely to have a material effect on the Company’s liquidity, capital resources, or other operations.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

The Company’s primary market risk is interest rate risk. Interest rate risk is the result of differing maturities or repricing intervals of interest-earning assets and interest-bearing liabilities and the fact that rates on these financial instruments do not change uniformly. These conditions may impact the earnings generated by the Company’s interest earning assets or the cost of its interest-bearing liabilities, thus directly impacting the Company’s overall earnings. The Company’s management actively monitors and manages interest rate risk. One way this is accomplished is through the development of and adherence to the Company’s asset/liability policy. This policy sets forth management’s strategy for matching the risk characteristics of the Company’s interest-earning assets and liabilities so as to mitigate the effect of changes in the rate environment. The Company’s market risk profile has not changed significantly since December 31, 2007.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

At the end of the period covered by this report, the Company carried out an evaluation, under the supervision and with the participation of the Company’s management, including the Company’s principal executive officer and principal financial officer, of the effectiveness of the design and operation of the Company’s disclosure controls and procedures pursuant to Securities Exchange Act Rule 13a-15.

Based upon that evaluation, the principal executive officer and principal financial officer concluded that the Company’s disclosure controls and procedures were effective (1) to provide reasonable assurance that information required to be disclosed by the Company in the reports

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filed or submitted by it under the Securities Exchange Act was recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and (2) to provide reasonable assurance that information required to be disclosed by the Company in such reports is accumulated and communicated to the Company's management, including its principal executive officer and principal financial officer, as appropriate to allow for timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

Management of the Company has evaluated, with the participation of the Company's principal executive officer and principal financial officer, changes in the Company's internal controls over financial reporting (as defined in Rule 13a -15(f) and 15d – 15(f) of the Exchange Act) during the third quarter of 2008. In connection with such evaluation, the Company has determined that there were no changes in the Company's internal control over financial reporting during the period covered by this report that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting. The Company reviews its disclosure controls and procedures, which may include its internal control over financial reporting, on an ongoing basis, and may from time to time make changes aimed at enhancing their effectiveness and to ensure that the Company's systems evolve with its business.

Part II. OTHER INFORMATION

Item 1. Legal Proceedings

Neither the Company nor its subsidiaries, nor any of their properties are subject to any legal proceedings other than ordinary routine litigation incidental to their business.

Item 1A. Risk Factors

Not applicable.

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

Trades of the Company's stock occur in the Over-the-Counter marketplace from time to time. The Company also has in place a Stock Repurchase Plan that provides liquidity to its shareholders in the event a willing buyer is not available to purchase shares that are offered for sale. The Company is under no obligation to purchase shares offered; however, it will accommodate such offers as its Stock Repurchase Plan allows. This plan was initially adopted in 1995 and is approved annually by resolution of the Board of Directors or the Executive Committee of the Board.

On April 15, 2008, the Executive Committee of Uwharrie Capital Corp mandated by resolution that the Company could repurchase 48,865 shares of its common stock at a cost of $261,428.

On June 30, 2008, the Executive Committee of Uwharrie Capital Corp mandated by resolution that the Company could repurchase 5,427 shares of its common stock at a cost of $29,431.

The Company did not repurchase any shares during the third quarter ending September 30, 2008.

Item 3. Defaults Upon Senior Securities

None

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

None

Item 5. Other Information

None

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Item 6. Exhibits

Exhibit Number	Description of Exhibit
3.1	Registrant's Articles of Incorporation *
3.2	Registrant's By-laws *
4	Form of stock certificate *
10.1	Incentive Stock Option Plan, as amended *
10.2	Employee Stock Ownership Plan and Trust **
10.3	2006 Incentive Stock Option Plan ***
10.4	2006 Employee Stock Purchase Plan ***
10.5	Amendment to the Employee Stock Ownership Plan and Trust ****
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes- Oxley Act of 2002 (filed herewith)
31.2	Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes- Oxley Act of 2002 (filed herewith)
32	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith)

* Incorporated by reference from exhibits to Registrant's Registration Statement on Form S-4 (Reg. No. 33-58882).
** Incorporated by reference to Registrant's Annual Report on Form 10-KSB for the Fiscal year ended 1999.
*** Incorporated by reference to Registrant's Quarterly Report on Form 10-Q for the Quarter ended June 30, 2006.
**** Filed here within this report.

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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 who is thereunto duly authorized.

UWHARRIE CAPITAL CORP
(Registrant)

Date: November 7, 2008	By:	/s/ Roger L. Dick Roger L. Dick President and Chief Executive Officer
Date: November 7, 2008	By:	/s/ Robert O. Bratton Robert O. Bratton Principal Financial Officer

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