100656

QUARTERLY REPORT

SECOND Quarter

Corporate Highlights

To Our Shareholders:

I am pleased to announce that Southern Michigan Bancorp, Inc. earned $803,000, or $.35 per share, for the second quarter of 2010. The financial performance for the period represents the fifth consecutive profitable quarter for the company. For the first six months of 2010, Southern earned $1,505,000, or $.65 per share. Both the quarterly and six-month financial results are substantial increases compared with the same periods of 2009.

The improvements in Southern's financial performance are attributable to our efforts to reduce costs associated with problem loans and to control operating expenses. Southern's provision for loan losses for the second quarter of 2010 was $150,000, a sharp reduction from the $500,000 provision for the second quarter of 2009. Net charge-offs for this year's second quarter totaled $368,000 compared with $766,000 for the same period one year ago. For the first six months of this year, our net charge-offs totaled $699,000 compared with $2,430,000 for the first six months of last year.

Total non-interest expenses for the most recent quarter declined by $317,000 compared with the total for the second quarter of 2009. The reduction was due principally to the absence of a one-time special FDIC deposit insurance assessment imposed on all banks during the second quarter of 2009. Absent deposit insurance assessments, most key operating expense categories have remained relatively flat for the first six months of 2010 compared with a year ago.

Our balance sheet has modestly increased since the beginning of 2010, with total assets rising to $468.8 million through the first six months of this year from $462.4 million. Total deposits during this period of historically low interest rates increased to $385.7 million as of June 30, 2010 from $380.9 million at year-end 2009. Loans, through the comparable period, declined to $324.1 million from $333.1 million. As a result, net interest income for the six-month period ended June 30, 2010 declined minimally to $8.1 million from $8.2 million compared with the same period a year ago. Our net interest margin for the first six months of 2010 was a healthy 4.02 percent, although slightly lower from 4.11 percent for the first six months of 2009.

Southern's consistent levels of profitability and capital strength will position the company to take advantage of growth opportunities likely to emerge with an economic recovery. Our annualized return on average assets for the six-month period ended June 30, 2010 was 0.64 percent, compared with 0.21 percent for the same period last year. The annualized return on average equity was 6.48 percent for the first six months of 2010 compared with 2.13 percent for the same period in 2009. Equally important, our Total and Tier 1 risk-based capital ratios of 12.58 percent and 11.32 percent, respectively, remain comfortably above the regulatory minimums for financial institutions to be categorized as "well-capitalized".

I have discussed with many of you the unprecedented nature and impact of the economic downturn in Michigan, which is now into its third year. Recent passage of the Dodd-Frank Act represents the most sweeping change to the financial services industry in more than a generation. The Act will establish new oversight agencies and regulatory mandates that are likely to increase Southern's cost of doing business as well as its minimum capital requirements. It is impossible at this time to fully anticipate the impact and costs to Southern of a prolonged economic recession, additional regulatory burdens, and implementation of national health care legislation, among other factors that have created more uncertainty rather than clarity for community banks.

Southern's management team continues to implement strategic initiatives developed since the onset of the economic downturn that emphasize:

- Providing high quality financial services to many underserved market segments throughout our primary service area;
- Streamlining servicing capabilities at both the customer contact and back office areas in an effort to ensure that efficiency targets are attained;
- Promptly identifying and resolving potential problem credit relationships; and
- Building capital in an effort to withstand a prolonged economic slump and to seize strategic opportunities as they may present themselves.

Our management team, employees and directors appreciate your continued support.

Sincerely,

John H. Castle
Chairman and Chief Executive Officer

SOUTHERN MICHIGAN BANCORP, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

	June 30, 2010	December 31, 2009
	(Unaudited)	(A)
	(In thousands, except share and per share data)	
ASSETS		
Cash and due from banks	$ 42,423	$ 24,814
Federal funds sold	1,887	2,540
Securities available for sale	55,071	56,948
Loans held for sale	1,440	605
Loans, net of allowance for loan losses of $5,726 in 2010 (2009-$6,075)	318,390	327,004
Premises and equipment, net	12,885	12,914
Accrued interest receivable	1,890	2,054
Net cash surrender value of life insurance	9,766	9,881
Goodwill	13,422	13,422
Other intangible assets, net	2,180	2,355
Other assets	9,402	9,872
TOTAL ASSETS	$ 468,756	$ 462,409
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities		
Deposits:		
Non-interest bearing	$ 57,728	$ 55,250
Interest bearing	328,008	325,655
TOTAL DEPOSITS	385,736	380,905
Securities sold under agreements to repurchase and overnight borrowings	14,899	14,799
Accrued expenses and other liabilities	4,510	4,039
Other borrowings	10,491	10,832
Subordinated debentures	5,155	5,155
Common stock subject to repurchase obligation in Employee Stock Ownership Plan, shares outstanding - 105,431 in 2010 (101,999 shares in 2009)	1,292	945
TOTAL LIABILITIES	422,083	416,675
Shareholders' equity:		
Preferred stock, 100,000 shares authorized; none issued or outstanding	-	-
Common stock, $2.50 par value:		
Authorized—4,000,000 shares		
Issued—2,340,717 shares in 2010 (2,323,410 shares in 2009)		
Outstanding (other than ESOP shares) - 2,235,286 shares in 2010 (2,221,411 shares in 2009)	5,588	5,553
Additional paid-in capital	18,056	18,363
Retained earnings	23,333	22,062
Accumulated other comprehensive income, net	74	193
Unearned Employee Stock Ownership Plan shares	(378)	(437)
Total shareholders' equity	46,673	45,734
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 468,756	$ 462,409

(A) The balance sheet at December 31, 2009 has been derived from the audited consolidated financial statements at that date.

SOUTHERN MICHIGAN BANCORP, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

	Three Months Ended June 30, 2010	Three Months Ended June 30, 2009	Six Months Ended June 30, 2010	Six Months Ended June 30, 2009
	(In thousands, except per share amounts)			
Interest income:				
Loans, including fees	$ 4,748	$ 4,971	$ 9,549	$ 9,915
Federal funds sold and balances with banks	34	11	57	20
Securities:				
Taxable	142	278	323	667
Tax exempt	198	223	402	453
Total interest income	5,122	5,483	10,331	11,055
Interest expense:				
Deposits	934	1,145	1,935	2,433
Other	175	207	343	402
Total interest expense	1,109	1,352	2,278	2,835
Net interest income	4,013	4,131	8,053	8,220
Provision for loan losses	150	500	350	1,950
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	3,863	3,631	7,703	6,270
Non-interest income:				
Service charges on deposit accounts	612	738	1,182	1,305
Trust fees	243	228	496	479
Net gains on security calls and sales	207	407	207	407
Net gains on loan sales	161	236	281	430
Earnings on life insurance assets	76	84	150	168
Gain on life insurance proceeds	-	-	156	-
Income and fees from automated teller machines	218	176	425	333
Other	197	269	441	504
TOTAL NON-INTEREST INCOME	1,714	2,138	3,338	3,626
Non-interest expense:				
Salaries and employee benefits	2,437	2,432	4,938	4,942
Occupancy, net	363	325	744	722
Equipment	233	231	454	455
Printing, postage and supplies	146	159	291	312
Telecommunication expenses	96	84	174	175
Professional and outside services	232	274	525	660
FDIC assessments	147	407	316	519
Software maintenance	97	143	208	214
Amortization of other intangibles	88	91	175	181
Other	718	728	1,422	1,441
Total non-interest expense	4,557	4,874	9,247	9,621
INCOME BEFORE INCOME TAXES	1,020	895	1,794	275
Federal income tax provision (credit)	217	144	289	(205)
NET INCOME	803	751	1,505	480
Basic Earnings Per Common Share	$ 0.35	$ 0.33	$ 0.65	$ 0.21
Diluted Earnings Per Common Share	$ 0.35	$ 0.33	$ 0.65	$ 0.21
Dividends Declared Per Common Share	$ 0.05	$ 0.05	$ 0.10	$ 0.10

Market Information

The Trust Department of Southern Michigan Bank & Trust acts as the transfer agent for the Company's stock. For information concerning the transfer of the Company's stock, or to participate in the dividend reinvestment program, please contact the Trust Department at (517) 279-5503 or (800) 379-7628.

The following brokerage firms make a market for Southern Michigan Bancorp, Inc. stock:

Boenning & Scattergood
Powell, Ohio
(866) 326-8113

Howe Barnes Investments, Inc.
Chicago, Illinois
(312) 655-2954 or
(800) 800-4693

Stifel, Nicolaus & Company, Inc.
Grand Rapids, Michigan
(800) 676-0477

Hilliard Lyons, Inc.
Coldwater, Michigan
(517) 278-4333 or
(800) 211-5257

Robert Baird & Company
Grand Rapids, Michigan
(616) 459-4491 or
(800) 888-6200

Officers of Southern Michigan Bank & Trust

COMMERCIAL LOANS

David Clow
Senior Vice President /
Head of Commercial Lending

Eric Anglin
Vice President

Ric Baker
Vice President

Deborah Davis
Vice President

Nick Grabowski
Vice President

Sarah Headley
Vice President

Robert Hungerford
Vice President

Doug Kiessling
Vice President

Joan Trenary
Vice President

James Sobeske
Vice President

Tom Swoish
Vice President

Jason Williams
Vice President

Cindy Woolner
Assistant Vice President /
Special Assets Manager

Marcia McClellan
Administration Officer

RESIDENTIAL & CONSUMER LOANS

Jamie Smoker
Senior Vice President /
Head of Residential
& Consumer Lending

Rick Feller
Vice President /
Lending and Sr. Collection Administrator

Phyllis Wingate
Vice President / Head of Retail
Loan Operations

Tina Mack
Assistant Vice President /
Loan Operations

Jeremiah Ervans
Assistant Vice President /
Retail Loan Officer

DeAnne Hawley
Assistant Vice President /
Retail Loan Officer

Shari Kline
Assistant Vice President /
Retail Loan Officer

Diane Krimmel
Assistant Vice President /
Retail Loan Officer

Lori Lemmon
Assistant Vice President /
Retail Loan Officer

Tammy Malatok
Assistant Vice President /
Retail Loan Officer

Gregory Mallar
Assistant Vice President /
Retail Loan Officer

Desiree Kauffman
Retail Loan Officer

Judie Ratering
Retail Loan Officer

Connie Swain-Caudill
Assistant Vice President /
Senior Collections Manager

Debbie Leer
Collections Officer

LOAN REVIEW

Trisha Pawloski
Assistant Vice President/
Loan Review Officer

TRUST DEPARTMENT

Mary Guthrie
Senior Vice President /
Senior Trust Officer

David Rumsey
Vice President /
Senior Investment Officer

Jean Winans
Vice President /
Senior Trust Officer

Susan White
Vice President /
Trust Officer

INVESTMENTS

Melissa Barlow
Vice President/
Senior Investment Officer

RETAIL BANKING SERVICES

Sally Cotton
First Vice President /
Senior Branch Administration Officer

ATHENS BRANCH

Marcia Carman
Branch Manager

BATTLE CREEK BRANCH

Claudia Murch
Assistant Vice President /
Branch Manager

CAMDEN BRANCH

Lori Neill
Branch Supervisor*

COLDWATER MAIN &
EAST CHICAGO BRANCHES

Abby Austin
Branch Manager

CASSOPOLIS BRANCH

Janet Nosich
Branch Manager

CENTREVILLE BRANCH

Paul Harker
Branch Manager

CONSTANTINE BRANCH

Lorraine Fifer
Branch Manager

HILLSDALE BRANCH

Ann Marie Bentley
Assistant Vice President /
Regional Branch Manager

MARSHALL BRANCH

Annette Campau
Assistant Vice President /
Community Bank Officer

MENDON BRANCH

Doreen Tobin
Assistant Vice President /
Regional Branch Manager

NORTH ADAMS BRANCH

Leonce Towers
Branch Supervisor*

TEKONSHA BRANCH

Dawn Copas
Branch Manager

THREE RIVERS MAIN BRANCH

Sharon Bachinski
Assistant Vice President /
Regional Branch Manager

THREE RIVERS WESTLAND BRANCH

Lynette Lorenz
Branch Manager

UNION CITY BRANCH

Ken Brooks
Vice President /
Regional Branch Manager

ACCOUNTING

Sara Herrmann
Vice President / Finance

INFORMATION SYSTEMS

Jeff Kiersey
Senior Vice President /
Chief Information Officer

Kelli Talbot
Vice President /
Banking Applications Analyst

Paul Mahle
Assistant Vice President /
Senior Data Processing Officer

Vikki Kline
Project / Research Officer

Matt Siefken
Network and Systems Officer

COMPLIANCE

Christine Hagaman
Vice President /
Compliance Officer

e-SERVICES

Jamie Tobalske
Assistant Vice President /
e-Services Officer

MARKETING

Patty Parker
Vice President

*Non Officer Position

Officers of Southern Michigan Bancorp, Inc.

John H. Castle
Chairman & Chief Executive Officer

Kurt G. *Miller*
President

Danice L. Chartrand
Senior Vice President /
Chief Financial Officer

Executive Officers of Southern Michigan Bank & Trust

John H. Castle
Chairman & Chief Executive Officer

Kurt G. Miller
President

Danice L. Chartrand
Senior Vice President /
Chief Financial Officer

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Cover Photo: Brooks Memorial Fountain in Marshall, Michigan