SECOND Quarter

Corporate Highlights

Southern Michigan BANCORP, INC.

To Our Shareholders:

I am pleased to report that Southern Michigan Bancorp, Inc. posted another quarter of solid results. Net income for the second quarter of 2012 was $1,027,000, or $.43 per share, compared with second quarter 2011 net income of $762,000, or $.33 per share. For the first six months of 2012, Southern earned $2,029,000, or $.86 per share, compared with $1,510,000, or $.65 per share, for the same six-month period a year ago.

Southern's success through the first six months of 2012 was driven largely by our management team's strategic focus on developing high quality small business lending relationships throughout our four-county primary service area. The results of those initiatives led to an increase in our commercial loan portfolio of $16 million during the most recent quarter, with total commercial loans exceeding $261 million at June 30, 2012. Net interest income for the first six months of 2012 grew by 10.6 percent to $8.4 million, compared with $7.6 million for the first six months of 2011.

Many of our customers have taken advantage of historically low interest rates to refinance their home mortgages. Gains on sales of mortgage loans grew substantially, totaling $878,000 for the first six months of 2012, compared with $522,000 for the same period a year ago. In addition, we are seeing modest improvement in purchases and sales of existing homes and in new home construction.

As of June 30, 2012, total assets were $503.9 million compared with $481.3 million as of June 30, 2011. Southern's annualized return on average assets for the first six months of 2012 was .78 percent compared with .61 percent for the same period a year ago. The annualized return on average equity for the first six months of 2012 improved to 7.66 percent compared with 6.17 percent for the same six-month period last year.

The strength and consistency of Southern's financial condition and performance is particularly noteworthy given the continued headwinds of an uncertain economy, burdensome regulations and escalating costs. During its June meeting, the board of directors approved an increase in the quarterly dividend from $.07 per share to $.09 per share. The board continues to evaluate dividend payout levels based on various performance criteria, including operating results and capital levels.

I will close on a personal note. In July, all of us in the Southern Family were deeply saddened by the sudden passing of Dave Clow, our Senior Vice President and Head of Commercial Lending. Dave joined Southern in 2004 as the Senior Commercial Lending Officer. He was a thoughtful mentor, an outstanding colleague and respected by peers throughout the banking industry. Most importantly, Dave was a wonderful friend to many within the bank and community. He will be missed and fondly remembered.

Sincerely,

JH Castle

John H. Castle
Chairman and Chief Executive Officer

100656

SOUTHERN MICHIGAN BANCORP, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

	June 30, 2012	December 31, 2011
	(Unaudited)	(A)
	(In thousands, except share and per share data)	
ASSETS		
Cash and cash equivalents	$ 34,772	$ 42,185
Federal funds sold	253	287
Securities available for sale	76,054	90,344
Loans held for sale	1,624	1,088
Loans, net of allowance for loan losses of $5,167 - 2012 ($5,412 - 2011)	344,041	327,392
Premises and equipment, net	12,392	12,546
Accrued interest receivable	1,826	2,148
Net cash surrender value of life insurance	10,480	10,312
Goodwill	13,422	13,422
Other intangible assets, net	1,504	1,666
Other assets	7,499	7,830
TOTAL ASSETS	$ 503,867	$ 509,220
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities		
Deposits:		
Non-interest bearing	$ 69,591	$ 61,930
Interest bearing	347,956	358,581
TOTAL DEPOSITS	417,547	420,511
Securities sold under agreements to repurchase and overnight borrowings	14,214	18,074
Accrued expenses and other liabilities	4,558	4,568
Other borrowings	7,448	7,751
Subordinated debentures	5,155	5,155
Common stock subject to repurchase obligation in Employee Stock Ownership Plan, shares outstanding - 119,594 in 2012 (115,170 shares in 2011)	1,644	1,296
TOTAL LIABILITIES	450,566	457,355
Shareholders' equity:		
Preferred stock, 100,000 shares authorized; none issued or outstanding	-	-
Common stock, $2.50 par value:		
Authorized—4,000,000 shares		
Issued—2,376,204 shares in 2012 (2,358,599 shares in 2011)		
Outstanding (other than ESOP shares) - 2,256,610 shares in 2012 (2,243,429 shares in 2011)	5,642	5,609
Additional paid-in capital	17,991	18,278
Retained earnings	29,223	27,576
Accumulated other comprehensive income, net	548	571
Unearned Employee Stock Ownership Plan shares	(103)	(169)
Total shareholders' equity	53,301	51,865
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 503,867	$ 509,220

(A) The balance sheet at December 31, 2011 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, 2012	Three Months Ended June 30, 2011	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
	(In thousands, except per share amounts)			
Interest income:				
Loans, including fees	$ 4,629	$ 4,334	$ 9,140	$ 8,704
Federal funds sold and balances with banks	31	47	57	98
Securities:				
Taxable	63	171	219	309
Tax-exempt	246	218	488	434
Total interest income	4,969	4,770	9,904	9,545
Interest expense:				
Deposits	587	803	1,248	1,647
Other	129	148	262	307
Total interest expense	716	951	1,510	1,954
Net interest income	4,253	3,819	8,394	7,591
Provision for loan losses	475	375	700	500
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	3,778	3,444	7,694	7,091
Non-interest income:				
Service charges on deposit accounts	413	568	807	1,079
Trust fees	263	293	561	568
Net gains on security calls and sales	-	-	3	2
Net gains on loan sales	476	205	878	522
Earnings on life insurance assets	80	84	168	164
Brokerage income	49	46	103	94
ATM and debit card fee income	292	257	564	492
Other	127	124	281	237
TOTAL NON-INTEREST INCOME	1,700	1,577	3,365	3,158
Non-interest expense:				
Salaries and employee benefits	2,267	2,294	4,688	4,741
Occupancy, net	277	336	560	709
Equipment	217	204	409	407
Printing, postage and supplies	105	102	244	243
Telecommunication expenses	61	98	157	197
Professional and outside services	280	199	536	420
FDIC assessments	100	110	200	275
Software maintenance	120	110	231	215
Amortization of other intangibles	81	84	162	169
Expenses relating to OREO property	74	86	202	131
ATM expenses	109	92	210	174
Other	451	344	825	669
Total non-interest expense	4,142	4,059	8,424	8,350
INCOME BEFORE INCOME TAXES	1,336	962	2,635	1,899
Federal income tax provision	309	200	606	389
NET INCOME	$ 1,027	$ 762	$ 2,029	$ 1,510
Basic Earnings Per Common Share	$ 0.43	$ 0.33	$ 0.86	$ 0.65
Diluted Earnings Per Common Share	0.43	0.33	0.86	0.65
Dividends Declared Per Common Share	0.09	0.05	0.16	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

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Nick Grabowski
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Robert Hungerford
Vice President

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Head of Residential
& Consumer Lending

Rick Feller
Vice President /
Lending and Sr. Collection Administrator

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Vice President / Head of Retail
Loan Operations

Jeremiah Ervans
Assistant Vice President /
Retail Loan Officer

Tim Fox
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
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Retail Loan Officer

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Desiree Kauffman
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Senior Trust Officer

R. 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

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Retail Banking Services /
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Claudia Murch
Assistant Vice President /
Regional Branch Manager

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CONSTANTINE BRANCH
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Doreen Tobin
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Paul Mahle
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Assistant Vice President /
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Systems Solutions Officer

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Project / Research Officer

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