SECOND Quarter
Corporate Highlights

Southern Michigan Bancorp, Inc.
Continuous Banking Since 1872

To Our Shareholders:

Southern Michigan Bancorp, Inc. reported net income of $1,146,000, or $0.48 per share, for the second quarter ended June 30, 2014. This represents an increase of 6.2 percent over the second quarter 2013 results of $1,079,000, or $0.45 per share. For the first six months of 2014, Southern earned $2,248,000, or $0.93 per share, compared with $2,134,000, or $0.89 per share, for the same six month period a year ago.

Our annualized return on average assets for the first six months of 2014 was .81 percent. The annualized return on average equity for the same period in 2013 was 7.74 percent. The tax equivalent net interest margin for the six month period ending June 30, 2014 was 3.79 percent. The second quarter dividend of $0.15 per share represents a 25 percent increase over the quarterly dividend of $0.12 per share for the comparable quarter of 2013. Through the first six months of 2014, Southern's cumulative dividend rate was $0.28 per share compared with $0.24 per share through the first six months of 2013.

Total assets as of June 30, 2014 increased slightly to $546.3 million from $539.5 million at year end 2013. Loan totals remained nearly flat as well at $384.5 million at June 30, 2014 as compared to $386 million as of December 31, 2013. However, on a year-over-year basis total assets grew $24 million from June 30, 2013 levels of $522.3 million. Gross loans increased by $17.7 million, nearly a 4.8 percent increase, compared with $366.8 million for the same period last year. Commercial loan totals grew year over year to $299.2 million from $282.6 million as of June 30, 2013. Proactively managing the balance sheet has positioned the bank with ample liquidity and very little leverage. In addition, our commercial loan pipeline remains strong and we anticipate loan growth in the second half of this year. Continued funding of new loans utilizing our liquidity should positively impact revenues.

Asset quality remains solid as delinquencies at quarter-end were 1.42 percent of total loans as compared to 1.79 percent as of June 30, 2013. Net charge-offs for the six month period ending June 30, 2014 totaled $227,000, or annualized .12 percent of total loans. The allowance for loan losses as of June 30, 2014 was $5.2 million, or 1.36 percent of total loans, after recording provision expense for the second quarter of $225,000.

Non-interest income decreased slightly to $1.6 million for the quarter ended June 30, 2014 as compared to $1.8 million for the second quarter of 2013. Gains from mortgage loans originated and sold in the secondary market for the quarter ended June 30, 2014 totaled $209,000, down $244,000, as compared to $453,000 for the same period in 2013. For the first six months of 2014, secondary market gains totaled $405,000, a reduction of $572,000, compared to $976,000 generated for the same six month period in 2013. This is an ongoing continuation of the dramatic slowdown in mortgage originations that is being experienced within our market area and throughout the industry.

There is no question that Southern continues to gain positive momentum as measured by any number of strategic benchmarks including earnings, asset quality and growth of our balance sheet and loan portfolio. Your continued support of Southern is appreciated.

Sincerely,

JH Castle

John H. Castle
Chairman and Chief Executive Officer

SOUTHERN MICHIGAN BANCORP, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

	June 30, 2014	December 31, 2013
	(Unaudited)	(A)
	(In thousands, except share and per share data)	
ASSETS		
Cash and cash equivalents	$ 19,726	$ 32,366
Federal funds sold	243	148
Securities available for sale	98,248	76,005
Loans held for sale	567	115
Loans, net of allowance for loan losses of $5,236-2014 ($5,238 -2013)	379,276	380,773
Premises and equipment, net	11,937	12,366
Accrued interest receivable	2,280	2,351
Net cash surrender value of life insurance	11,138	10,979
Goodwill	13,422	13,422
Other intangible assets, net	903	1,045
Other assets	8,532	9,889
TOTAL ASSETS	$ 546,272	$ 539,459
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities		
Deposits:		
Non-interest bearing	$ 93,867	$ 85,670
Interest bearing	362,138	364,730
TOTAL DEPOSITS	456,005	450,400
Securities sold under agreements to repurchase and overnight borrowings	12,078	18,479
Accrued expenses and other liabilities	5,316	6,351
Other borrowings	6,800	-
Subordinated debentures	5,155	5,155
Common stock subject to repurchase obligation in Employee Stock Ownership Plan, shares outstanding - 124,971 in 2014 (126,931 shares in 2013)	2,356	2,247
TOTAL LIABILITIES	487,710	482,632
Shareholders' equity:		
Preferred stock, 100,000 shares authorized; none issued or outstanding	-	-
Common stock, $2.50 par value:		
Authorized—4,000,000 shares		
Issued—2,405,669 shares in 2014 (2,392,630 shares in 2013)		
Outstanding (other than ESOP shares) - 2,280,698 shares in 2014 (2,265,699 shares in 2013)	5,696	5,665
Additional paid-in capital	17,377	17,533
Retained earnings	35,919	34,346
Accumulated other comprehensive income, net	(430)	(717)
Total shareholders' equity	58,562	56,827
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 546,272	$ 539,459

(A) The balance sheet at December 31, 2013 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, 2014	Three Months Ended June 30, 2013	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013
	(In thousands, except per share amounts)			
Interest income:				
Loans, including fees	$ 4,611	$ 4,537	$ 9,199	$ 9,035
Federal funds sold and balances with banks	20	26	40	51
Securities:				
Taxable	230	166	423	288
Tax-exempt	199	222	395	447
Total interest income	5,060	4,951	10,057	9,821
Interest expense:				
Deposits	325	465	714	970
Other	71	70	145	148
Total interest expense	396	535	859	1,118
Net interest income	4,664	4,416	9,198	8,703
Provision for loan losses	225	175	225	400
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	4,439	4,241	8,973	8,303
Non-interest income:				
Service charges on deposit accounts	515	478	1,001	875
Trust fees	279	265	569	545
Net gains on security calls and sales	4	-	37	-
Net gains on loan sales	209	453	405	976
Earnings on life insurance assets	77	86	159	170
ATM and debit card fee income	325	313	615	592
Other	227	192	428	352
TOTAL NON-INTEREST INCOME	1,636	1,787	3,214	3,510
Non-interest expense:				
Salaries and employee benefits	2,414	2,390	4,778	4,925
Occupancy, net	309	275	676	567
Equipment	158	227	331	435
Printing, postage and supplies	120	124	225	233
Telecommunication expenses	85	68	158	137
Professional and outside services	246	369	590	679
FDIC assessments	92	94	180	182
Software maintenance	235	260	433	532
Amortization of other intangibles	71	74	142	148
Loan related expenses	51	57	392	116
ATM expenses	125	112	241	216
Other	597	460	958	743
Total non-interest expense	4,503	4,510	9,104	8,913
INCOME BEFORE INCOME TAXES	1,572	1,518	3,083	2,900
Federal income tax provision	426	439	835	766
NET INCOME	$ 1,146	$ 1,079	$ 2,248	$ 2,134
Basic Earnings Per Common Share	$ 0.48	$ 0.45	$ 0.94	$ 0.89
Diluted Earnings Per Common Share	0.48	0.45	0.93	0.89
Dividends Declared Per Common Share	0.15	0.12	0.28	0.24

Market Information

Inquiries regarding stock certificate administration, address changes, transfers, and other related services should be directed to:
IST Shareholder Services
Website:www.istshareholderservices.com
Phone: (630) 480-0393
Toll free: (800) 757-5755
Fax: (630) 480-0641
Address: 433 South Carlton Ave., Wheaton, IL 60187-4872

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

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

Raymond James Financial Associates
Chicago, Illinois
(312) 655-2961 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

Royal Securities Company
Grand Rapids, Michigan
(616) 459-2844 or (888) 804-8891

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Senior Collections Manager

Lynn Roper
Secondary Market /
Loan Servicing Officer

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Risk Management Officer

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Senior Investment Officer

Jean Winans
Vice President /
Senior Trust Officer

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Retail Banking Services /
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BATTLE CREEK BRANCH
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Assistant Vice President / Branch
Manager / Retail Loan Officer

TEKONSHA BRANCH
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Angie Smith
Assistant Vice President /
Operations Manager

Becky Omo
Assistant Vice President /
Operations Representative

Jamie Tobalske
Assistant Vice President /
e-Services Officer

Vikki Kline
Project / Research Officer

MARKETING

Patty Parker
Vice President

Southern Michigan Bancorp, Inc.
Continuous Banking Since 1872
www.smb-t.com

Executive Officers of Southern Michigan Bank & Trust and Southern Michigan Bancorp, Inc.

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Chairman & Chief Executive Officer

Kurt G. Miller
President / Chief Credit Officer

Danice L. Chartrand
Senior Vice President /
Chief Financial Officer