FIRST BANCORP /NC/
Form 10-K
March 16, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2009

Commission File Number 0-15572

FIRST BANCORP

(Exact Name of Registrant as Specified in its Charter)

North Carolina (State of Incorporation)	56-1421916 (I.R.S. Employer Identification Number)
341 North Main Street, Troy, North Carolina	27371-0508
(Address of Principal Executive Offices)	(Zip Code)
Registrant's telephone number, including area code:	(910) 576-6171

Securities Registered Pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, No Par Value	The Nasdaq Global Select Market

Securities Registered Pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act of 1933. ¨ YES x NO

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Securities Exchange Act of 1934. ¨ YES x NO

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the preceding twelve 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. x YES ¨ NO

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files. ¨ YES ¨ NO

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of the Form 10-K or any amendment to the Form 10-K. ¨

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. (Check one)

¨ Large Accelerated File	x 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 x NO

The aggregate market value of the Common Stock, no par value, held by non-affiliates of the registrant, based on the closing price of the Common Stock as of June 30, 2009 as reported by The NASDAQ Global Select Market, was approximately $231,067,238.

The number of shares of the registrant's Common Stock outstanding on March 4, 2010 was 16,736,730.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's Proxy Statement to be filed pursuant to Regulation 14A are incorporated herein by reference into Part III.

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* Information called for by Part III (Items 10 through 14) is incorporated herein by reference to the Registrant's definitive Proxy Statement for the 2010 Annual Meeting of Shareholders to be filed with the Securities and Exchange Commission on or before April 30, 2010.

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FORWARD-LOOKING STATEMENTS

This report contains statements that could be deemed forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934 and the Private Securities Litigation Reform Act, which statements are inherently subject to risks and uncertainties. Forward-looking statements are statements that include projections, predictions, expectations or beliefs about future events or results or otherwise are not statements of historical fact. Such statements are often characterized by the use of qualifying words (and their derivatives) such as "expect," "believe," "estimate," "plan," "project," or other statements concerning our opinions or judgment about future events. Factors that could influence the accuracy of such forward-looking statements include, but are not limited to, the financial success or changing strategies of our customers, our level of success in integrating acquisitions, actions of government regulators, the level of market interest rates, and general economic conditions. For additional information that could affect the matters discussed in this paragraph, see the "Risk Factors" section in Item 1A of this report.

PART I

Item 1. Business

General Description

The Company

First Bancorp (the "Company") is a bank holding company. The principal activity of the Company is the ownership and operation of First Bank (the "Bank"), a state-chartered bank with its main office in Troy, North Carolina. The Company also owns and operates a nonbank subsidiary, Montgomery Data Services, Inc. ("Montgomery Data"), a data processing company. This subsidiary is fully consolidated for financial reporting purposes. The Company is also the parent to a series of statutory business trusts organized under the laws of the State of Delaware that were created for the purpose of issuing trust preferred debt securities. The Company's outstanding debt associated with these trusts was $46.4 million at December 31, 2009 and 2008.

The Company was incorporated in North Carolina on December 8, 1983, as Montgomery Bancorp, for the purpose of acquiring 100% of the outstanding common stock of the Bank through a stock-for-stock exchange. On December 31, 1986, the Company changed its name to First Bancorp to conform its name to the name of the Bank, which had changed its name from Bank of Montgomery to First Bank in 1985.

The Bank was organized in 1934 and began banking operations in 1935 as the Bank of Montgomery, named for the county in which it operated. As of December 31, 2009, the Bank operated in a 36-county area centered in Troy, North Carolina. Troy, population 3,500, is located in the center of Montgomery County, approximately 60 miles east of Charlotte, 50 miles south of Greensboro, and 80 miles southwest of Raleigh. The Bank conducts business from 91 branches covering a geographical area from Little River, South Carolina to the southeast, to Wilmington, North Carolina to the east, to Kill Devil Hills, North Carolina to the northeast, to Radford, Virginia to the north, to Wytheville, Virginia to the northwest, and to Harmony, North Carolina to the west. The Bank also has a loan production office in Blacksburg, which is located in southwestern Virginia and represents the Bank's furthest location to the north of Troy. Of the Bank's 91 branches, 77 are in North Carolina, with nine branches in South Carolina and five branches in Virginia (where the Bank operates under the name "First Bank of Virginia"). Ranked by assets, the Bank was the sixth largest bank headquartered in North Carolina as of December 31, 2009.

On June 19, 2009, the Bank acquired substantially all of the assets and liabilities of Cooperative Bank, which had been closed earlier that day by regulatory authorities. Cooperative Bank operated through twenty-four

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branches located primarily in the coastal region of North Carolina. In connection with the acquisition, the Bank assumed assets with a book value of $959 million, including $829 million in loans and $706 million in deposits. The loans and foreclosed real estate purchased are covered by loss share agreements between the Federal Deposit Insurance Corporation (FDIC) and First Bank which affords the Bank significant loss protection. The Company recorded a gain of $67.9 million as a result of this acquisition. Additional information regarding this transaction is contained in Management's Discussion and Analysis of Financial Condition and Results of Operations and Note 2 to the audited consolidated financial statements.

As of December 31, 2009, the Bank had two wholly owned subsidiaries, First Bank Insurance Services, Inc. ("First Bank Insurance") and First Troy SPE, LLC. First Bank Insurance was acquired as an active insurance agency in 1994 in connection with the Company's acquisition of a bank that had an insurance subsidiary. On December 29, 1995, the insurance agency operations of First Bank Insurance were divested. From December 1995 until October 1999, First Bank Insurance was inactive. In October 1999, First Bank Insurance began operations again as a provider of non-FDIC insured investments and insurance products. Currently, First Bank Insurance's primary business activity is the placement of property and casualty insurance coverage. First Troy SPE, LLC, which was organized in December 2009, is a holding entity for certain foreclosed properties.

The Company's principal executive offices are located at 341 North Main Street, Troy, North Carolina 27371-0508, and its telephone number is (910) 576-6171. Unless the context requires otherwise, references to the "Company" in this annual report on Form 10-K shall mean collectively First Bancorp and its consolidated subsidiaries.

General Business

The Bank engages in a full range of banking activities, with the acceptance of deposits and the making of loans being its most basic activities. The Bank offers deposit products such as checking, savings, NOW and money market accounts, as well as time deposits, including various types of certificates of deposits (CDs) and individual retirement accounts (IRAs). For business customers, the Bank offers repurchase agreements (also called securities sold under agreement to repurchase), which are similar to interest-bearing deposits and allow the Bank to pay interest to business customers without statutory limitations on the number of withdrawals that these customers can make. The Bank provides loans for a wide range of consumer and commercial purposes, including loans for business, agriculture, real estate, personal uses, home improvement and automobiles. The Bank also offers credit cards, debit cards, letters of credit, safe deposit box rentals, bank money orders and electronic funds transfer services, including wire transfers. In addition, the Bank offers internet banking, mobile banking, cash management and bank-by-phone capabilities to its customers, and is affiliated with ATM networks that give Bank customers access to 55,000 ATMs, with no surcharge fee. In 2007, the Bank introduced remote deposit capture, which provides business customers with a method to electronically transmit checks received from customers into their bank account without having to visit a branch. In 2008, the Bank joined the Certificate of Deposit Account Registry Service (CDARS), which gives our customers the ability to obtain FDIC insurance on deposits of up to $50 million, while continuing to work directly with their local First Bank branch.

Because the majority of the Bank's customers are individuals and small to medium-sized businesses located in the counties it serves, management does not believe that the loss of a single customer or group of customers would have a material adverse impact on the Bank. There are no seasonal factors that tend to have any material effect on the Bank's business, and the Bank does not rely on foreign sources of funds or income. Because the Bank operates primarily within the coastal and central Piedmont regions of North Carolina, the economic conditions of those areas could have a material impact on the Company. See additional discussion below in the section entitled "Territory Served and Competition."

Beginning in 1999, First Bank Insurance began offering non-FDIC insured investment and insurance products, including mutual funds, annuities, long-term care insurance, life insurance, and company retirement plans, as well as financial planning services (the “investments division”). In May 2001, First Bank Insurance

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added to its product line when it acquired two insurance agencies that specialized in the placement of property and casualty insurance. In October 2003, the "investments division" of First Bank Insurance became a part of the Bank. The primary activity of First Bank Insurance is now the placement of property and casualty insurance products. In February 2010, First Bank Insurance reported that it had acquired The Insurance Center, Inc., a Troy-based property and casualty insurance agency with approximately 500 customers.

Montgomery Data's primary business is to provide electronic data processing services for the Bank. Ownership and operation of Montgomery Data allows the Company to do all of its electronic data processing without paying fees for such services to an independent provider. Maintaining its own data processing system also allows the Company to adapt the system to its individual needs and to the services and products it offers. Although not a significant source of income, Montgomery Data has historically made its excess data processing capabilities available to area financial institutions for a fee. For the years ended December 31, 2009, 2008 and 2007, external customers provided gross revenues of $139,000, $167,000 and $204,000, respectively. As of December 31, 2009 Montgomery Data had one outside customer. However this customer terminated its service agreement with Montgomery Data effective in January 2010. In light of the demands of providing service to the Bank, the Company has decided to discontinue this service for third parties, and the Company expects to merge Montgomery Data into the Bank in 2010.

Until December 31, 2007, the Company had another subsidiary, First Bancorp Financial Services. First Bancorp Financial was originally organized under the name of First Recovery in September of 1988 for the purpose of providing a back-up data processing site for Montgomery Data and other financial and non-financial clients. First Recovery's back-up data processing operations were divested in 1994. Since that time, First Bancorp Financial had been occasionally used to purchase and dispose of parcels of real estate that had been acquired by the Bank through foreclosure or from branch closings. First Bancorp Financial Services had been substantially inactive for most of the last decade, and the Company elected to dissolve this subsidiary effective December 31, 2007.

First Bancorp Capital Trust I was organized in October 2002 for the purpose of issuing $20.6 million in debt securities. These debt securities were called by the Company at par on November 7, 2007 and First Bancorp Capital Trust I was dissolved.

First Bancorp Capital Trust II and First Bancorp Capital Trust III were organized in December 2003 for the purpose of issuing $20.6 million in debt securities ($10.3 million was issued from each trust). These borrowings are due on January 23, 2034 and are also structured as trust preferred capital securities in order to qualify as regulatory capital. These debt securities are callable by the Company at par on any quarterly interest payment date beginning on January 23, 2009. The interest rate on these debt securities adjusts on a quarterly basis at a weighted average rate of three-month LIBOR plus 2.70%.

First Bancorp Capital Trust IV was organized in April 2006 for the purpose of issuing $25.8 million in debt securities. These borrowings are due on June 15, 2036 and are structured as trust preferred capital securities, which qualify as capital for regulatory capital adequacy requirements. These debt securities are callable by the Company at par on any quarterly interest payment date beginning on June 15, 2011. The interest rate on these debt securities adjusts on a quarterly basis at a rate of three-month LIBOR plus 1.39%.

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Territory Served and Competition

The Company's headquarters are located in Troy, Montgomery County, North Carolina. The Company serves primarily the south central area of the Piedmont and the southeastern coastal regions of North Carolina, with additional operations in northeastern South Carolina and southwestern Virginia. The following table presents, for each county where the Company operates, the number of bank branches operated by the Company within the county at December 31, 2009, the approximate amount of deposits with the Company in the county as of December 31, 2009, the Company's approximate deposit market share at June 30, 2009, and the number of bank competitors located in the county at June 30, 2009.

County	Number of Branches	Deposits (in millions)	Market Share	Number of Competitors
Anson, NC	1	$ 11	4.2 %	5
Beaufort, NC	3	48	6.3 %	6
Bladen, NC	1	29	11.4 %	5
Brunswick, NC	4	103	4.3 %	12
Cabarrus, NC	2	36	1.9 %	11
Carteret, NC	2	42	4.7 %	8
Chatham, NC	2	75	11.5 %	10
Chesterfield, SC	3	76	21.0 %	7
Columbus, NC	2	45	6.3 %	6
Dare, NC	1	18	1.8 %	11
Davidson, NC	3	106	4.2 %	10
Dillon, SC	3	72	26.6 %	3
Duplin, NC	3	125	26.3 %	6
Florence, SC	2	34	1.7 %	14
Guilford, NC	1	54	0.6 %	21
Harnett, NC	3	123	13.1 %	10
Horry, SC	1	7	0.1 %	26
Iredell, NC	2	35	1.5 %	22
Lee, NC	4	201	24.9 %	10
Montgomery, NC	5	104	38.1 %	4
Montgomery, VA	1	33	1.9 %	13
Moore, NC	11	464	23.6 %	11
New Hanover, NC	5	194	5.0 %	19
Onslow, NC	2	52	4.9 %	9
Pulaski, VA	1	22	5.7 %	8
Randolph, NC	4	69	3.6 %	15
Richmond, NC	1	23	5.0 %	6
Robeson, NC	5	187	17.3 %	10
Rockingham, NC	1	28	2.4 %	11
Rowan, NC	2	54	3.5 %	12
Scotland, NC	2	59	17.7 %	6
Stanly, NC	4	96	10.2 %	6
Wake, NC	1	16	0.1 %	30
Washington, VA	1	26	2.0 %	16
Wythe, VA	2	62	10.7 %	10
Brokered & Internet Deposits	-	204		

Total	91	$ 2,933

The Company's 91 branches and facilities are primarily located in small communities whose economies are based primarily on services, manufacturing and light industry. Although the Company's market is predominantly small communities and rural areas, the market area is not dependent on agriculture. Textiles, furniture, mobile homes, electronics, plastic and metal fabrication, forest products, food products, chicken hatcheries, and cigarettes are among the leading manufacturing industries in the trade area. Leading producers of lumber and rugs are located in Montgomery County, North Carolina. The Pinehurst area within Moore County, North Carolina, is a widely known golf resort and retirement area. The High Point, North Carolina, area is widely

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known for its furniture market. New Hanover and Brunswick Counties, located in the southeastern coastal region of North Carolina, are popular with tourists and have significant retirement populations. Additionally, several of the communities served by the Company are "bedroom" communities of large cities like Charlotte, Raleigh and Greensboro, while several branches are located in medium-sized cities such as Albemarle, Asheboro, High Point, Southern Pines and Sanford. The Company also has branches in small communities such as Bennett, Polkton, Vass, and Harmony.

Approximately 16% of the Company's deposit base is in Moore County. Accordingly, material changes in competition, the economy or population of Moore County could materially impact the Company. No other county comprises more than 10% of the Company's deposit base.

The Company competes in its various market areas with, among others, several large interstate bank holding companies. These large competitors have substantially greater resources than the Company, including broader geographic markets, higher lending limits and the ability to make greater use of large-scale advertising and promotions. A significant number of interstate banking acquisitions have taken place in the past decade, thus further increasing the size and financial resources of some of the Company's competitors, two of which are among the largest bank holding companies in the nation. In many of the Company's markets, the Company also competes against banks that have been organized within the past ten to fifteen years. These new banks have often focused on loan and deposit balance sheet growth, and not necessarily on earnings profitability. This strategy often allows them to offer more attractive terms on loans and deposits than the Company is able to offer because the Company must achieve an acceptable level of profitability. Moore County, which as noted above comprises a disproportionate share of the Company's deposits, is a particularly competitive market, with at least eleven other financial institutions having a physical presence. See "Supervision and Regulation" below for a further discussion of regulations in the Company's industry that affect competition.

The Company competes not only against banking organizations, but also against a wide range of financial service providers, including federally and state-chartered savings and loan institutions, credit unions, investment and brokerage firms and small-loan or consumer finance companies. One of the credit unions in the Company's market area is among the largest in the nation. Competition among financial institutions of all types is virtually unlimited with respect to legal ability and authority to provide most financial services. The Company also experiences competition from internet banks, particularly in the area of time deposits.

Despite the competitive market, the Company believes it has certain advantages over its competition in the areas it serves. The Company seeks to maintain a distinct local identity in each of the communities it serves and actively sponsors and participates in local civic affairs. Most lending and other customer-related business decisions can be made without delays often associated with larger systems. Additionally, employment of local managers and personnel in various offices and low turnover of personnel enable the Company to establish and maintain long-term relationships with individual and corporate customers.

Lending Policy and Procedures

Conservative lending policies and procedures and appropriate underwriting standards are high priorities of the Bank. Loans are approved under the Bank's written loan policy, which provides that lending officers, principally branch managers, have authority to approve loans of various amounts up to $350,000, with lending limits varying depending upon whether the loan is secured or unsecured. Each of the Bank's regional senior lending officers has discretion to approve secured loans of various principal amounts up to $500,000 and together can approve loans up to $4,000,000. Loans above $4,000,000 must be approved by the Executive Committee of the board of directors.

The Bank's board of directors reviews and approves loans that exceed management's lending authority, loans to executive officers, directors, and their affiliates and, in certain instances, other types of loans. New credit extensions

are reviewed daily by the Bank’s senior management and at least monthly by its board of directors.

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The Bank continually monitors its loan portfolio to identify areas of concern and to enable management to take corrective action. Lending officers and the board of directors meet periodically to review past due loans and portfolio quality, while assuring that the Bank is appropriately meeting the credit needs of the communities it serves. Individual lending officers are responsible for pursuing collection of past-due amounts and monitoring any changes in the financial status of borrowers.

The Bank also contracts with an independent consulting firm to review new loan originations meeting certain criteria, as well as to assign risk grades to existing credits meeting certain thresholds. The consulting firm's observations, comments, and risk grades, including variances with the Bank's risk grades, are shared with the audit committee of the Company's board of directors and are considered by management in setting Bank policy, as well as in evaluating the adequacy of the allowance for loan losses. The consulting firm also provides training on a periodic basis to the Company's loan officers to keep them updated on current developments in the marketplace. For additional information, see "Allowance for Loan Losses and Loan Loss Experience" under Item 7 below.

Investment Policy and Procedures

The Company has adopted an investment policy designed to maximize the Company's income from funds not needed to meet loan demand, in a manner consistent with appropriate liquidity and risk objectives. Pursuant to this policy, the Company may invest in federal, state and municipal obligations, federal agency obligations, public housing authority bonds, industrial development revenue bonds, Federal Home Loan Bank bonds, Fannie Mae bonds, Government National Mortgage Association bonds, Freddie Mac bonds, Student Loan Marketing Association bonds, and, to a limited extent, corporate bonds. Except for corporate bonds, the Company's investments must be rated at least Baa by Moody's or BBB by Standard and Poor's. Securities rated below A are periodically reviewed for creditworthiness. The Company may purchase non-rated municipal bonds only if such bonds are in the Company's general market area and determined by the Company to have a credit risk no greater than the minimum ratings referred to above. Industrial development authority bonds, which normally are not rated, are purchased only if they are judged to possess a high degree of credit soundness to assure reasonably prompt sale at a fair value. The Company is also authorized by its board of directors to invest a portion of its securities portfolio in high quality corporate bonds, with the amount of such bonds not to exceed 15% of the entire securities portfolio. Prior to purchasing a corporate bond, the Company's management performs due diligence on the issuer of the bond, and the purchase is not made unless the Company believes that the purchase of the bond bears no more risk to the Company than would an unsecured loan to the same company.

The Company's investment officer implements the investment policy, monitors the investment portfolio, recommends portfolio strategies and reports to the Company's Investment Committee. The Investment Committee generally meets on a quarterly basis to review investment activity and to assess the overall position of the securities portfolio. The Investment Committee compares the Company's securities portfolio with portfolios of other companies of comparable size. In addition, reports of all purchases, sales, issuer calls, net profits or losses and market appreciation or depreciation of the bond portfolio are reviewed by the Company's board of directors each month. Once a quarter, the Company's interest rate risk exposure is evaluated by its board of directors. Each year, the written investment policy is approved by the board of directors.

Mergers and Acquisitions

As part of its operations, the Company has pursued an acquisition strategy over the years to augment its internal growth. The Company regularly evaluates the potential acquisition of, or merger with, various financial institutions. The Company's acquisitions have generally fallen into one of three categories - 1) an acquisition of a financial institution or branch thereof within a market in which the Company operates, 2) an acquisition of a financial institution or branch thereof in a market contiguous or nearly contiguous to a market in which the Company operates,

or 3) an acquisition of a company that has products or services that the Company does not

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currently offer. Historically, the Company has paid for its acquisitions with cash and/or common stock and any operating income or loss has been fully borne by the Company beginning on the closing date of the acquisition.

In 2009, FDIC-assisted acquisitions began to occur frequently as banking regulators closed problem banks. In FDIC-assisted transactions, the acquiring bank often does not pay any consideration for the failed bank, and in some cases receives cash from the FDIC as part of the transaction. In addition, the acquiring bank usually enters into one or more loss share agreements with the FDIC, which affords the acquiring bank significant loss protection. As discussed below, the Company completed a FDIC-assisted transaction in 2009.

The Company believes that it can enhance its earnings by pursuing these types of acquisition opportunities through any combination or all of the following: 1) achieving cost efficiencies, 2) enhancing the acquiree's earnings or gaining new customers by introducing a more successful banking model with more products and services to the acquiree's market base, 3) increasing customer satisfaction or gaining new customers by providing more locations for the convenience of customers, and 4) leveraging the Company's customer base by offering new products and services. There is also the possibility, especially in a FDIC-assisted transaction, to record a gain on the acquisition date arising from the difference between the purchase price and the acquisition date fair value of the acquired assets and liabilities.

Since 2000, the Company has completed acquisitions in each of the three categories described above. During that time, the Company has 1) completed four whole-bank traditional acquisitions, with one being in its existing market areas and the other three being in contiguous markets, with total assets exceeding $700 million, 2) purchased ten bank branches from other banks (both in existing market area and in contiguous/nearly contiguous markets) with total assets of approximately $250 million, and 3) acquired two insurance agencies, which provided the Company with the ability to offer property and casualty insurance coverage.

In addition to the traditional acquisitions discussed above, on June 19, 2009, the Bank acquired substantially all of the assets and liabilities of Cooperative Bank in a FDIC-assisted transaction. Cooperative Bank operated through twenty-one branches in North Carolina and three branches in South Carolina in the same markets in which the Bank was already operating, as well as in several new, mostly contiguous markets. In connection with the acquisition, First Bank assumed assets with a book value of $959 million, including $829 million in loans and $706 million in deposits. The loans and foreclosed real estate purchased are covered by two loss share agreements with the FDIC, which afford First Bank significant loss protection. Under the loss share agreements, the FDIC will cover 80% of covered loan and foreclosed real estate losses up to $303 million and 95% of losses in excess of that amount. The term for loss sharing on residential real estate loans is ten years, while the term for loss sharing on non-residential real estate loans is five years in respect to losses and eight years in respect to loss recoveries. The reimbursable losses from the FDIC are based on the book value of the relevant loan as determined by the FDIC at the date of the transaction. New loans made after that date are not covered by the loss share agreements. The Company received $26 million from the FDIC as result of this acquisition and recorded an acquisition gain of $67.9 million.

There are many factors that the Company considers when evaluating how much to offer for potential acquisition candidates (including FDIC-assisted transactions) with a few of the more significant factors being projected impact on earnings per share, projected impact on capital, and projected impact on book value and tangible book value. Significant assumptions that affect this analysis include the estimated future earnings stream of the acquisition candidate, estimated credit and other losses to be incurred, the amount of cost efficiencies that can be realized, and the interest rate earned/lost on the cash received/paid. In addition to the earnings per share comparison, the Company also considers other factors including (but not limited to) marketplace acquisition statistics, location of the candidate in relation to the Company's expansion strategy, market growth potential, management of the candidate, potential integration issues (including corporate culture), and the size of the acquisition candidate.

The Company plans to continue to evaluate acquisition opportunities that could potentially benefit the

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Company and its shareholders. These opportunities may include acquisitions that do not fit the categories discussed above.

For a further discussion of recent acquisition activity, see "Merger and Acquisition Activity" under Item 7 below.

Employees

As of December 31, 2009, the Company had 728 full-time and 72 part-time employees. The Company is not a party to any collective bargaining agreements and considers its employee relations to be good.

Supervision and Regulation

As a bank holding company, the Company is subject to supervision, examination and regulation by the Board of Governors of the Federal Reserve System (the "Federal Reserve Board") and the North Carolina Office of the Commissioner of Banks (the "Commissioner"). The Bank is subject to supervision and examination by the FDIC and the Commissioner. For additional information, see also Note 15 to the consolidated financial statements.

Supervision and Regulation of the Company

The Company is a bank holding company within the meaning of the Bank Holding Company Act of 1956, as amended. The Company is also regulated by the Commissioner under the North Carolina Bank Holding Company Act of 1984.

A bank holding company is required to file quarterly reports and other information regarding its business operations and those of its subsidiaries with the Federal Reserve Board. It is also subject to examination by the Federal Reserve Board and is required to obtain Federal Reserve Board approval prior to making certain acquisitions of other institutions or voting securities. The Federal Reserve Board requires the Company to maintain certain levels of capital - see "Capital Resources and Shareholders' Equity." The Federal Reserve Board also has the authority to take enforcement action against any bank holding company that commits any unsafe or unsound practice, or violates certain laws, regulations or conditions imposed in writing by the Federal Reserve Board. The Federal Reserve Board generally prohibits a bank holding company from declaring or paying a cash dividend that would impose undue pressure on the capital of subsidiary banks or would be funded only through borrowing or other arrangements which might adversely affect a bank holding company's financial position. Under the Federal Reserve Board policy, a bank holding company is not permitted to continue its existing rate of cash dividends on its common stock unless its net income is sufficient to fully fund each dividend and its prospective rate of earnings retention appears consistent with its capital needs, asset quality and overall financial condition.

The Federal Reserve Board has amended Regulation E, which implements the Electronic Fund Transfer Act, and the official staff commentary to the regulation, which interprets the requirements of Regulation E. The final rule limits the ability of a financial institution to assess an overdraft fee for paying automated teller machine (ATM) and one-time debit card transactions that overdraw a consumer's account, unless the consumer affirmatively consents, or opts in, to the institution's payment of overdrafts for these transactions. The rule has a mandatory compliance date of July 1, 2010 for new accounts and August 15, 2010 for existing accounts. Management believes that implementation of the new provisions will result in the reduction of overdraft fees collected by the Bank.

The Commissioner is empowered to regulate certain acquisitions of North Carolina banks and bank holding companies, issue cease and desist orders for violations of North Carolina banking laws, and promulgate rules necessary to effectuate the purposes of the North Carolina Bank Holding Company Act of 1984.

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Regulatory authorities have cease and desist powers over bank holding companies and their nonbank subsidiaries where their actions would constitute a serious threat to the safety, soundness or stability of a subsidiary bank. Those authorities may compel holding companies to invest additional capital into banking subsidiaries upon acquisitions or in the event of significant loan losses or rapid growth of loans or deposits.

The United States Congress and the North Carolina General Assembly have periodically considered and adopted legislation that has impacted the Company.

U.S. Treasury Capital Purchase Program

On October 3, 2008, in response to the financial crises affecting the banking system and financial markets and going concern threats to investment banks and other financial institutions, the Emergency Economic Stabilization Act of 2008 (the "EESA") was signed into law. Pursuant to the EESA, the U.S. Treasury was given the authority to, among other things, purchase up to $700 billion of mortgages, mortgage-backed securities and certain other financial instruments from financial institutions for the purpose of stabilizing and providing liquidity to the U.S. financial markets.

On October 14, 2008, the Secretary of the U.S. Department of the Treasury announced that the Treasury would purchase equity stakes in a wide variety of banks and thrifts. Under the program, known as the Capital Purchase Program, the Treasury made $250 billion of capital available from EESA to U.S. financial institutions in the form of purchases of preferred stock. In addition to the preferred stock, the Treasury received, from participating financial institutions, warrants to purchase common stock with an aggregate market price equal to 15% of the preferred investment. Participating financial institutions were required to adopt the Treasury's standards for executive compensation and corporate governance for the period during which the Treasury holds equity issued under the Capital Purchase Program.

Although we believed that our capital position was sound, we concluded that the Capital Purchase Program would allow us to raise additional capital on favorable terms in comparison with other available alternatives. Accordingly, we applied to participate in the Capital Purchase Program. The Treasury approved our application in December 2008, and we received $65 million in proceeds from the sale of 65,000 shares of cumulative perpetual preferred stock with a liquidation value of $1,000 per share to the Treasury on January 9, 2009. The preferred stock issued to the Treasury pays a dividend of 5% for the first five years and 9% thereafter. As part of the transaction, we also granted the Treasury a ten-year warrant to purchase up to 616,308 shares of our common stock at an exercise price of $15.82.

Under the terms of the Capital Purchase Program, the Treasury's consent will be required for any increase in our dividends paid to common stockholders (above a quarterly dividend of $0.19 per common share) or the Company's redemption, purchase or acquisition of common stock or any trust preferred securities issued by the Company's capital trusts until the third anniversary of the senior preferred share issuance to the Treasury unless prior to such third anniversary the senior preferred shares are redeemed in whole or the Treasury has transferred all of these shares to third parties.

Participants in the Capital Purchase Program were required to accept several compensation-related limitations associated with this Program. Each of our senior executive officers has agreed in writing to accept the compensation standards in existence at that time under the Capital Purchase Program and thereby cap or eliminate some of their contractual or legal rights. The provisions agreed to were as follows:

No Golden Parachute Payments. For purposes of the Capital Purchase Program, "golden parachute payment" was defined to mean a severance payment resulting from involuntary termination of employment or from a bankruptcy event of the employer, which exceeds three times the terminated employee's average annual base salary over the five

years prior to termination. Our senior executive officers have agreed to forego all golden parachute payments for as long as two conditions remain true: they remain “senior executive officers” (CEO,

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CFO and the next three highest-paid executive officers), and the Treasury continues to hold our equity or debt securities issued under the Capital Purchase Program. The period during which the Treasury holds those securities is the "Capital Purchase Program Covered Period."

Recovery of Incentive Compensation if Based on Certain Material Inaccuracies. Our senior executive officers have also agreed to a "clawback provision," which means that we can recover incentive compensation paid during the Capital Purchase Program Covered Period that is later found to have been paid based on materially inaccurate financial statements or other materially inaccurate measurements of performance.

No Compensation Arrangements That Encourage Excessive Risks. During the Capital Purchase Program Covered Period, we are not allowed to enter into compensation arrangements that encourage senior executive officers to take "unnecessary and excessive risks that threaten the value" of the Company. Therefore, the Company's Compensation Committee is required to meet at least once a year with our senior risk officers to review our executive compensation arrangements in light of our risk management policies and practices. Our senior executive officers' written agreements include their obligation to accept any changes in our incentive compensation arrangements resulting from the Compensation Committee's review.

Limit on Federal Income Tax Deductions. During the Capital Purchase Program Covered Period, we are not allowed to take federal income tax deductions for compensation paid to senior executive officers in excess of $500,000 per year, with certain exceptions that do not apply to our senior executive officers.

On February 17, 2009, President Obama signed the American Recovery and Reinvestment Act of 2009 (the "Stimulus Act") into law. The Stimulus Act modified the compensation-related limitations contained in the Capital Purchase Program and created additional compensation-related limitations. The limitations in the Stimulus Act apply to all participants in the Troubled Asset Relief Program (under which the Capital Purchase Program was created), regardless of when participation commenced. Thus, the newly enacted compensation-related limitations are applicable to the Company, subject to the Treasury Department's issuance of implementing regulations. The compensation-related limitations applicable to the Company which have been added or modified by the Stimulus Act are as follows:

No Severance Payments. Under the Stimulus Act, the definition of "golden parachute" was expanded to include any severance payment resulting from termination of employment, except for payments for services performed or benefits accrued. In addition, the Stimulus Act expanded the group of employees to which such restrictions apply. Consequently, under the Stimulus Act, we are prohibited from making any severance payment to our "senior executive officers" (defined in the Stimulus Act as the five highest paid senior executive officers) and our next five most highly compensated employees during the Capital Purchase Program Covered Period.

Recovery of Incentive Compensation if Based on Certain Material Inaccuracies. The Stimulus Act also contains the "clawback provision" discussed above, but extends its application to our next 20 most highly compensated employees.

No Compensation Arrangements That Encourage Earnings Manipulation. In addition to the Capital Purchase Program prohibition on compensation arrangements that encourage unnecessary and excessive risk, the Stimulus Act prohibits us during the Capital Purchase Program Covered Period from entering into compensation arrangements that encourage manipulation of reported earnings to enhance the compensation of any of our employees.

Limit on Incentive Compensation. The Stimulus Act contains a provision that prohibits the payment or accrual of any bonus, retention award or incentive compensation to any of our senior executive officers during the Capital Purchase Program Covered Period, other than awards of long-term restricted stock that (i) do not fully vest during the Capital Purchase Program Covered Period, (ii) have a value not greater than one-third of the total annual compensation of the awardee and (iii) are subject to such other restrictions as determined by the Secretary

of the Treasury. The prohibition on bonus, incentive compensation and retention awards does not preclude payments required under written employment contracts entered into on, or prior to, February 11, 2009.

Compensation and Human Resources Committee Functions. The Stimulus Act requires that our Compensation Committee be comprised solely of independent directors and that it meet at least semiannually to discuss and evaluate our employee compensation plans in light of an assessment of any risk posed to us from such compensation plans.

Compliance Certifications. The Stimulus Act also requires a written certification by our Chief Executive Officer and Chief Financial Officer of our compliance with the provisions of the Stimulus Act. These certifications are contained in this Annual Report on Form 10-K.

Treasury Review of Excessive Bonuses Previously Paid. The Stimulus Act directs the Secretary of the Treasury to review all compensation paid to our senior executive officers and the next 20 most highly compensated employees prior to adoption of the Stimulus Act to determine whether any such payments were inconsistent with the purposes of the Capital Purchase Program or the Stimulus Act or were otherwise contrary to the public interest. If the Secretary of the Treasury makes such a finding, the Secretary of the Treasury is directed to negotiate with the Capital Purchase Program recipient and the employee recipient for appropriate reimbursements to the federal government with respect to the compensation.

Say on Pay. Under the Stimulus Act, during the Capital Purchase Program Covered Period, we must include in the proxy statement for our annual meeting of shareholders a non-binding say on pay vote by the shareholders on executive compensation.

Limitation on Luxury Expenditures. The Stimulus Act required us to adopt a company-wide policy regarding excessive or luxury expenditures, such as entertainment expenses, office or facility renovation expenses and transportation services expenses.

Supervision and Regulation of the Bank

Federal banking regulations applicable to all depository financial institutions, among other things: (i) provide federal bank regulatory agencies with powers to prevent unsafe and unsound banking practices; (ii) restrict preferential loans by banks to “insiders” of banks; (iii) require banks to keep information on loans to major shareholders and executive officers and (iv) bar certain director and officer interlocks between financial institutions.

As a state-chartered bank, the Bank is subject to the provisions of the North Carolina banking statutes and to regulation by the Commissioner. The Commissioner has a wide range of regulatory authority over the activities and operations of the Bank, and the Commissioner’s staff conducts periodic examinations of the Bank and its affiliates to ensure compliance with state banking regulations. Among other things, the Commissioner regulates the merger and consolidation of state-chartered banks, the payment of dividends, loans to officers and directors, recordkeeping, types and amounts of loans and investments, and the establishment of branches. The Commissioner also has cease and desist powers over state-chartered banks for violations of state banking laws or regulations and for unsafe or unsound conduct that is likely to jeopardize the interest of depositors.

The dividends that may be paid by the Bank to the Company are subject to legal limitations under North Carolina law. In addition, regulatory authorities may restrict dividends that may be paid by the Bank or the Company’s other subsidiaries. The ability of the Company to pay dividends to its shareholders is largely dependent on the dividends paid to the Company by the Bank.

The Bank is a member of the FDIC, which currently insures the deposits of member banks. For this protection, each member bank pays a quarterly statutory assessment, based on its level of deposits, and is subject

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to the rules and regulations of the FDIC. In the years leading up to 2006, due to the funded status of the insurance fund, the FDIC did not assess the Bank any insurance premiums. However, in late 2006 the FDIC adopted new regulations that resulted in all financial institutions, including the Bank, being assessed deposit insurance premiums ranging from 5 cents to 43 cents per $100 of assessable deposits beginning in 2007. The amount of the assessment within that range was based on risk factors that were established by the FDIC. Based on the specified risk factors, for 2007 and 2008, the Bank was assigned an assessment rate of 5.1 cents per $100 of assessable deposits, which resulted in annual insurance premium expense to the Bank of approximately $932,000 in 2007. However, as part of the 2006 legislation that created the new assessment schedule, the rules provided credits to certain institutions that paid deposit insurance premiums in years prior to 1996. As a result, the Bank received a one-time credit of $832,000 that was used to offset FDIC insurance premiums in 2007, which left the Bank with an actual expense of $100,000 in 2007. The Bank had no credit to apply in 2008, and the Company incurred approximately $1.2 million in deposit insurance premium expense during 2008.

On December 16, 2008, the FDIC raised the deposit insurance assessment rates uniformly for all institutions by 7 cents for every $100 of domestic deposits effective for the first quarter of 2009. On February 27, 2009, the FDIC announced that, commencing in April 2009, its minimum rates would increase to a range of twelve cents to sixteen cents per $100 in deposits. During 2009, we recorded approximately $3.9 million in annual FDIC insurance premium expense (excluding the special assessment discussed below).

The FDIC also announced on February 27, 2009 an interim rule that imposed a one-time special assessment of seven cents per $100 in insured deposits to be collected on September 30, 2009, which resulted in a $1.6 million expense for the Bank that was recorded in the second quarter of 2009 and paid on September 30, 2009. The interim rule also permits the FDIC to impose emergency special assessments from time to time after June 30, 2009 if the FDIC board believes the deposit insurance fund will fall to a level that would adversely affect public confidence in federal deposit insurance. To date, the FDIC has not imposed additional special assessments, but the FDIC did require banks to prepay their estimated insurance premiums for 2010 through 2012 by December 31, 2009, which resulted in the Bank prepaying approximately $16.9 million in premiums. This prepaid amount will be recorded as expense on our books over the three year period. Our 2010 FDIC expense is expected to be approximately $4.7 million.

In addition to deposit insurance assessments, the FDIC is authorized to collect assessments against insured deposits to be paid to the Finance Corporation (FICO) to service FICO debt incurred in connection with the resolution of the thrift industry crisis in the 1980s. The FICO assessment rate is adjusted quarterly. The average annual assessment rate in 2009 was 1.04 cents per $100 for insured deposits, which resulted in approximately $243,000 in expense for the Bank for 2009. For the first quarter of 2010, the FICO assessment rate for such deposits will increase to 1.06 cents per $100 of insured deposits, which is expected to result in expense of approximately $309,000 in 2010.

Pursuant to EESA, the maximum deposit insurance amount per depositor has been increased from $100,000 to $250,000 until December 31, 2013. Additionally, in 2008, regulatory authorities enacted legislation that enabled the FDIC to establish its Temporary Liquidity Guarantee Program (“TLGP”). The TGLP had two primary components – 1) a transaction account guarantee program, and 2) a debt guarantee program. Under the transaction account guarantee program of the TLGP, the FDIC will fully guarantee, until June 30, 2010, all noninterest-bearing transaction accounts, including NOW accounts with interest rates of 0.5 percent or less and IOLTAs (lawyer trust accounts). Under the debt guarantee program, the FDIC will guarantee certain senior unsecured debt of insured depository institutions, or their qualified holding companies, issued between October 14, 2008 and October 31, 2009. After an initial phase-in period, both programs became elective options for banks during 2009. We elected to participate in both programs, although we did not utilize the debt guarantee program, which has now expired as it relates to new issuances of debt. The cost of the transaction account guarantee program has not been significant.

The FDIC is also authorized to approve conversions, mergers, consolidations and assumptions of deposit

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liability transactions between insured banks and uninsured banks or institutions, and to prevent capital or surplus diminution in such transactions if the resulting, continuing, or assumed bank is an insured nonmember bank. In addition, the FDIC monitors the Bank's compliance with several banking statutes, such as the Depository Institution Management Interlocks Act and the Community Reinvestment Act of 1977. The FDIC also conducts periodic examinations of the Bank to assess its compliance with banking laws and regulations, and it has the power to implement changes to, or restrictions on, the Bank's operations if it finds that a violation is occurring or is threatened.

Given the ongoing financial crisis and the current presidential administration, legislation that would affect regulation in the banking industry is introduced in most legislative sessions. Neither the Company nor the Bank can predict what other legislation might be enacted or what other regulations or assessments might be adopted, or if enacted or adopted, the effect thereof on the Bank's operations.

See "Capital Resources and Shareholders' Equity" under Item 7 below for a discussion of regulatory capital requirements.

Available Information

The Company maintains a corporate Internet site at www.FirstBancorp.com, which contains a link within the "Investor Relations" section of the site to each of its filings with the Securities and Exchange Commission, including its annual reports on Form 10-K, its quarterly reports on Form 10-Q, its current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934. These filings are available, free of charge, as soon as reasonably practicable after the Company electronically files such material with, or furnishes it to, the Securities and Exchange Commission. These filings can also be accessed at the Securities and Exchange Commission's website located at www.sec.gov. Information included on the Company's Internet site is not incorporated by reference into this annual report.

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Item 1A. Risk Factors

Difficult market conditions and economic trends have adversely affected our industry and our business.

A general economic downturn began in the latter half of 2007. Dramatic declines in the housing market, with decreasing home prices and increasing delinquencies and foreclosures, have negatively impacted the credit performance of mortgage and construction loans and resulted in significant write-downs of assets by many financial institutions. In addition, the value of real estate collateral supporting many loans has declined and may continue to decline. General downward economic trends, reduced availability of commercial credit and increasing unemployment have negatively impacted the credit performance of commercial and consumer credit, resulting in additional write-downs. We believe that the economic downtrends are largely responsible for the deterioration in loan quality that we experienced in 2008 and 2009, including higher levels of loan charge-offs, higher levels of nonperforming assets, and higher provisions for loan losses. Concerns over the stability of the financial markets and the economy have resulted in decreased lending by financial institutions to their customers and to each other. This market turmoil and tightening of credit has led to increased commercial and consumer delinquencies, lack of confidence, increased market volatility and widespread reduction in general business activity. Financial institutions, including us, have experienced a decrease in access to borrowings. The resulting economic pressure on consumers and businesses and the lack of confidence in the financial markets may adversely affect our business, financial condition, results of operations and stock price.

As a result of the foregoing factors, there is a potential for new federal or state laws and regulations regarding lending and funding practices and liquidity standards, and bank regulatory agencies are expected to be very aggressive in responding to concerns and trends identified in examinations. This increased governmental action may increase our costs and limit our ability to pursue certain business opportunities. The FDIC has increased deposit insurance premiums and assessments to restore its deposit insurance funds. We may be required to pay even higher premiums to the FDIC because financial institution failures resulting from the depressed market conditions are expected to increase.

Our ability to assess the creditworthiness of customers and to estimate the losses inherent in our credit exposure is made more complex by these difficult market and economic conditions. A worsening of these conditions would likely exacerbate the adverse effects of these difficult market and economic conditions on us, our customers and the other financial institutions in our market. As a result, we may experience additional increases in foreclosures, delinquencies and customer bankruptcies, as well as more restricted access to funds.

There can be no assurance that recent legislative and regulatory initiatives to address difficult market and economic conditions will stabilize the U.S. banking system.

The Emergency Economic Stabilization Act of 2008, or EESA, authorized the U.S. Treasury to, among other things, purchase up to $700 billion of mortgages, mortgage-backed securities and certain other financial instruments from financial institutions and their holding companies under a Troubled Asset Relief Program, or TARP. The purpose of the TARP was to restore confidence and stability to the U.S. banking system and to encourage financial institutions to increase their lending to customers and to each other. Under the TARP Capital Purchase Program, the U.S. Treasury invested capital in qualified financial institutions in exchange for senior preferred stock and a warrant to purchase shares of equity securities of the financial institution. The EESA also increased federal deposit insurance on most deposit accounts from $100,000 to $250,000 until December 31, 2013.

The EESA followed, and has been followed by, numerous actions by the Federal Reserve Board, the U.S. Congress, the U.S. Treasury, the FDIC, the SEC and other regulatory authorities seeking to address liquidity and credit issues resulting from the economic downturn that began in 2007. These measures have included homeowner relief that

encourages loan restructuring and modification; the establishment of significant liquidity

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and credit facilities for financial institutions and investment banks; the lowering of the federal funds rate; emergency action against short selling practices; a temporary guaranty program for money market funds; the establishment of a commercial paper funding facility to provide back-stop liquidity to commercial paper issuers; and coordinated international efforts to address illiquidity and other weaknesses in the banking sector. The purpose of these legislative and regulatory actions is to stabilize the U.S. banking system.

The EESA and the other regulatory initiatives described above may not have their desired effects. If the volatility in the markets continues and economic conditions fail to improve or worsen, our business, financial condition and results of operations could be materially and adversely affected.

We are vulnerable to the economic conditions within the fairly small geographic region in which we operate.

Like many businesses, our overall success is partially dependent on the economic conditions in the marketplace where we operate. Our marketplace is predominately concentrated in the central Piedmont and coastal regions of North Carolina. As is the case for most of the country, these regions are currently experiencing recessionary economic conditions, which we believe is a factor in our increases in borrower delinquencies, nonperforming assets, and loan losses during 2009 compared to recent prior years. If economic conditions in our marketplace worsen, it could have an adverse impact on us. In particular, if economic conditions related to real estate values in our marketplace were to worsen, our loan losses would likely increase. At December 31, 2009, approximately 90% of our loans were secured by real estate collateral, which means that additional decreases in real estate values could have an adverse impact on our operations.

Current levels of unprecedented market volatility may adversely affect the market value of our common stock.

The capital and credit markets have been experiencing volatility and disruption for more than a year. In some cases, the markets have produced downward pressure on stock prices for certain companies without regard to those companies' underlying financial strength. We believe this is the case with our common stock as our stock price has ranged from a low of $6.87 in March 2009 to a high of $19.00 in September 2009.

The market value of our stock may also be affected by conditions affecting the financial markets generally, including price and trading fluctuations. These conditions may result in (i) volatility in the level of, and fluctuations in, the market prices of stocks generally and, in turn, our stock and (ii) sales of substantial amounts of our stock in the market, in each case that could be unrelated or disproportionate to changes in our operating performance. These broad market fluctuations may adversely affect the market value of our stock.

If our goodwill becomes impaired, we may be required to record a significant charge to earnings.

Under generally accepted accounting principles, goodwill is required to be tested for impairment at least annually and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. The test for goodwill impairment involves comparing the fair value of a company's reporting units to their respective carrying values. For our company, our community banking operation is our only material reporting unit. The price of our common stock is one of several measures available for estimating the fair value of our community banking operations. For much of 2009, the stock market value of our common stock traded below the book value of our company. Subject to the results of other valuation techniques, if this situation persists or worsens, this could indicate that our next test of goodwill will result in a determination that there is impairment. We may be required to record a significant charge to earnings in our financial statements during the period in which any impairment of our goodwill is determined, which could have a negative impact on our results of operations.

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We might be required to raise additional capital in the future, but that capital may not be available or may not be available on terms acceptable to us when it is needed.

We are required to maintain adequate capital levels to support our operations. In the future, we might need to raise additional capital to support growth or absorb loan losses. Our access to capital markets (excluding the Capital Purchase Program) has remained limited for most of the past two years. Our ability to raise additional capital will depend on conditions in the capital markets at that time, which are outside our control, and on our financial performance. Accordingly, we cannot be certain of our ability to raise additional capital in the future if needed or on terms acceptable to us. If we cannot raise additional capital when needed, our ability to conduct our business could be materially impaired.

The soundness of other financial institutions could adversely affect us.

Since the middle of 2007, the financial services industry as a whole, as well as the securities markets generally, have been materially adversely affected by substantial declines in the values of nearly all asset classes and by a significant lack of liquidity. Financial institutions in particular have been subject to increased volatility and an overall loss in investor confidence. Our ability to engage in routine funding transactions could be adversely affected by the actions and commercial soundness of other financial institutions. Financial services companies are interrelated as a result of trading, clearing, counterparty or other relationships. We have exposure to many different industries and counterparties, and we routinely execute transactions with counterparties in the financial services industry, including brokers and dealers, commercial banks, and investment banks. Defaults by, or even rumors or questions about, one or more financial services companies, or the financial services industry generally, have led to market-wide liquidity problems and could lead to losses or defaults by us or by other institutions. We can make no assurance that any such losses would not materially and adversely affect our business, financial condition or results of operations.

We are subject to extensive regulation, which could have an adverse effect on our operations.

We are subject to extensive regulation and supervision from the North Carolina Commissioner of Banks, the FDIC, and the Federal Reserve Board. This regulation and supervision is intended primarily for the protection of the FDIC insurance fund and our depositors and borrowers, rather than for holders of our equity securities. In the past, our business has been materially affected by these regulations. This trend is likely to continue in the future. As an example, the Federal Reserve Board has amended Regulation E, which implements the Electronic Fund Transfer Act, and the official staff commentary to the regulation, which interprets the requirements of Regulation E. The amended regulation limits the ability of a financial institution to assess an overdraft fee for paying automated teller machine (ATM) and one-time debit card transactions that overdraw a consumer's account, unless the consumer affirmatively consents, or opts in, to the institution's payment of overdrafts for these transactions. The rule has a mandatory compliance date of July 1, 2010 for new accounts and August 15, 2010 for existing accounts. We believe that implementation of the new provisions will result in the reduction of overdraft fees collected.

Regulatory authorities have extensive discretion in their supervisory and enforcement activities, including the imposition of restrictions on operations, the classification of our assets and determination of the level of the allowance for loan losses. Changes in the regulations that apply to us, or changes in our compliance with regulations, could have a material impact on our operations.

Additionally, the documents that we executed with the Treasury when they purchased the Series A preferred stock allow the Treasury to unilaterally change the terms of the Series A preferred stock or impose additional requirements on us if there is a change in law. For example, the Stimulus Act imposed executive compensation restrictions that went beyond those imposed by the terms of the Capital Purchase Program. Additional changes or requirements could restrict our ability to conduct business, could subject us to additional cost and expense or

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could change the terms of the senior preferred stock agreement to the detriment of our common shareholders. While it may be possible for us to redeem the senior preferred stock in the event the Treasury imposes any changes or additional requirements that we believe are detrimental, there can be no assurances that our federal regulator will approve such redemption (as is required by law) or that we will have the ability to implement such redemption.

Because of our participation in the Capital Purchase Program, we are subject to restrictions on our ability to declare or pay dividends and repurchase our shares as well as restrictions on compensation paid to our executive officers.

Pursuant to the terms of the securities purchase agreement between our company and the U.S. Treasury, our ability to declare or pay dividends on any of our shares is limited. Specifically, we are unable to declare dividend payments on common stock if we are in arrears on the payment of dividends on the Series A preferred stock issued to the U.S. Treasury. Further, until January 9, 2012, we are not permitted to increase dividends on our common stock above the amount of the last quarterly cash dividend per share declared prior to October 14, 2008 ($0.19 per share) without the U.S. Treasury's approval unless all of the shares of Series A preferred stock have been redeemed or transferred by the U.S. Treasury to unaffiliated third parties.

In addition, our ability to repurchase our shares is restricted. The consent of the U.S. Treasury generally is required for us to make any stock repurchase (other than in connection with the administration of any employee benefit plan in the ordinary course of business and consistent with past practice) until January 9, 2012, unless all of the shares of Series A preferred stock have been redeemed or transferred by the U.S. Treasury to unaffiliated third parties. Further, we may not repurchase any shares of our common stock if we are in arrears on the payment of Series A preferred stock dividends.

In addition, pursuant to the terms of the securities purchase agreement between our company and the U.S. Treasury, we agreed to adhere to the U.S. Treasury's standards for executive compensation and corporate governance for the period during which the U.S. Treasury holds the equity securities issued pursuant to the agreement, including the shares of common stock which may be issued upon exercise of the warrant. The EESA that was signed into law on February 17, 2009 contains additional restrictions on executive compensation and standards of corporate governance that go beyond those in the securities purchase agreement. See the section above entitled "U.S. Treasury Capital Purchase Program" for additional discussion of this matter.

We are subject to interest rate risk, which could negatively impact earnings.

Net interest income is the most significant component of our earnings. Our net interest income results from the difference between the yields we earn on our interest-earning assets, primarily loans and investments, and the rates that we pay on our interest-bearing liabilities, primarily deposits and borrowings. When interest rates change, the yields we earn on our interest-earning assets and the rates we pay on our interest-bearing liabilities do not necessarily move in tandem with each other because of the difference between their maturities and repricing characteristics. This mismatch can negatively impact net interest income if the margin between yields earned and rates paid narrows. Interest rate environment changes can occur at any time and are affected by many factors that are outside our control, including inflation, recession, unemployment trends, the Federal Reserve's monetary policy, domestic and international disorder and instability in domestic and foreign financial markets.

Our allowance for loan losses may not be adequate to cover actual losses.

Like all financial institutions, we maintain an allowance for loan losses to provide for probable losses caused by customer loan defaults. The allowance for loan losses may not be adequate to cover actual loan losses, and in this case additional and larger provisions for loan losses would be required to replenish the allowance. Provisions for loan losses are a direct charge against income.

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We establish the amount of the allowance for loan losses based on historical loss rates, as well as estimates and assumptions about future events. Because of the extensive use of estimates and assumptions, our actual loan losses could differ, possibly significantly, from our estimate. We believe that our allowance for loan losses is adequate to provide for probable losses, but it is possible that the allowance for loan losses will need to be increased for credit reasons or that regulators will require us to increase this allowance. Either of these occurrences could materially and adversely affect our earnings and profitability.

The value of our investment securities portfolio may be negatively affected by continued disruptions in the securities markets.

The market for some of the investment securities held in our portfolio has become volatile over the past twelve months. The continuing volatility of securities markets could detrimentally affect the value of our investment securities, including reduced valuations due to the perception of heightened credit and liquidity risks. We can make no assurance that declines in market value related to disruptions in the securities markets will not result in other than temporary impairment of these assets, which would lead to accounting charges that could have a material adverse effect on our net income and capital levels.

In the normal course of business, we process large volumes of transactions involving millions of dollars. If our internal controls fail to work as expected, if our systems are used in an unauthorized manner, or if our employees subvert our internal controls, we could experience significant losses.

We process large volumes of transactions on a daily basis and are exposed to numerous types of operational risk. Operational risk includes the risk of fraud by persons inside or outside the Company, the execution of unauthorized transactions by employees, errors relating to transaction processing and systems and breaches of the internal control system and compliance requirements. This risk also includes potential legal actions that could arise as a result of an operational deficiency or as a result of noncompliance with applicable regulatory standards.

We establish and maintain systems of internal operational controls that provide us with timely and accurate information about our level of operational risk. Although not foolproof, these systems have been designed to manage operational risk at appropriate, cost-effective levels. Procedures exist that are designed to ensure that policies relating to conduct, ethics, and business practices are followed. From time to time, losses from operational risk may occur, including the effects of operational errors. We continually monitor and improve our internal controls, data processing systems, and corporate-wide processes and procedures, but there can be no assurance that future losses will not occur.

There can be no assurance that we will continue to pay cash dividends.

Although we have historically paid cash dividends, there is no assurance that we will continue to pay cash dividends. Future payment of cash dividends, if any, will be at the discretion of our board of directors and will be dependent upon our financial condition, results of operations, capital requirements, economic conditions, and such other factors as the board may deem relevant. As a result of the board of directors' consideration of these factors, beginning in the first quarter of 2009, our board of directors declared a quarterly dividend of $0.08 per share, which was a decrease from the previous rate of $0.19 per share. The board of directors declared a quarterly dividend of $0.08 per share for each quarter in 2009.

As a result of our participation in the Capital Purchase Program, the Treasury's consent will be required for any dividends paid to common stockholders above a quarterly dividend rate of $0.19 per common share until January 9, 2012, unless prior to then the Series A preferred shares are redeemed in whole or the Treasury has transferred all of these shares to third parties. Also, in the event that we do not pay dividends due on the Series A preferred stock, we are prohibited from paying dividends on our common stock.

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The $67.9 million gain we recorded in connection with the acquisition of Cooperative Bank could be retroactively decreased.

We accounted for the Cooperative Bank acquisition under the purchase method of accounting, recording the acquired assets and liabilities of Cooperative at fair value based on preliminary purchase accounting adjustments. Determining the fair value of assets and liabilities, particularly illiquid assets and liabilities, is a complicated process involving a significant amount of judgment regarding estimates and assumptions. Based on the preliminary adjustments made, the fair value of the assets we acquired exceeded the fair value of the liabilities assumed by $53.8 million, which resulted in a gain for our Company. During the third and fourth quarters of 2009, we obtained third-party appraisals for the majority of Cooperative's collateral dependent problem loans. Overall, the appraised values were higher than our original estimates made as of the acquisition date. In addition, during the third and fourth quarters, we received payoffs related to certain loans for which losses had been anticipated. Accordingly, as required by relevant accounting rules, we retrospectively adjusted the fair value of the loans acquired for these factors, which resulted in the gain being adjusted upward to $67.9 million.

Under purchase accounting, we have until one year after the acquisition to finalize the fair value adjustments, meaning that until then we could materially adjust the fair value estimates of Cooperative's assets and liabilities based on new or updated information. Such adjustments could reduce or eliminate the extent by which the assets acquired exceeded the liabilities assumed and would result in a retroactive decrease to the $67.9 million gain.

Item 1B. Unresolved Staff Comments

None

Item 2. Properties

The main offices of the Company and the Bank are owned by the Bank and are located in a three-story building in the central business district of Troy, North Carolina. The building houses administrative and bank teller facilities. The Bank's Operations Division, including customer accounting functions, offices and operations of Montgomery Data, and offices for loan operations, are housed in two one-story steel frame buildings approximately one-half mile west of the main office. Both of these buildings are owned by the Bank. The Company operates 91 bank branches. Except as discussed below, the Company owns all of its bank branch premises except eight branch offices for which the land and buildings are leased and eight branch offices for which the land is leased but the building is owned. The Company also leases one loan production office.

In addition to the aforementioned leases, the Company is also temporarily renting 19 branch facilities from the FDIC related to the Cooperative acquisition. As provided by the purchase and assumption agreement with the FDIC, the Company had the option to purchase these facilities from the FDIC at a date following the transaction. The Company has committed to purchase these properties at an aggregate purchase price of $14.7 million and expects the purchase to occur in the second quarter of 2010. There are no other options to purchase or lease additional properties. The Company considers its facilities adequate to meet current needs and believes that lease renewals or replacement properties can be acquired as necessary to meet future needs.

Item 3. Legal Proceedings

Various legal proceedings may arise in the ordinary course of business and may be pending or threatened against the Company and its subsidiaries. However, neither the Company nor any of its subsidiaries is involved in any pending legal proceedings that management believes could have a material effect on the consolidated financial position of the Company.

There were no tax shelter penalties assessed by the Internal Revenue Service against the Company during the

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year ended December 31, 2009.

PART II

Item 5. Market for the Registrant's Common Stock, Related Shareholder Matters, and Issuer Purchases of Equity Securities

The Company's common stock trades on The NASDAQ Global Select Market under the symbol FBNC. Table 22, included in "Management's Discussion and Analysis" below, sets forth the high and low market prices of the Company's common stock as traded by the brokerage firms that maintain a market in the Company's common stock and the dividends declared for the periods indicated. On March 6, 2009, the Company announced that because of the challenging economic environment and a desire to conserve capital, it would declare a cash dividend of $0.08 per share for the first quarter of 2009, which was a reduction from the previous dividend rate of $0.19 per share. The Company paid cash dividends of $0.08 per share for each quarter of 2009. For the foreseeable future, it is the Company's current intention to continue to pay cash dividends of $0.08 per share on a quarterly basis. Under the terms of the Company's participation in the U.S. Treasury's Capital Purchase Program, until January 9, 2012, the Company cannot declare a quarterly cash dividend exceeding $0.19 per share without the prior approval of the Treasury. See "Business - Supervision and Regulation" above and Note 15 to the consolidated financial statements for a discussion of other regulatory restrictions on the Company's payment of dividends. As of December 31, 2009, there were approximately 2,700 shareholders of record and another 4,200 shareholders whose stock is held in "street name." There were no sales of unregistered securities during the year ended December 31, 2009.

Additional Information Regarding the Registrant's Equity Compensation Plans

At December 31, 2009, the Company had four equity-based compensation plans, one of which was assumed in a corporate acquisition. The Company's 2007 Equity Plan is the only one of the four plans under which new grants of equity-based awards are possible.

The following table presents information as of December 31, 2009 regarding shares of the Company's stock that may be issued pursuant to the Company's equity based compensation plans. The table does not include information with respect to shares subject to outstanding options granted under a stock incentive plan assumed by the Company in connection with the acquisition of the company that originally granted those options. Footnote (2) to the table indicates the total number of shares of common stock issuable upon the exercise of options under the assumed plan as of December 31, 2009, and the weighted average exercise price of those options. No additional options may be granted under the assumed plan. At December 31, 2009, the Company had no warrants or stock appreciation rights outstanding under any compensation plans.

	As of December 31, 2009		
	(a)	(b)	(c)
Plan category	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities available for future issuance under equity compensation plans (excluding securities reflected in

			column (a))
Equity compensation plans approved by security holders (1)	743,828	$ 17.80	864,941
Equity compensation plans not approved by security holders			
Total (2)	743,828	$ 17.80	864,941

(1) Consists of (A) the Company's 2007 Equity Plan, which is currently in effect; (B) the Company's 2004 Stock Option Plan; and (C) the Company's 1994 Stock Option Plan, each of which was approved by our shareholders.

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(2) The table does not include information for stock incentive plans that the Company assumed in connection with mergers and acquisitions of the companies that originally established those plans. As of December 31, 2009, a total of 9,288 shares of common stock were issuable upon exercise under an assumed plan. The weighted average exercise price of those outstanding options is $11.82 per share. No additional options may be granted under the assumed plan.

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Performance Graph

The performance graph shown below compares the Company's cumulative total return to shareholders for the five-year period commencing December 31, 2004 and ending December 31, 2009, with the cumulative total return of the Russell 2000 Index (reflecting overall stock market performance of small-capitalization companies), and an index of banks with between $1 billion and $5 billion in assets, as constructed by SNL Securities, LP (reflecting changes in banking industry stocks). The graph and table assume that $100 was invested on December 31, 2004 in each of the Company's common stock, the Russell 2000 Index, and the SNL Bank Index, and that all dividends were reinvested.

First Bancorp
Comparison of Five-Year Total Return Performances (1)
Five Years Ending December 31, 2009

	Total Return Index Values (1) December 31,					
	2004	2005	2006	2007	2008	2009
First Bancorp	$ 100.00	76.68	85.96	77.18	78.40	61.01
Russell 2000	100.00	104.55	123.76	121.82	80.66	102.58
SNL Index-Banks between $1 billion and $5 billion	100.00	98.29	113.74	82.85	68.72	49.26

Notes:

(1) Total return indices were provided from an independent source, SNL Securities LP, Charlottesville, Virginia, and assume initial investment of $100 on December 31, 2004, reinvestment of dividends, and changes in market values. Total return index numerical values used in this example are for illustrative purposes only.

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Issuer Purchases of Equity Securities

Pursuant to authorizations by the Company's board of directors, the Company has from time to time repurchased shares of common stock in private transactions and in open-market purchases. The most recent board authorization was announced on July 30, 2004 and authorized the repurchase of 375,000 shares of the Company's stock. The Company did not repurchase any shares of its common stock during the quarter ended December 31, 2009. Under the terms of the Company's participation in the U.S. Treasury's Capital Purchase Program, the Treasury's consent is required for any stock repurchases prior to January 9, 2012, unless the Company has redeemed the Series A preferred stock in whole, or the Treasury has transferred all of these shares to third parties.

Issuer Purchases of Equity Securities

Period	Total Number of Shares Purchased (2)	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (1)	Maximum Number of Shares That May Yet Be Purchased Under the Plans or Programs (1)
Month #1 (October 1, 2009 to October 31, 2009)				234,667
Month #2 (November 1, 2009 to November 30, 2009)				234,667
Month #3 (December 1, 2009 to December 31, 2009)				234,667
Total				234,667

Footnotes to the Above Table

(1) All shares available for repurchase are pursuant to publicly announced share repurchase authorizations. On July 30, 2004, the Company announced that its Board of Directors had approved the repurchase of 375,000 shares of the Company's common stock. The repurchase authorization does not have an expiration date. Subject to the restrictions discussed above related to the Company's participation in the U.S. Treasury's Capital Purchase Program, there are no plans or programs the Company has determined to terminate prior to expiration, or under which the Company does not intend to make further purchases.

(2) The table above does not include shares that were used by option holders to satisfy the exercise price of the call options issued by the Company to its employees and directors pursuant to the Company's stock option plans. There were no such exercises during the three months ended December 31, 2009.

Item 6. Selected Consolidated Financial Data

Table 1 on page 60 of this report sets forth the selected consolidated financial data for the Company.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

Management's Discussion and Analysis is intended to assist readers in understanding our results of operations and changes in financial position for the past three years. This review should be read in conjunction with the consolidated

financial statements and accompanying notes beginning on page 77 of this report and the supplemental financial data contained in Tables 1 through 22 included with this discussion and analysis.

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Overview - 2009 Compared to 2008

Net income was significantly higher in 2009 than in 2008 due to a gain that resulted from the Cooperative Bank acquisition in June 2009. Most items of income and expense were higher in 2009 than in 2008 as a result of the Cooperative acquisition. Our provision for loan losses was not impacted by the acquisition, but increased significantly due to deterioration of asset quality, which we believe was primarily caused by the recessionary economic environment, including its unfavorable effect on real estate values.

Financial Highlights ($ in thousands except per share data)		2009		2008		Change	
Earnings							
Net interest income	$	107,096		86,559		23.7	%
Provision for loan losses		20,186		9,880		104.3	%
Noninterest income		89,518		20,657		333.4	%
Noninterest expenses		78,551		62,211		26.3	%
Income before income taxes		97,877		35,125		178.7	%
Income tax expense		37,618		13,120		186.7	%
Net income		60,259		22,005		173.8	%
Preferred stock dividends and accretion		(3,972	)	—			
Net income available to common shareholders	$	56,287		22,005		155.8	%
Net income per common share							
Basic	$	3.38		1.38		144.9	%
Diluted		3.37		1.37		146.0	%
At Year End							
Assets	$	3,545,356		2,750,567		28.9	%
Loans		2,652,865		2,211,315		20.0	%
Deposits		2,933,108		2,074,791		41.4	%
Ratios							
Return on average assets		1.82	%	0.89	%		
Return on average common equity		22.55	%	10.44	%		
Net interest margin (taxable-equivalent)		3.81	%	3.74	%		

The following is a more detailed discussion of our results for 2009 compared to 2008:

For the year ended December 31, 2009, we reported net income available to common shareholders of $56.3 million compared to $22.0 million reported for 2008. Earnings per diluted common share were $3.37 for the year ended December 31, 2009 compared to $1.37 for 2008.

In the second quarter of 2009, we realized a $67.9 million gain related to the acquisition of Cooperative Bank in Wilmington, North Carolina. This gain resulted from the difference between the purchase price and the acquisition-date fair value of the acquired assets and liabilities. The after-tax impact of this gain was $41.1 million, or $2.46 per diluted common share.

We also recorded preferred stock dividends and accretion related to our issuance of preferred stock to the U.S. Treasury, which reduced net income available to common shareholders and earnings per diluted common share. For the year ended December 31, 2009, total preferred stock dividends of $4 million reduced our net income available to common shareholders.

Total assets at December 31, 2009, including the impact of the Cooperative acquisition, amounted to $3.5 billion, 28.9% higher than a year earlier. Total loans at December 31, 2009 amounted to $2.7 billion, a 20.0% increase from a year earlier, and total deposits amounted to $2.9 billion at December 31, 2009, a 41.4% increase

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from a year earlier.

Excluding the effects of the Cooperative acquisition, we experienced a general decline in loans and an increase in deposits during 2009. Excluding the impact of Cooperative, loans declined approximately 4% in 2009. We continue to originate and renew a significant amount of loans each month, but normal paydowns of loans have exceeded new loan growth. Excluding the impact of Cooperative, we experienced deposit growth of approximately 7% in 2009. Additionally, we have steadily lowered our levels of brokered deposits and internet deposits since the Cooperative acquisition. Brokered deposits comprised just 2.6% of total deposits at December 31, 2009, with internet deposits comprising an additional 4.4%.

Net interest income for the year ended December 31, 2009 amounted to $107.1 million, a 23.7% increase from 2008. The increases in net interest income were primarily due to 1) the higher average balances of loans and deposits previously discussed, and 2) a higher net interest margin.

Our net interest margin (tax-equivalent net interest income divided by average earnings assets) for 2009 was 3.81% compared to 3.74% for 2008. During 2009, there were no changes in the interest rates set by the Federal Reserve, and we were able to reprice at lower rates maturing time deposits that had been originated in periods of higher interest rates.

The current economic environment, including its unfavorable effect on real estate values, has resulted in an increase in our loan losses and nonperforming assets, which has led to significantly higher provisions for loan losses. Our provision for loan losses amounted to $20.2 million for 2009 compared to $9.9 million recorded in 2008.

The increases in the provisions for loan losses are solely attributable to our “non-covered” loan portfolio, which excludes loans assumed from Cooperative that are subject to loss share agreements with the FDIC. We do not expect to record any significant loan loss provisions in the foreseeable future related to the loan portfolio acquired from Cooperative because these loans were written down to estimated fair market value in connection with the recording of the acquisition.

Our non-covered nonperforming assets at December 31, 2009 amounted to $92 million compared to $35 million at December 31, 2008. At December 31, 2009, the ratio of non-covered nonperforming assets to total non-covered assets was 3.10% compared to 1.29% at December 31, 2008.

Our ratio of annualized net charge-offs to average non-covered loans was 0.56% for 2009 compared to 0.24% for 2008.

Noninterest income for the year ended December 31, 2009 amounted to $89.5 million compared to $20.7 million for 2008. The primary reason for the increase was the $67.9 million gain realized from the Cooperative acquisition that occurred in June 2009, as discussed above.

Noninterest expenses for the year ended December 31, 2009 amounted to $78.6 million, a 26.3% increase from the $62.2 million recorded in 2008. Incremental operating expenses associated with the Cooperative acquisition were the primary reason for the increases in 2009. Additionally, FDIC insurance expense amounted to $5.5 million for the year ended December 31, 2009, compared to $1.2 million for 2008. Included in the $5.5 million in FDIC insurance expense for 2009 was $1.6 million related to a special assessment that was levied by the FDIC on all banks in the second quarter of 2009. Also, during 2009, we recorded $1.3 million in acquisition related expenses.

Our effective tax rate was 36%-38% for each of the years ended December 31, 2009 and 2008.

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Overview - 2008 Compared to 2007

Net income was approximately 1% higher in 2008 than in 2007, while earnings per share were down 9% due to a higher number of shares of stock outstanding as a result of shares issued in connection with our acquisition of Great Pee Dee Bancorp, Inc. in April 2008. Overall our profitability measures were down in 2008 primarily as a result of a lower net interest margin, higher provision for loan losses, and higher expenses that were associated with our growth.

Financial Highlights ($ in thousands except per share data)		2008		2007		Change	
Earnings							
Net interest income	$	86,559		79,284		9.2	%
Provision for loan losses		9,880		5,217		89.4	%
Noninterest income		20,657		17,217		20.0	%
Noninterest expenses		62,211		56,324		10.5	%
Income before income taxes		35,125		34,960		0.5	%
Income tax expense		13,120		13,150		-0.2	%
Net income	$	22,005		21,810		0.9	%
Net income per share							
Basic	$	1.38		1.52		-9.2	%
Diluted		1.37		1.51		-9.3	%
At Year End							
Assets	$	2,750,567		2,317,249		18.7	%
Loans		2,211,315		1,894,295		16.7	%
Deposits		2,074,791		1,838,277		12.9	%
Ratios							
Return on average assets		0.89	%	1.02	%		
Return on average equity		10.44	%	12.77	%		
Net interest margin (taxable-equivalent)		3.74	%	4.00	%		

The following is a more detailed discussion of our results for 2008 compared to 2007:

Net income for the year ended December 31, 2008 was $22.0 million or $1.37 per diluted share, compared to net income of $21.8 million, or $1.51 per diluted share, reported for 2007, a decrease of 9.3% in earnings per share. The 2008 earnings reflect the impact of the acquisition of Great Pee Dee, which had $211 million in total assets as of the acquisition date, and resulted in the issuance of 2,059,091 shares of First Bancorp common stock.

We experienced strong balance sheet growth in 2008. Total assets at December 31, 2008 amounted to $2.8 billion, 18.7% higher than a year earlier. Total loans at December 31, 2008 amounted to $2.2 billion, a 16.7% increase from a year earlier, and total deposits amounted to $2.1 billion at December 31, 2008, a 12.9% increase from a year earlier. Total shareholders' equity amounted to $219.9 million at December 31, 2008, a 26.3% increase from a year earlier. The high growth rates were impacted by the acquisition of Great Pee Dee on April 1, 2008, which had $184 million in loans, $148 million in deposits, and $211 million in assets on that date.

Net interest income for the year ended December 31, 2008 amounted to $86.6 million, a 9.2% increase from 2007. The increases in net interest income during 2008 were primarily due to growth in loans and deposits.

The impact of the growth in loans and deposits on net interest income was partially offset by a decline in our net interest margin. Our net interest margin for 2008 was 3.74% compared to 4.00% for 2007. Our net interest margin was negatively impacted by the Federal Reserve lowering interest rates by a total of 500 basis points from

September 2007 to December 2008. When interest rates are lowered, our net interest margin declines, at least temporarily, as most of our adjustable rate loans reprice downward immediately, while rates on our customer time deposits are fixed, and thus do not adjust downward until they mature.

Our provision for loan losses for the year ended December 31, 2008 was $9.9 million compared to $5.2 million recorded in 2007. The higher provision in 2008 was primarily related to negative trends in asset quality.

The recessionary economic environment resulted in an increase in our delinquencies and classified assets during 2008. At December 31, 2008, our nonperforming assets were $35.4 million compared to $10.9 million at December 31, 2007. Our nonperforming assets to total assets ratio was 1.29% at December 31, 2008 compared to 0.47% at December 31, 2007. For the year ended December 31, 2008, our ratio of net charge-offs to average loans was 0.24% compared to 0.16% for 2007.

Noninterest income for 2008 amounted to $20.7 million, a 20.0% increase over 2007. The positive variance in noninterest income for the twelve months ended December 31, 2008 primarily related to increases in service charges on deposit accounts. These higher service charges were primarily associated with expanding the availability of our customer overdraft protection program in the fourth quarter of 2007 to include debit card purchases and ATM withdrawals. Previously the overdraft protection program, in which we charge a fee for honoring payments on overdrawn accounts, only applied to written checks.

Noninterest expenses for 2008 amounted to $62.2 million, a 10.5% increase from 2007. This increase was primarily attributable to our growth, including 2008 acquisition of Great Pee Dee. Additionally, we recorded FDIC insurance expense of $1,157,000 for year ended December 31, 2008, compared to $100,000 for 2007, as a result of the FDIC beginning to charge for FDIC insurance again in order to replenish its reserves.

Our effective tax rate was 37%-38% for each of years ended December 31, 2008 and 2007.

Outlook for 2010

We expect the banking industry to continue to face significant challenges in 2010. Economic data remains weak and unemployment rates have hit 30 year highs in much of our market area. While many analysts believe the worst of the national housing market decline is over, the Carolinas and Virginia are thought by some to have been a region that experienced housing declines later than other regions of the country. Thus, our region may not be as far along as other regions as it relates to a housing recovery. Also, many analysts believe that the commercial real estate market may be the next segment of bank loan portfolios to experience heavy losses. Like most banks, we have a significant amount of both residential real estate and commercial real estate loans.

Although we have consistently operated our company in what we believe is a conservative manner and have asset quality ratios that compare favorably to peer ratios, we continue to experience steady increases in our nonperforming assets and our loan losses. For our company, we have not yet seen a lessening, or even a leveling off, of the unfavorable asset quality indicators that we review. Accordingly, until we begin to see tangible signs of recovery, we expect that our provisions for loan losses will continue to be elevated in comparison to historical norms.

Additionally, we expect loan demand to remain at low levels due to economic conditions and depressed real estate values, which we believe will result in a continued decline in our loan portfolio. We also expect deposit growth to be low in 2010. We believe that growth in our deposits that would otherwise occur will be offset by the loss of higher priced maturing deposits that are not renewed at maturity by customers in search of a higher yield. Based on the above factors, we believe that our net interest margin will not vary materially from the net interest margins recently realized.

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We expect legislation regarding fees charged on nonsufficient funds will lower noninterest income in the second half of 2010. In 2010, we expect to realize a modest amount of efficiencies from various internal initiatives, as well as efficiencies related to our Cooperative acquisition, which should result in our level of quarterly noninterest expenses being slightly lower than that realized in the fourth quarter of 2009.

Critical Accounting Policies

The accounting principles we follow and our methods of applying these principles conform with accounting principles generally accepted in the United States of America and with general practices followed by the banking industry. Certain of these principles involve a significant amount of judgment and may involve the use of estimates based on our best assumptions at the time of the estimation. The allowance for loan losses, intangible assets, and the valuation of acquired assets are three policies we have identified as being more sensitive in terms of judgments and estimates, taking into account their overall potential impact to our consolidated financial statements.

Allowance for Loan Losses

Due to the estimation process and the potential materiality of the amounts involved, we have identified the accounting for the allowance for loan losses and the related provision for loan losses as an accounting policy critical to our consolidated financial statements. The provision for loan losses charged to operations is an amount sufficient to bring the allowance for loan losses to an estimated balance considered adequate to absorb losses inherent in the portfolio.

Our determination of the adequacy of the allowance is based primarily on a mathematical model that estimates the appropriate allowance for loan losses. This model has two components. The first component involves the estimation of losses on loans defined as “impaired loans.” A loan is considered to be impaired when, based on current information and events, it is probable we will be unable to collect all amounts due according to the contractual terms of the loan agreement. The estimated valuation allowance is the difference, if any, between the loan balance outstanding and the value of the impaired loan as determined by either 1) an estimate of the cash flows that we expect to receive from the borrower discounted at the loan’s effective rate, or 2) in the case of a collateral-dependent loan, the fair value of the collateral.

The second component of the allowance model is an estimate of losses for all loans not considered to be impaired loans. Loans that we have classified as having normal credit risk are segregated by loan type, and estimated loss percentages are assigned to each loan type, based on the historical losses, current economic conditions, and operational conditions specific to each loan type. Loans that we have risk graded as having more than “standard” risk but not considered to be impaired are segregated between those relationships with outstanding balances exceeding $500,000 and those that are less than that amount. For those loan relationships with outstanding balances exceeding $500,000, we review the attributes of each individual loan and assign any necessary loss reserve based on various factors including payment history, borrower strength, collateral value, and guarantor strength. For loan relationships less than $500,000 with more than standard risk but not considered to be impaired, loss percentages are based on a multiple of the estimated loss rate for loans of a similar loan type with normal risk. The multiples assigned vary by type of loan, depending on risk, and we have consulted with an external credit review firm in assigning those multiples.

The reserve estimated for impaired loans is then added to the reserve estimated for all other loans. This becomes our “allocated allowance.” In addition to the allocated allowance derived from the model, we also evaluate other data such as the ratio of the allowance for loan losses to total loans, net loan growth information, nonperforming asset levels and trends in such data. Based on this additional analysis, we may determine that an additional amount of allowance for loan losses is necessary to reserve for probable losses. This additional amount, if any, is our “unallocated allowance.” The sum of the allocated allowance and the unallocated allowance is compared to the actual allowance for

loan losses recorded on our books and any adjustment

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necessary for the recorded allowance to equal the computed allowance is recorded as a provision for loan losses. The provision for loan losses is a direct charge to earnings in the period recorded.

Loans covered under loss share agreements are recorded at fair value at acquisition date. Therefore, amounts deemed uncollectible at acquisition date become a part of the fair value calculation and are excluded from the allowance for loan losses. Subsequent decreases in the amount expected to be collected result in a provision for loan losses with a corresponding increase in the allowance for loan losses. Subsequent increases in the amount expected to be collected result in a reversal of any previously recorded provision for loan losses and related allowance for loan losses, or prospective adjustment to the accretable yield if no provision for loan losses had been recorded. Proportional adjustments are also recorded to the FDIC receivable under the loss share agreements.

Although we use the best information available to make evaluations, future material adjustments may be necessary if economic, operational, or other conditions change. In addition, various regulatory agencies, as an integral part of their examination process, periodically review our allowance for loan losses. Such agencies may require us to recognize additions to the allowance based on the examiners' judgment about information available to them at the time of their examinations.

For further discussion, see "Nonperforming Assets" and "Summary of Loan Loss Experience" below.

Intangible Assets

Due to the estimation process and the potential materiality of the amounts involved, we have also identified the accounting for intangible assets as an accounting policy critical to our consolidated financial statements.

When we complete an acquisition transaction, the excess of the purchase price over the amount by which the fair market value of assets acquired exceeds the fair market value of liabilities assumed represents an intangible asset. We must then determine the identifiable portions of the intangible asset, with any remaining amount classified as goodwill. Identifiable intangible assets associated with these acquisitions are generally amortized over the estimated life of the related asset, whereas goodwill is tested annually for impairment, but not systematically amortized. Assuming no goodwill impairment, it is beneficial to our future earnings to have a lower amount assigned to identifiable intangible assets and higher amount of goodwill as opposed to having a higher amount considered to be identifiable intangible assets and a lower amount classified as goodwill.

The primary identifiable intangible asset we typically record in connection with a whole bank or bank branch acquisition is the value of the core deposit intangible, whereas when we acquire an insurance agency, the primary identifiable intangible asset is the value of the acquired customer list. Determining the amount of identifiable intangible assets and their average lives involves multiple assumptions and estimates and is typically determined by performing a discounted cash flow analysis, which involves a combination of any or all of the following assumptions: customer attrition/runoff, alternative funding costs, deposit servicing costs, and discount rates. We typically engage a third party consultant to assist in each analysis. For the whole bank and bank branch transactions recorded to date, the core deposit intangibles have generally been estimated to have a life ranging from seven to ten years, with an accelerated rate of amortization. For insurance agency acquisitions, the identifiable intangible assets related to the customer lists were determined to have a life of ten to fifteen years, with amortization occurring on a straight-line basis.

Subsequent to the initial recording of the identifiable intangible assets and goodwill, we amortize the identifiable intangible assets over their estimated average lives, as discussed above. In addition, on at least an annual basis, goodwill is evaluated for impairment by comparing the fair value of our reporting units to their related carrying value, including goodwill (our community banking operation is our only material reporting unit). At our last evaluation, the

fair value of our community banking operation exceeded its carrying value, including goodwill. If the carrying value of a reporting unit were ever to exceed its fair value, we would determine whether

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the implied fair value of the goodwill, using a discounted cash flow analysis, exceeded the carrying value of the goodwill. If the carrying value of the goodwill exceeded the implied fair value of the goodwill, an impairment loss would be recorded in an amount equal to that excess. Performing such a discounted cash flow analysis would involve the significant use of estimates and assumptions.

We review identifiable intangible assets for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Our policy is that an impairment loss is recognized, equal to the difference between the asset's carrying amount and its fair value, if the sum of the expected undiscounted future cash flows is less than the carrying amount of the asset. Estimating future cash flows involves the use of multiple estimates and assumptions, such as those listed above.

Fair Value and Discount Accretion of Acquired Loans

We consider that the determination of the initial fair value of loans acquired in the June 19, 2009, FDIC-assisted transaction, the initial fair value of the related FDIC loss share receivable, and the subsequent discount accretion of the purchased loans to involve a high degree of judgment and complexity. The carrying value of the acquired loans and the FDIC loss share receivable reflect management's best estimate of the amount to be realized on each of these assets. We determined current fair value accounting estimates of the assumed assets and liabilities in accordance with the Financial Accounting Standard Board's (FASB) Accounting Standard Codification (ASC) 805 "Business Combinations." However, the amount that we realize on these assets could differ materially from the carrying value reflected in our financial statements, based upon the timing of collections on the acquired loans in future periods. To the extent the actual values realized for the acquired loans are different from the estimates, the FDIC loss share receivable will generally be impacted in an offsetting manner due to the loss-sharing support from the FDIC.

Because of the inherent credit losses associated with the acquired loans, the amount that we recorded as the fair values for the loans was less than the contractual unpaid principal balance due from the borrowers, with the difference being referred to as the "discount" on the acquired loans. For the acquired loans that were impaired on the date of acquisition, we are applying the guidance in ASC 310-30 (originally issued as AICPA Statement of Position No. 03-3, "Accounting for Certain Loans or Debt Securities Acquired in a Transfer") in accounting for the discount. We have initially applied the cost recovery method permitted by ASC 310-30 to all purchased impaired loans due to the uncertainty as to the timing of expected cash flows. This will result in the recognition of interest income on these impaired loans only when the cash payments received from the borrower exceed the recorded net book value of the related loans.

For nonimpaired purchased loans, we have also elected to apply ASC 310-30 in the accounting for the accretion of the discount. We are accreting the discount for these loans based on the expected cash flows of the loans.

Merger and Acquisition Activity

We completed the following acquisitions during 2008 and 2009 (none in 2007). The results of each acquired company/branch are included in our financial statements beginning on their respective acquisition dates.

(a) On April 1, 2008, we completed the acquisition of Great Pee Dee Bancorp, Inc. (Great Pee Dee). Great Pee Dee was the parent company of Sentry Bank and Trust (Sentry), a South Carolina community bank with one branch in Florence, South Carolina and two branches in Cheraw, South Carolina. Great Pee Dee had $211 million in total assets as of the date of acquisition. This acquisition represented a natural extension of our market area, with Sentry's Cheraw offices being in close proximity to our Rockingham, North Carolina branch and Sentry's Florence office being in close proximity to our existing branches in Dillon and Latta, South Carolina. Our primary reason for the acquisition was to expand into a contiguous market with facilities, operations and experienced staff in place. The terms of the agreement called for shareholders of Great Pee Dee to receive 1.15

shares of First Bancorp stock for each share of Great Pee Dee stock they owned. The transaction resulted in the issuance of 2,059,091 shares of our common stock that were valued at approximately $37.0 million and the assumption of employee stock options with a fair market value of approximately $0.6 million. The value of the stock issued was determined using a Company stock price of $17.98, which was the average of the daily closing price of our stock for the five trading days closest to the July 12, 2007 announcement of the execution of the definitive merger agreement. The value of the employee stock options assumed was determined using the Black-Scholes option-pricing model. The operating results of Great Pee Dee are included in our financial statements beginning on the April 1, 2008 acquisition date.

As a result of this acquisition, we recorded approximately $847,000 in an intangible asset related to the core deposit base that is being amortized on a straight-line basis over the weighted average life of the core deposit base, which was estimated to be 7.4 years. Additionally, we recorded approximately $16,330,000 in goodwill that is not being systematically amortized, but rather is subject to an annual impairment test. We agreed to a purchase price that resulted in recognition of goodwill primarily due to the reasons noted above, as well as the generally positive earnings of Great Pee Dee.

(b) On June 19, 2009, we announced that First Bank, our banking subsidiary, had entered into a purchase and assumption agreement with the Federal Deposit Insurance Corporation (FDIC), as receiver for Cooperative Bank, Wilmington, North Carolina. According to the terms of the agreement, First Bank acquired all deposits (except certain brokered deposits) and borrowings, and substantially all of the assets of Cooperative Bank and its subsidiary, Lumina Mortgage. The loans and foreclosed real estate purchased are covered by two loss share agreements between the FDIC and First Bank, which afford First Bank significant loss protection. Under the loss share agreements, the FDIC will cover 80% of covered loan and foreclosed real estate losses up to $303 million and 95% of losses in excess of that amount. The term for loss sharing on residential real estate loans is ten years, while the term for loss sharing on non-residential real estate loans is five years in respect to losses and eight years in respect to loss recoveries. The reimbursable losses from the FDIC are based on the book value of the relevant loan as determined by the FDIC at the date of the transaction.

Cooperative Bank operated through twenty-one branches in North Carolina and three branches in South Carolina, with assets totaling approximately $959 million and approximately 200 employees. This acquisition represented a natural extension of our market area with most of Cooperative's offices being in close proximity to our existing branches in the coastal regions of North and South Carolina.

We received a $123 million discount on the assets acquired and paid no deposit premium, which, after applying estimates of purchase accounting fair market value adjustments to the acquired assets and assumed deposits, resulted in a gain of $67.9 million.

As a result of this acquisition, we recorded approximately $3.8 million in an intangible asset related to the core deposit base that is being amortized on a straight-line basis over the weighted average life of the core deposit base, which was estimated to be 8 years.

See Note 2 and Note 6 to the consolidated financial statements for additional information regarding intangible assets.

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ANALYSIS OF RESULTS OF OPERATIONS

Net interest income, the "spread" between earnings on interest-earning assets and the interest paid on interest-bearing liabilities, constitutes the largest source of our earnings. Other factors that significantly affect operating results are the provision for loan losses, noninterest income such as service fees and noninterest expenses such as salaries, occupancy expense, equipment expense and other overhead costs, as well as the effects of income taxes.

Net Interest Income

Net interest income on a reported basis amounted to $107,096,000 in 2009, $86,559,000 in 2008, and $79,284,000 in 2007. For internal purposes and in the discussion that follows, we evaluate our net interest income on a tax-equivalent basis by adding the tax benefit realized from tax-exempt securities to reported interest income. Net interest income on a tax-equivalent basis amounted to $107,914,000 in 2009, $87,217,000 in 2008, and $79,838,000 in 2007. Management believes that analysis of net interest income on a tax-equivalent basis is useful and appropriate because it allows a comparison of net interest amounts in different periods without taking into account the different mix of taxable versus non-taxable investments that may have existed during those periods. The following is a reconciliation of reported net interest income to tax-equivalent net interest income.

		Year ended December 31,		
($ in thousands)		2009	2008	2007
Net interest income, as reported	$	107,096	86,559	79,284
Tax-equivalent adjustment		818	658	554
Net interest income, tax-equivalent	$	107,914	87,217	79,838

Table 2 analyzes net interest income on a tax-equivalent basis. Our net interest income on a taxable-equivalent basis increased by 23.7% in 2009 and 9.2% in 2008. There are two primary factors that cause changes in the amount of net interest income we record - 1) growth in loans and deposits, and 2) our net interest margin (tax-equivalent net interest income divided by average interest-earning assets). In 2008 and 2009, growth in loans and deposits increased net interest income. In 2008, the positive effects of the growth were partially offset by lower net interest margins, while in 2009, net interest income was enhanced by a slightly higher net interest margin.

Loans outstanding grew by 20.0% and 16.7% in 2009 and 2008, respectively, while deposits increased 41.4% in 2009 and 12.9% in 2008. A majority of the increase in loans and deposits in 2009 and 2008 came as a result of the June 19, 2009 acquisition of Cooperative Bank and the April 1, 2008 acquisition of Great Pee Dee, respectively.

As illustrated in Table 3, this growth positively impacted net interest income in both 2009 and 2008. In both years, the positive impact on net interest income of growth in interest-earning assets, primarily loans, more than offset the higher interest expense associated with funding the asset growth. In 2009, growth in interest-earning assets resulted in an increase in interest income of $25.3 million, while growth in interest-bearing liabilities only resulted in $12.6 million in higher interest expense. In 2008, growth in interest-earning assets resulted in an increase in interest income of $23.2 million, while growth in interest-bearing liabilities only resulted in $11.6 million in higher interest expense. As a result, balance sheet growth resulted in an increase in tax-equivalent net interest income of $12.7 million in 2009 and $11.6 million in 2008.

Table 3 also illustrates the impact that changes in the rates that we earned/paid had on our net interest income in 2008 and 2009. Beginning in late 2007 and throughout 2008, the Federal Reserve reduced interest rates significantly as a result of recessionary economic conditions. For 2008, the lower interest rates resulted in a decrease in our interest income of $24.2 million compared to a decrease in interest expense of only $19.9 million,

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which resulted in a reduction in net interest income of $4.2 million. Thus the declining interest rates negatively impacted net interest income for 2008. In 2009, there were no changes in interest rates set by the Federal Reserve and we were able to reprice maturing time deposits at lower prices. In 2009, the impact of lower interest rates resulted in a reduction of interest expense of $25.0 million, due mostly to the ability to reprice time deposits at lower levels, while our interest income only declined by $17.0 million. Thus, the impact of overall lower rates resulted in an $8.0 million increase in net interest income.

We measure the spread between the yield on our earning assets and the cost of our funding primarily in terms of the ratio entitled “net interest margin” which is defined as tax-equivalent net interest income divided by average earning assets. Our net interest margin increased seven basis points in 2009 to 3.81% after decreasing in 2008 to 3.74% from 4.00% in 2007.

In 2008, our lower net interest margin was caused primarily by the significant decreases in interest rates that the Federal Reserve announced beginning in late 2007 and that continued throughout 2008. From September 2007 to December 2008, the Federal Reserve reduced interest rates by a total of 500 basis points. When interest rates are lowered, our net interest margin declines, at least temporarily, because generally our assets that reprice when interest rates change reprice downward immediately by the full amount of the interest rate change, while most of our liabilities that are subject to adjustment reprice at a lag to the rate change and typically not to the full extent of the rate change. Also, many of our deposit accounts had rates lower than 5.00% prior to the rate cuts, and thus could not be reduced by 500 basis points.

In addition to the negative effects mentioned above, our net interest margin in 2008 was negatively impacted by our deposit growth being concentrated in deposit account types that carry high interest rates. In 2008, we offered higher interest rates on several of our deposit products in order to attract deposits and enhance our liquidity, which was negatively impacted by our acquisition of Great Pee Dee Bancorp, which had $184 million in loans and only $148 million in deposits.

In 2009, our net interest margin improved slightly as the Federal Reserve made no changes to interest rates. As a result, we were able to reprice many of our maturing time deposits, which had been originated in periods of higher interest rates, at lower rates. We were also able to generally decrease the rates we paid on other types of deposits as a result of an increase in deposits and liquidity that lessened our need to offer premium interest rates.

For the reasons discussed above, in 2009 the yields we realized on our interest-earning assets decreased by a smaller amount than did the rates we paid on our interest-bearing liabilities, while conversely, in 2008 the yields we realized on our interest-earning assets decreased by a larger amount than did the rates we paid on our interest-bearing liabilities. As derived from Table 2, in 2009 , the yield realized on average earning assets decreased by only 85 basis points from 2008 (from 6.38% to 5.53%) while the average rate paid on interest-bearing liabilities decreased by 108 basis points (from 3.04% to 1.96%). The difference in these changes in 2009 positively impacted our net interest margin. In comparing 2008 to 2007, the yield realized on average earning assets decreased by 110 basis points (from 7.48% to 6.38%) while the average rate paid on interest-bearing liabilities decreased by only 100 basis points (from 4.04% to 3.04%). The differences in these changes in 2008 negatively impacted our net interest margin.

In addition to the factors noted above, our net interest income in 2008 and 2009 was impacted by certain purchase accounting adjustments related to our acquisitions of Cooperative Bank and Great Pee Dee. In our Cooperative Bank acquisition, we assumed a loan portfolio that had interest rates that were generally consistent with interest rates in our loan portfolio. However, as a result of the efforts to attract deposits and maintain sufficient liquidity in the period prior to the bank’s closing, Cooperative Bank’s time deposits had interest rates that were significantly higher than the existing market rate for time deposits. Accounting regulations required us to record a premium on those deposits and amortize the premium as a reduction to interest expense over the life of the deposit portfolio to reduce the yield on

those deposits to a market rate of interest. In addition, as discussed in “Critical Accounting Policies” above, we are accreting the initial discount recorded on nonimpaired

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Cooperative loans over the expected cash flows of the loans. Less significant interest income and expense purchase accounting adjustments were also recorded in 2008 and 2009 related to our acquisition of Great Pee Dee. The following tables present the purchase accounting adjustments made in 2008 and 2009 that impacted net interest income.

($ in thousands)	Year Ended December 31, 2009		
	Cooperative	Great Pee Dee	Total
Interest income – reduced by premium amortization on loans	$ –	(196)	(196)
Interest income – increased by accretion of loan discount	1,469	–	1,469
Interest expense – reduced by premium amortization of deposits	(3,711)	(200)	(3,911)
Interest expense – reduced by premium amortization of borrowings	–	(464)	(464)
Impact on net interest income	$ 5,180	468	5,648

($ in thousands)	Year Ended December 31, 2008		
	Cooperative	Great Pee Dee	Total
Interest income – reduced by premium amortization on loans	$ –	(147)	(147)
Interest income – increased by accretion of loan discount	–	–	–
Interest expense – reduced by premium amortization of deposits	–	(898)	(898)
Interest expense – reduced by premium amortization of borrowings	–	(347)	(347)
Impact on net interest income	$ –	1,098	1,098

The following table presents the purchase accounting entries that we expect to record in 2010.

	Cooperative	Great Pee Dee	Total
Interest income – reduced by premium amortization on loans	$ –	(147)	(147)
Interest income – increased by accretion of loan discount	See note below	–	–
Interest expense – reduced by premium amortization of deposits	(2,211)	–	(2,211)
Interest expense – reduced by premium amortization of borrowings	–	(338)	(338)
Impact on net interest income	$ 2,211	191	2,402

We cannot determine the amount of interest income, if any, to be recognized from the accretion of the loan discount on Cooperative loans because it is reliant on our ongoing assessment of expected cash flows of the loans, which is impacted by any changes in expected credit losses related to the loans.

See additional information regarding net interest income in the section entitled "Interest Rate Risk."

Provision for Loan Losses

The provision for loan losses charged to operations is an amount sufficient to bring the allowance for loan losses to an estimated balance considered appropriate to absorb probable losses inherent in our loan portfolio. Management's determination of the adequacy of the allowance is based on the level of loan growth, an evaluation of the portfolio, current economic conditions, historical loan loss experience and other risk factors.

The current economic environment which began in late 2007 has resulted in declines in real estate values, and increases in loan delinquencies, loan losses and nonperforming assets, which has led to significantly higher provisions for loan losses. Our provision for loan losses was $20,186,000 in 2009, compared to $9,880,000 in 2008 and $5,217,000 in 2007.

The increases in the provisions for loan losses are solely attributable to our "non-covered" loan portfolio,

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which excludes loans assumed from Cooperative that are subject to the loss share agreement with the FDIC. We do not expect to record any significant loan loss provisions in the foreseeable future related to the loan portfolio acquired from Cooperative because these loans were written down to estimated fair market value in connection with the recording of the acquisition.

Non-covered nonperforming assets at December 31, 2009 amounted to $92 million compared to $35 million and $10 million at December 31, 2008 and 2007, respectively. At December 31, 2009, the ratio of non-covered nonperforming assets to total non-covered assets was 3.10% compared to 1.29% and 0.47% at December 31, 2008 and 2007, respectively.

For the year ended December 31, 2009, the ratio of net charge-offs to average non-covered loans was 0.56% compared to 0.24% for 2008 and 0.16% in 2007.

See the section entitled "Allowance for Loan Losses and Loan Loss Experience" below for a more detailed discussion of the allowance for loan losses. The allowance is monitored and analyzed regularly in conjunction with our loan analysis and grading program, and adjustments are made to maintain an adequate allowance for loan losses.

Noninterest Income

Our noninterest income amounted to $89,518,000 in 2009, $20,657,000 in 2008, and $17,217,000 in 2007.

As shown in Table 4, core noninterest income, which excludes the Cooperative acquisition gain and other miscellaneous gains and losses, amounted to $21,870,000 in 2009, a 6.6% increase from $20,515,000 in 2008. The 2008 core noninterest income of $20,515,000 was 22.6% higher than the $16,740,000 recorded in 2007.

See Table 4 and the following discussion for an understanding of the components of noninterest income.

Service charges on deposit accounts in 2009 amounted to $13,854,000, a 2.4% increase compared to $13,535,000 recorded in 2008. The $13,535,000 recorded in 2008 was 35.5% more than the 2007 amount of $9,988,000. The increase in 2009 can be attributed to a larger customer base as a result of the Cooperative acquisition. The primary reason for the increase in 2008 was the expansion of our overdraft protection program in the fourth quarter of 2007 to include overdraft protection for debit card purchases and ATM withdrawals. Previously the overdraft protection program, in which we charge a fee for honoring payments on overdrawn accounts, only applied to written checks. We expect legislation that will be effective beginning on July 1, 2010 to reduce our fees earned on overdrafts. The legislation prohibits us from charging an overdraft fee for paying automated teller machine (ATM) and one-time debit card transactions that overdraw a consumer's account, unless the consumer affirmatively consents, or opts in, to the institution's payment of overdrafts for these transactions.

Other service charges, commissions and fees amounted to $4,848,000 in 2009, a 10.4% increase from the $4,392,000 earned in 2008. The 2008 amount of $4,392,000 was a 12.6% increase from the $3,902,000 recorded in 2007. This category of noninterest income includes items such as electronic payment processing revenue (which includes fees related to credit card transactions by merchants and customers and fees earned from debit card transactions), ATM charges, safety deposit box rentals, fees from sales of personalized checks, and check cashing fees. The growth in this category for both years was primarily due to the increased acceptance and popularity of debit cards (for which we earn income for each use by our customers) and the overall growth in our total customer base, including growth achieved from corporate acquisitions.

Fees from presold mortgages amounted to $1,505,000 in 2009, $869,000 in 2008, and $1,135,000 in 2007. The increase in fees earned in 2009 was due to the increased mortgage refinance activity due to a favorable interest rate

environment. The decrease in fees earned in 2008 was primarily a result of lower volume caused by the declining market for home sales.

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Commissions from sales of insurance and financial products amounted to $1,524,000 in 2009, $1,552,000 in 2008, and $1,511,000 in 2007. This line item includes commissions we receive from three sources - 1) sales of credit life insurance associated with new loans, 2) commissions from the sales of investment, annuity, and long-term care insurance products, and 3) commissions from the sale of property and casualty insurance. The following table presents the contribution of each of the three sources to the total amount recognized in this line item:

($ in thousands)	2009	2008	2007
Commissions earned from:			
Sales of credit life insurance	$ 281	294	304
Sales of investments, annuities, and long term care insurance	503	474	387
Sales of property and casualty insurance	740	784	820
Total	$ 1,524	1,552	1,511

Data processing fees amounted to $139,000 in 2009, $167,000 in 2008, and $204,000 in 2007. As noted earlier, Montgomery Data has historically made its excess data processing capabilities available to area financial institutions for a fee. As of the year ended December 31, 2007, Montgomery Data had two outside customers. In 2008, the two customers merged with one another, thus leaving Montgomery Data with one customer at December 31, 2008 and 2009. However this customer terminated its service agreement with Montgomery Data effective in January 2010. In light of the demands of providing service to the Bank, we have decided to discontinue this service for third parties, and we expect to merge Montgomery Data into the Bank later in 2010.

Noninterest income not considered to be "core" amounted to a net gain of $67,648,000 in 2009, a net gain of $142,000 in 2008, and a net gain of $477,000 in 2007. In 2009, as previously discussed, we realized a gain of $67,894,000 from the acquisition of Cooperative Bank in June 2009.

Noninterest Expenses

Noninterest expenses for 2009 were $78,551,000, compared to $62,211,000 in 2008 and $56,324,000 in 2007. Table 5 presents the components of our noninterest expense during the past three years.

As reflected in the amounts noted above, noninterest expenses increased 26.3% in 2009 and 10.5% in 2008. The increases in noninterest expenses over the past three years have occurred in every line item of expense and have been primarily a result of our significant growth. Due to acquisition and internal growth, over the past three years our number of bank branches has increased from 68 to 91, and the number of full time equivalent employees has increased from 620 at December 31, 2006 to 764 at December 31, 2009. Additionally, from December 31, 2006 to December 31, 2009, the amount of loans outstanding increased 52.4% and deposits increased 73.0%.

Within personnel expense, employee benefits expense increased by approximately $3.5 million, or 48.1%, in 2009. The primary reasons for the increase in this line item relate to higher health care expense and higher pension expense. We self-insure our employees' health care expense; therefore, incurred health care costs directly impact the

expense we record. In 2009 employee health care expense increased to $3.7 million compared to $2.1 million in 2008 as a result higher claims. Pension expense also increased during 2009, amounting to $3.7 million in 2009 compared to $2.3 million in 2008. This increase was primarily a result of investment losses experienced by the pension plan's assets in 2008. In order to manage this expense, effective June 2009, we are no longer adding new participants to our pension plan.

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In 2009, as a result of the acquisition of Cooperative Bank we incurred approximately $1.3 million in acquisition expenses, primarily consisting of professional fees. Due to recent changes in relevant accounting guidance, we were required to record these acquisition costs as a current period expense. In previous years, any direct expenses associated with an acquisition were capitalized as part of the cost of the acquisition.

FDIC deposit insurance expense has significantly increased over the past two years. From 2004 through 2006, we were not required to pay any FDIC deposit insurance premiums. As discussed above in "Supervision and Regulation of the Bank," in 2006 the FDIC modified its rules relating to the assessment of deposit insurance premiums. In 2007, 2008, and 2009, we incurred approximately $0.1 million, $1.2 million, and $5.5 million, respectively, in FDIC deposit insurance premium expense. The $5.5 million in FDIC insurance expense for 2009 included a special assessment, which applied to all banks, of $1.6 million and was recorded in the second quarter of 2009.

Our ratio of noninterest expense to average assets was 2.54% in 2009 compared to 2.50% in 2008 and 2.63% in 2007. Our efficiency ratio (noninterest expense divided by the sum of tax-equivalent net interest income plus noninterest income) was 39.79% in 2009 compared to 57.67% in 2008 and 58.03% in 2007. For both of the ratios described in this paragraph, a lower ratio is more favorable than a higher ratio, as they generally indicate the amount of expenditures required to produce additional amounts of income. The significantly lower efficiency ratio in 2009 was a result of the acquisition gain related to Cooperative that amounted to $67.9 million.

Income Taxes

The provision for income taxes was $37,618,000 in 2009, $13,120,000 in 2008, and $13,150,000 in 2007.

Table 6 presents the components of tax expense and the related effective tax rates. The effective tax rate for 2009 was 38.4% compared to 37.4% in 2008 and 37.6% in 2007. In 2009, due to the acquisition of Cooperative Bank we recorded a gain of $67.9 million, which resulted in a $26.8 million increase in the provision for income taxes. We expect our effective tax rate to be in the 36%-38% range for the foreseeable future.

Table 1 reflects the fact that in 2005, we recorded incremental tax expense of $4.3 million related to the settlement of a state tax matter with the North Carolina Department of Revenue. See prior year filings for discussion of this matter.

Stock-Based Compensation

We recorded stock-based compensation expense of $449,000, $143,000 and $190,000 for the years ended December 31, 2009, 2008 and 2007, respectively.

On June 1 of 2007, 2008, and 2009, we made stock-based grants of 2,250 options to each of our non-employee directors. In 2008, in addition to the annual director grant, our board of directors approved a grant of incentive-based stock awards to 19 senior officers under the First Bancorp 2007 Equity Plan. In 2009, our board of directors approved a grant of long-term restricted stock to certain senior executives under the 2007 Equity Plan. Both grants are discussed in the following paragraphs.

On June 17, 2008, 262,599 stock options and 81,337 performance units were awarded to 19 senior officers under the 2007 Equity Plan. Each performance unit represents the right to receive one share of First Bancorp common stock upon satisfaction of the vesting conditions. This grant has both performance conditions (earnings per share targets) and service conditions that must be met in order to vest. The 262,599 stock options and 81,337 performance units represented the maximum amount of options and performance units that could have vested if the Company were to achieve specified maximum goals for earnings per share during the three annual performance periods ending on December 31, 2008, 2009, and 2010. Up to one-third of the total number of options and performance units granted

will vest annually as of December 31 of each year beginning in 2010, if (1) the Company achieves specific EPS goals during the corresponding performance period and (2) the award

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recipient continues employment for a period of two years beyond the corresponding performance period. Compensation expense for this grant will be recorded over the various service periods based on the estimated number of options and performance units that are probable to vest. If the awards do not vest, no compensation cost will be recognized and any previously recognized compensation cost will be reversed. We did not achieve the minimum earnings per share performance goal for 2008, and thus one-third of the above grant was permanently forfeited. During June 2009, as a result of the significant gain realized related to the Cooperative Bank acquisition, we determined that it was probable that the EPS goal for 2009 would be met. Accordingly, we recorded compensation expense of $149,000 in June 2009 and $75,000 in the third and fourth quarters of 2009. We expect to record compensation expense of approximately $75,000 on a quarterly basis through the vesting period of December 31, 2011. We currently do not believe that the EPS goals for 2010 will be met, and thus no compensation expense has been recorded related to that performance period.

On December 11, 2009, the board of directors granted 29,267 long-term restricted shares of common stock to certain senior executives. This restricted stock vests in accordance with the minimum rules for long-term equity grants for companies participating in the United States Treasury's Troubled Asset Relief Program (TARP). These rules require that the vesting of the stock be tied to repayment of the financial assistance. For each 25% of total financial assistance repaid, 25% of the total long-term restricted stock may become transferrable. The amount of compensation expense recorded by the Company in 2009 on account of this grant was insignificant. The total compensation expense associated with this grant was $398,000 and is being initially amortized over a four year period.

Excluding the incentive grants noted above, our stock-based compensation expense related to options currently outstanding is insignificant. We expect to continue the annual grant of 2,250 stock options to each of our non-employee directors in 2010. This annual grant resulted in us recording an expense of $150,000 ($91,000 after-tax) in 2009.

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ANALYSIS OF FINANCIAL CONDITION AND CHANGES IN FINANCIAL CONDITION

Overview

Over the past two years, we have experienced significant increases in our levels of loans and deposits, which has resulted in an increase in assets from $2.3 billion at December 31, 2007 to $3.5 billion at December 31, 2009. Changes in our loans and deposit balances occur as a result of organic growth or decline, as well as acquisitions. During the second quarter of 2009, we acquired Cooperative Bank under a purchase and assumption agreement with the FDIC. During the second quarter of 2008, we completed the acquisition of Great Pee Dee Bancorp through merger. The following table presents detailed information regarding the nature of our growth in 2008 and 2009:

($ in thousands)	Balance at beginning of period	Internal growth (1)	Growth from Acquisitions	Balance at end of period	Total percentage growth	Internal percentage growth (1)
2009						
Loans	$2,211,315	(159,554)	601,104	2,652,865	20.0 %	-7.2 %
Deposits – Noninterest bearing	229,478	7,720	35,224	272,422	18.7 %	3.4 %
Deposits – NOW	198,775	131,576	32,015	362,366	82.3 %	66.2 %
Deposits – Money market	340,739	110,444	45,757	496,940	45.8 %	32.4 %
Deposits – Savings	125,240	2,855	21,243	149,338	19.2 %	2.3 %
Deposits – Brokered time	78,569	(45,180)	42,943	76,332	-2.8 %	-57.5 %
Deposits – Internet time	5,206	(38,854)	161,672	128,024	n/a	n/a
Deposits – Time >$100,000	520,198	35,826	148,104	704,128	35.4 %	6.9 %
Deposits – Time <$100,000	576,586	(58,131)	225,103	743,558	29.0 %	-10.1 %
Total deposits	$2,074,791	146,256	712,061	2,933,108	41.4 %	7.0 %
2008						
Loans	$1,894,295	133,180	183,840	2,211,315	16.7 %	7.0 %
Deposits – Noninterest bearing	232,141	(11,099)	8,436	229,478	-1.1 %	-4.8 %
Deposits – NOW	192,785	(4,405)	10,395	198,775	3.1 %	-2.3 %
Deposits – Money market	264,653	61,025	15,061	340,739	28.7 %	23.1 %
Deposits – Savings	100,955	21,697	2,588	125,240	24.1 %	21.5 %
Deposits – Brokered time	–	53,012	25,557	78,569	n/a	n/a
Deposits – Internet time	–	5,206	–	5,206	n/a	n/a
Deposits – Time >$100,000	479,176	3,350	37,672	520,198	8.6 %	0.7 %
Deposits – Time <$100,000	568,567	(39,981)	48,000	576,586	1.4 %	-7.0 %
Total deposits	$1,838,277	88,805	147,709	2,074,791	12.9 %	4.8 %

(1) Excludes the impact of acquisitions.

As derived from the table above, for 2009, our loans increased by $442 million, or 20.0%, which was due to our acquisition of Cooperative Bank on June 19, 2009, which resulted in an increase in loans of $601 million. During 2009, deposits increased $858 million, or 41.4%, of which $146 million was internal growth and $712 million was from the Cooperative Bank acquisition. For 2009, internally generated loans decreased $160 million, or 7.2%, while internally generated deposits increased by $146 million, or 7.0%. We believe internally generated loans declined due to lower loan demand in the recessionary economy, as well as an initiative that began in 2008 to require generally

higher loan interest rates to better compensate us for our risk. Also, we have de-emphasized certain types of lending, most notably acquisition and development land loans and non-owner occupied commercial real estate.

Overall, deposit growth for 2009 was strong, which we primarily attribute to customers shifting money to

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banks from other non-FDIC insured sources. Deposit growth in NOW accounts for 2009 was impacted by a $65 million deposit received during the last week of the year.

The deposit portfolio assumed from Cooperative Bank had a high concentration of time deposits, comprising approximately 81% of total deposits compared to our recent historical average of 55%-57%. Time deposits are generally our bank's most expensive funding source. Additionally, Cooperative Bank's time deposits were more heavily concentrated in brokered time deposits and time deposits gathered by placing interest rates on internet websites. Prior to the Cooperative acquisition, we had $66 million in brokered deposits and $7 million in internet deposits. The acquisition brought us an additional $43 million in brokered deposits and $162 million in internet deposits. We believe these two types of deposit sources have little long term value, as the interest rates are relatively high and there is limited opportunity to develop additional business with those customers. We expect that our level of internet deposits will continue to steadily decline in the future as those deposits mature because we plan to offer interest rates on renewals that are less competitive than the relatively high rates that Cooperative was offering. We expect to replace those deposits with either retail deposits or brokered deposits at lower interest rates. At December 31, 2009, brokered deposits comprised just 2.6% of deposits and internet deposits comprised 4.4% of total deposits.

In 2008, we experienced internal loan growth of 7.0%, which was partially due to our 2005 expansion into Mooresville, North Carolina, a high growth market near Charlotte, and our 2005 expansion into the coastal North Carolina counties of New Hanover County and Brunswick County. Loan growth in these markets totaled $77 million in 2008.

Internal deposit growth was 4.8% in 2008, with most of the growth occurring in money market accounts. The growth in money market accounts was almost entirely within a high interest rate money market account that was created in order to attract deposits to fund loan growth, as well as to enhance overall liquidity. We believe that the generally lower growth (or negative growth) experienced in 2008 in the other non-time deposit categories was partially a result of customers shifting funds to this money market account. The increase in the Savings category in 2008 was due to a $25 million deposit from one customer into a high interest rate savings account.

Internal non-brokered time deposit growth in denominations of less than $100,000 decreased 7% in 2008. Time deposits are a highly rate sensitive category of deposits. In 2008, we decided not to match promotional time deposit interest rates being offered by several of our local competitors, which we felt were too high compared to alternative funding sources, and consequently we experienced a loss of internally generated time deposits. Instead of matching the high interest rates, we decided to utilize brokered time deposits because they had interest rates meaningfully lower than rates in the local marketplace. We ended 2008 with a total of $79 million in brokered time deposits compared to none in 2007. The $79 million in brokered time deposits at December 31, 2008 represented just 3.8% of our total deposits, which we believe is a relatively low level of reliance on this wholesale funding source. In addition to the $79 million in brokered deposits at December 31, 2008, we also had $5 million in time deposits that we raised during the year from an internet posting service.

As can be seen in the table above, our acquisition of Great Pee Dee Bancorp in 2008 resulted in the assumption of $184 million in loans and $148 million in deposits.

Our overall liquidity improved during 2009 compared to 2008. Excluding the Cooperative acquisition, we experienced $146 million in deposit growth, while loans decreased $160 million, thereby creating $306 million in additional liquidity. Additionally, the receipt of $65 million in proceeds from the January 2009 sale of preferred stock to the US Treasury improved our liquidity. There was no significant impact on our liquidity as a result of the Cooperative acquisition. Our liquid assets (cash and securities) as a percentage of our total deposits and borrowings increased from 16.5% at December 31, 2008 to 17.8% at December 31, 2009. In addition, the growth in our deposits has lessened our reliance on borrowings, which declined by $190 million during 2009.

Our capital ratios improved significantly in 2009 as a result of our sale of $65 million of preferred stock to

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the US Treasury under the Capital Purchase Program on January 9, 2009. All of our capital ratios have continually exceeded the regulatory thresholds for "well-capitalized" status for all periods covered by this report.

Due to the recessionary economic environment that began in 2007, our asset quality ratios have worsened. Our non-covered nonperforming assets to total non-covered assets ratio was 3.10% at December 31, 2009 compared to 1.29% at December 31, 2008, and 0.47% at December 31, 2007. For the year ended December 31, 2009, our ratio of net charge-offs to average non-covered loans was 0.56% compared to 0.24% for 2008, and 0.16% for 2007.

Distribution of Assets and Liabilities

Table 7 sets forth the percentage relationships of significant components of our balance sheet at December 31, 2009, 2008, and 2007.

In the two years leading up to 2009, loans comprised 80%-81% of total assets while deposits comprised 76%-79% of total assets. In 2009, primarily as a result of the general decline in loan balances (excluding Cooperative) and the increases in deposits, the percentage of loans to total assets decreased to 74%, while the percentage of deposits to total assets increased to 82%. With higher levels of cash realized from our increased liquidity during 2009, we paid down our level of borrowings, which resulted in borrowings comprising only 5% of total assets compared to 10%-13% at the prior two year ends.

Securities

Information regarding our securities portfolio as of December 31, 2009, 2008, and 2007 is presented in Tables 8 and 9.

The composition of the investment securities portfolio reflects our investment strategy of maintaining an appropriate level of liquidity while providing a relatively stable source of income. The investment portfolio also provides a balance to interest rate risk and credit risk in other categories of the balance sheet while providing a vehicle for the investment of available funds, furnishing liquidity, and supplying securities to pledge as required collateral for certain deposits.

Total securities amounted to $214.2 million, $187.2 million, and $151.8 million at December 31, 2009, 2008, and 2007, respectively. In 2008, our level of securities increased primarily due to purchases of securities we initiated in order to collateralize public deposits. In 2009, we experienced higher cash balances as a result of deposit growth that exceeded loan growth. We invested a portion of this cash in investment securities, which resulted in higher securities balances. In 2009, the majority of our purchases were mortgage-backed securities issued by the Government National Mortgage Association (Ginnie Mae), which are 100% guaranteed by the United States government and carry a zero percent weighting for risk-based capital purposes. In general, we prefer to invest in relatively short-term investments in order to provide liquidity and manage interest rate risk. We have never held investments in Freddie Mac or Fannie Mae preferred stock.

The majority of our "government-sponsored enterprise" securities are issued by the Federal Home Loan Bank and carry one maturity date, often with an issuer call feature. At December 31, 2009, of the $37 million in carrying value of government-sponsored enterprise securities, $32 million were issued by the Federal Home Loan Bank system and the other $5 million were issued by the Federal Farm Credit Bank system.

Our $112 million of mortgage-backed securities have been all been issued by either Freddie Mac, Fannie Mae, or Ginnie Mae, each of which are government-sponsored corporations. We have no "private label" mortgage-backed securities. Mortgage-backed securities vary in their repayment in correlation with the underlying pools of home

mortgage loans.

Included in mortgage-backed securities at December 31, 2009 were collateralized mortgage obligations

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("CMOs") with an amortized cost of $5.4 million and a fair value of $5.6 million. The CMOs that we have invested in are substantially all "early tranche" portions of the CMOs, which minimizes our long-term interest rate risk.

At December 31, 2009, our $14 million investment in corporate bonds was comprised of the following:

($ in thousands) Issuer	S&P Issuer Ratings (1)	Maturity Date	Amortized Cost	Market Value
First Citizens Bancorp (South Carolina) Bond	BB	4/1/15	$2,994	2,859
Bank of America Trust Preferred Security	BB	12/11/26	2,053	1,918
Wells Fargo Trust Preferred Security	A-	1/15/27	2,567	2,428
Bank of America Trust Preferred Security	BB	4/15/27	5,063	4,831
First Citizens Bancorp (North Carolina) Trust Preferred Security	BB	3/1/28	2,092	1,811
First Citizens Bancorp (South Carolina) Trust Preferred Security	Not Rated	6/15/34	1,000	589
Total investment in corporate bonds			$15,769	14,436

(1) The ratings are as of January 26, 2010.

Our $17 million investment in equity securities at each year end is comprised almost entirely of capital stock in the Federal Home Loan Bank of Atlanta (FHLB). The FHLB requires us to purchase their stock in order to borrow from them. The amount they require us to invest is based on our level of borrowings from them. At December 31, 2009, our investment in capital stock of the FHLB amounted to $16.5 million of our total investment in equity securities of $17.0 million. Until February 27, 2009, the FHLB redeemed their stock at par as borrowings were repaid. On February 27, 2009, the FHLB announced that they would no longer automatically redeem their stock when loans are repaid. Instead, they stated that they would evaluate whether they would repurchase stock on a quarterly basis. Since that time the FHLB has not repurchased any excess stock.

The fair value of securities held to maturity, which we carry at amortized cost, was $534,000 more than the carrying value at December 31, 2009 and $179,000 less than the carrying value at December 31, 2008. Our $34.4 million in securities held to maturity are comprised almost entirely of municipal bonds issued by state and local governments throughout our market area. The denominations of the bonds are all less than $1,000,000 and we have no significant concentration of bond holdings from one government entity, with the single largest exposure to any one entity being $2,000,000. Management evaluated any unrealized losses on individual securities at each year end and determined them to be of a temporary nature and caused by fluctuations in market interest rates, not by concerns about the ability of the issuers to meet their obligations.

At December 31, 2009, 2008, and 2007, a net unrealized gain of $1,832,000, $273,000, and $86,000, respectively, was included in the carrying value of securities classified as available for sale. During those three years, interest rates have generally declined, which typically increases the value of our investment securities. Management evaluated any unrealized losses on individual securities at each year end and determined them to be of a temporary nature and caused by fluctuations in market interest rates and the overall economic environment, not by concerns about the ability of the issuers to meet their obligations. Net unrealized gains, net of applicable deferred income taxes, of $1,117,000, $167,000, and $52,000 have been reported as part of a separate component of shareholders' equity (accumulated other comprehensive income (loss)) as of December 31, 2009, 2008, and 2007, respectively.

The weighted average taxable-equivalent yield for the securities available for sale portfolio was 3.62% at December 31, 2009. The expected weighted average life of the available for sale portfolio using the call date for above-market

callable bonds, the maturity date for all other non-mortgage-backed securities, and the expected life for mortgage-backed securities, was 4.9 years.

The weighted average taxable-equivalent yield for the securities held to maturity portfolio was 5.91% at December 31, 2009. The expected weighted average life of the held to maturity portfolio using the call date for above-market callable bonds and the maturity date for all other securities, was 7.5 years.

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As of December 31, 2009 and 2008, we own no investment securities of any one issuer, other than government-sponsored enterprises or corporations, in which aggregate book values and market values exceeded 10% of shareholders' equity.

Loans

Table 10 provides a summary of the loan portfolio composition of our total loans at each of the past five year ends.

As previously discussed, in our acquisition of Cooperative Bank, we entered into loss share agreements with the FDIC, which afford us significant protection from losses from all loans and other real estate acquired in the acquisition. Because of the loss protection provided by the FDIC, the financial risk of the Cooperative Bank loans is significantly different from those assets not covered under the loss share agreements. Accordingly, we present separately loans subject to the FDIC loss share agreements as "covered loans" and loans that are not subject to the loss share agreements as "non-covered loans." Table 10a presents a breakout of covered and non-covered loans as of December 31, 2009.

The loan portfolio is the largest category of our earning assets and is comprised of commercial loans, real estate mortgage loans, real estate construction loans, and consumer loans. We restrict virtually all of our lending to our 36 county market area, which is located in central and southeastern North Carolina, four counties in southern Virginia and five counties in northeastern South Carolina. The diversity of the region's economic base has historically provided a stable lending environment.

In 2009, net loans outstanding increased $441.6 million, or 20.0% to $2.65 billion. All of the loan growth in 2009 was assumed in the acquisition of Cooperative Bank in June 2009, as non-covered loans declined by $78.5 million in 2009.

In 2008, loans outstanding increased $317.0 million, or 16.7% to $2.21 billion. Of the $317.0 million in loan growth in 2008, approximately $183.8 million was assumed in the acquisition of Great Pee Dee Bancorp, Inc. in April 2008.

The great majority of our loan growth over the years has been real estate mortgage loans and loans secured by real estate have consistently comprised 80% to 85% of our outstanding loan balances. The majority of our "real estate" loans are personal and commercial loans where cash flow from the borrower's occupation or business are the primary repayment source, with the real estate pledged providing a secondary repayment source.

Table 10 indicates that the two types of loans that have had the largest variances in the amount outstanding as a percent of total loans have been construction/land development loans and residential mortgage loans. In 2005 we expanded our branch network to what was then the fast-growing southeast coast of North Carolina, which had a high demand for construction and land development loans. In 2008, due to recessionary conditions, particularly in the new housing market, loan demand for these types of loans weakened and we tightened our loan underwriting criteria for these types of loans, which reduced growth. Due to economic conditions, for the past two years we have made very few new acquisition and land development loans, and we expect this trend to continue.

From 2005 to 2008, our level of residential mortgage loans generally declined as we experienced higher growth in other loan categories. Due to the Cooperative transaction, our percentage of residential loans increased significantly because Cooperative's loan portfolio was heavily concentrated in residential mortgages.

Table 11 provides a summary of scheduled loan maturities over certain time periods, with fixed rate loans and adjustable rate loans shown separately. Approximately 30% of our accruing loans outstanding at December

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31, 2009 mature within one year and 73% of total loans mature within five years. As of December 31, 2009, the percentages of variable rate loans and fixed rate loans as compared to total performing loans were 49% and 51%, respectively. We intentionally make a blend of fixed and variable rate loans so as to reduce interest rate risk.

Nonperforming Assets

Nonperforming assets include nonaccrual loans, troubled debt restructurings, loans past due 90 or more days and still accruing interest, and other real estate. As a matter of policy we place all loans that are past due 90 or more days on nonaccrual basis, and thus there were no loans at any of the past five year ends that were 90 days past due and still accruing interest.

Nonaccrual loans are loans on which interest income is no longer being recognized or accrued because management has determined that the collection of interest is doubtful. Placing loans on nonaccrual status negatively impacts earnings because (i) interest accrued but unpaid as of the date a loan is placed on nonaccrual status is reversed and deducted from interest income, (ii) future accruals of interest income are not recognized until it becomes probable that both principal and interest will be paid and (iii) principal charged-off, if appropriate, may necessitate additional provisions for loan losses that are charged against earnings. In some cases, where borrowers are experiencing financial difficulties, loans may be restructured to provide terms significantly different from the originally contracted terms.

Table 12 summarizes our nonperforming assets at the dates indicated. Because of the loss protection provided by the FDIC, we present separately nonperforming assets subject to the loss share agreements as “covered” and nonperforming assets that are not subject to the loss share agreements as “non-covered.”

Table 12a presents our nonperforming assets at December 31, 2009 by general geographic region and further segregated into “covered” nonperforming assets and “non-covered” nonperforming assets. The majority of our nonperforming assets are located in the Eastern North Carolina region, which has experienced the most negative effects of the recession of any of our regions.

Due largely to the recessionary economic conditions that began in late 2007 and worsened in 2008 and 2009, we have experienced increases in our nonperforming assets. Our total nonperforming assets were also significantly impacted by the Cooperative acquisition.

Non-covered nonperforming loans totaled $83.5 million, $30.6, and $7.8 million, as of December 31, 2009, 2008, and 2007, respectively. Total non-covered nonperforming loans as a percentage of total loans amounted to 3.91%, 1.38%, and 0.41%, at December 31, 2009, 2008, and 2007, respectively.

At December 31, 2009, troubled debt restructurings amounted to $21.3 million, an increase of $17.3 million over the $4.0 million reported at December 31, 2008. This increase was the result of our working with borrowers experiencing financial difficulties by modifying certain loan terms and was also impacted by our analysis of the Federal Reserve’s October 2009 guidance related to real estate loan workouts, which provided clarification of situations involving borrowers that should be reported as troubled debt restructurings.

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The following is the composition, by loan type, of all of our nonaccrual loans at each period end:

	At December 31, 2009 (1)	At December 31, 2008
Commercial, financial, and agricultural	$ 4,033	1,726
Real estate – construction, land development, and other land loans	80,669	6,936
Real estate – mortgage – residential (1-4 family) first mortgages	48,424	10,856
Real estate – mortgage – home equity loans/lines of credit	16,951	2,242
Real estate – mortgage – commercial and other	28,476	3,624
Installment loans to individuals	1,569	1,216
Total nonaccrual loans	$ 180,122	26,600

(1) Includes both covered and non-covered loans.

The following segregates our nonaccrual loans at December 31, 2009 into covered and non-covered loans:

	Covered Nonaccrual Loans	Non-covered Nonaccrual Loans	Total Nonaccrual Loans
Commercial, financial, and agricultural	$ 263	3,770	4,033
Real estate – construction, land development, and other land loans	54,023	26,646	80,669
Real estate – mortgage – residential (1-4 family) first mortgages	31,315	17,109	48,424
Real estate – mortgage – home equity loans/lines of credit	13,451	3,500	16,951
Real estate – mortgage – commercial and other	18,595	9,881	28,476
Installment loans to individuals	269	1,300	1,569
Total nonaccrual loans	$ 117,916	62,206	180,122

If the nonaccrual and restructured loans as of December 31, 2009, 2008 and 2007 had been current in accordance with their original terms and had been outstanding throughout the period (or since origination if held for part of the period), gross interest income in the amounts of approximately $9,800,000, $1,930,000 and $610,000 for nonaccrual loans and $1,200,000, $310,000 and $1,000 for restructured loans would have been recorded for 2009, 2008, and 2007, respectively. Interest income on such loans that was actually collected and included in net income in 2009, 2008 and 2007 amounted to approximately $2,147,000, $826,000 and $252,000 for nonaccrual loans (prior to their being placed on nonaccrual status), and $866,000, $155,000, and $1,000 for restructured loans, respectively. At December 31, 2009 and 2008, the Company had no commitments to lend additional funds to debtors whose loans were nonperforming.

Management routinely monitors the status of certain large loans that, in management's opinion, have credit weaknesses that could cause them to become nonperforming loans. In addition to the nonperforming loan amounts discussed above, management believes that an estimated $5 million of non-covered loans and $21 million of covered loans that were performing in accordance with their contractual terms at December 31, 2009 have the potential to develop problems depending upon the particular financial situations of the borrowers and economic conditions in

general. Management has taken these potential problem loans into consideration when evaluating the adequacy of the allowance for loan losses at December 31, 2009 (see discussion below).

Loans classified for regulatory purposes as loss, doubtful, substandard, or special mention that have not been disclosed in the problem loan amounts and the potential problem loan amounts discussed above do not represent or result from trends or uncertainties that management reasonably expects will materially impact future operating results, liquidity, or capital resources, or represent material credits about which management is aware of any information that causes management to have serious doubts as to the ability of such borrowers to comply with the loan repayment terms.

Other real estate includes foreclosed, repossessed, and idled properties. Non-covered other real estate has increased over the past three years, amounting to $8.8 million at December 31, 2009, $4.8 million at December 31, 2008, and $3.0 million at December 31, 2007. At December 31, 2009, we also held $47.4 million in other

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real estate that is subject to the loss share agreement with the FDIC. We believe that the fair values of the items of other real estate, less estimated costs to sell, equal or exceed their respective carrying values at the dates presented.

The following table presents the detail of our other real estate at each of the past two year ends:

	At December 31, 2009 (1)	At December 31, 2008
Vacant land	$ 44,078	975
1-4 family residential properties	10,004	2,149
Commercial real estate	2,141	1,693
Other	–	15
Total other real estate	$ 56,223	4,832

(1) Includes both covered and non-covered real estate.

The following segregates our other real estate at December 31, 2009 into covered and non-covered:

	Covered Other Real Estate	Non-covered Other Real Estate	Total Other Real Estate
Vacant land	$ 40,836	3,242	44,078
1-4 family residential properties	6,171	3,833	10,004
Commercial real estate	423	1,718	2,141
Other	–	–	–
Total other real estate	$ 47,430	8,793	56,223

Allowance for Loan Losses and Loan Loss Experience

The allowance for loan losses is created by direct charges to operations (known as a "provision for loan losses" for the period in which the charge is taken). Losses on loans are charged against the allowance in the period in which such loans, in management's opinion, become uncollectible. The recoveries realized during the period are credited to this allowance. We consider our procedures for recording the amount of the allowance for loan losses and the related provision for loan losses to be a critical accounting policy. See the heading "Critical Accounting Policies" above for further discussion.

The factors that influence management's judgment in determining the amount charged to operating expense include past loan loss experience, composition of the loan portfolio, evaluation of probable inherent losses and current economic conditions.

We use a loan analysis and grading program to facilitate our evaluation of probable inherent loan losses and the adequacy of our allowance for loan losses. In this program, risk grades are assigned by management and tested by an independent third party consulting firm. The testing program includes an evaluation of a sample of new loans, loans we identify as having potential credit weaknesses, loans past due 90 days or more, loans originated by new loan officers, nonaccrual loans and any other loans identified during previous regulatory and other examinations.

We strive to maintain our loan portfolio in accordance with what management believes are conservative loan underwriting policies that result in loans specifically tailored to the needs of our market areas. Every effort is made to

identify and minimize the credit risks associated with such lending strategies. We have no foreign loans, few agricultural loans and do not engage in significant lease financing or highly leveraged transactions. Commercial loans are diversified among a variety of industries. The majority of loans captioned in the tables discussed below as “real estate” loans are personal and commercial loans where real estate provides additional security for the loan. Collateral for virtually all of these loans is located within our principal market area.

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The allowance for loan losses amounted to $37.3 million at December 31, 2009 compared to $29.3 million at December 31, 2008 and $21.3 million at December 31, 2007. At December 31, 2009, the entire allowance for loan losses is attributable to non-covered loans, with the Cooperative covered loans having no allowance allocation because these loans were written down to estimated fair market value in connection with the recording of the acquisition.

The ratio of the allowance for loan losses to non-covered loans was 1.75%, 1.32%, and 1.13% as of December 31, 2009, 2008, and 2007, respectively. The increasing allowance percentage has been necessary due to the higher level of delinquencies and classified and nonperforming loans. As noted in Table 12, our allowance for loan losses as a percentage of non-covered nonperforming loans ("coverage ratio") amounted to 45% at December 31, 2009 compared to 96% at December 31, 2008 and 273% at December 31, 2007. Due to the secured nature of virtually all of our loans that are on nonaccrual status, the variance in the coverage ratio is not necessarily indicative of the relative adequacy of the allowance for loan losses.

Table 13 sets forth the allocation of the allowance for loan losses at the dates indicated. The amount of the unallocated portion of the allowance for loan losses did not vary materially at any of the past three year ends. The allowance for loan losses is available to absorb losses in all categories.

Management considers the allowance for loan losses adequate to cover probable loan losses on the loans outstanding as of each reporting date. It must be emphasized, however, that the determination of the allowance using our procedures and methods rests upon various judgments and assumptions about economic conditions and other factors affecting loans. No assurance can be given that we will not in any particular period sustain loan losses that are sizable in relation to the amount reserved or that subsequent evaluations of the loan portfolio, in light of conditions and factors then prevailing, will not require significant changes in the allowance for loan losses or future charges to earnings.

In addition, various regulatory agencies, as an integral part of their examination process, periodically review the allowance for loan losses and losses on foreclosed real estate. Such agencies may require us to recognize additions to the allowance based on the examiners' judgments about information available to them at the time of their examinations.

For the years indicated, Table 14 summarizes our balances of loans outstanding, average loans outstanding, and a detailed rollforward of the allowance for loan losses. In addition to the increases to the allowance for loan losses related to normal provisions, the increases in the dollar amounts of the allowance for loan losses in 2008 and 2006 were also affected by amounts recorded to provide for loans assumed in corporate acquisitions. In 2008, we added $3,158,000 to the allowance for loan losses related to approximately $184 million in loans assumed in the acquisition of Great Pee Dee in April 2008.

Net loan charge-offs amounted to $12.1 million in 2009, $5.1 million in 2008, and $2.8 million in 2007. The higher amounts in 2008 and 2009 reflect the impact of deteriorating loan quality that has been impacted by the recessionary economic conditions. Net charge-offs as a percentage of average non-covered loans represented 0.56%, 0.24%, and 0.16%, during 2009, 2008, and 2007, respectively.

Deposits and Securities Sold Under Agreements to Repurchase

At December 31, 2009, deposits outstanding amounted to $2.933 billion, an increase of $858 million, or 41.4%, from December 31, 2008. Approximately $146 million, or 17%, of the deposit growth in 2009 was internally generated, while the remaining $712 million, or 83%, resulted from the acquisition of Cooperative Bank in June 2009. Overall, deposit growth for 2009 was strong, which we primarily attribute to customers shifting money to banks from other

non-FDIC insured sources. Deposit growth in NOW accounts for 2009 was impacted by a $65 million deposit received during the last week of the year.

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In 2008, deposits grew from $1.838 billion to $2.075 billion, an increase of $237 million, or 12.9%, from December 31, 2007. Approximately $89 million, or 38%, of the deposit growth in 2008 was internally generated, while the remaining $148 million, or 62%, resulted from the acquisition of Great Pee Dee in April 2008.

The nature of our deposit growth is illustrated in the table on page 43. The following table reflects the mix of our deposits at each of the past three year ends:

	2009		2008		2007	
Noninterest-bearing deposits	9	%	11	%	13	%
NOW deposits	12	%	10	%	10	%
Money market deposits	17	%	16	%	14	%
Savings deposits	5	%	6	%	6	%
Brokered deposits	3	%	4	%	–	
Internet deposits	4	%	0	%	–	
Time deposits > $100,000	24	%	25	%	26	%
Time deposits < $100,000	26	%	28	%	31	%
Total deposits	100	%	100	%	100	%
Securities sold under agreements to repurchase as a percent of total deposits	2	%	3	%	2	%

The deposit mix remained relatively consistent from 2007 to 2009. Time deposits have declined slightly and money markets have increased partially as a result of customers shifting their funds between the two categories. Additionally, the percentages for time deposits have declined because we have chosen not to match certain promotional time deposit interest rates being offered by several of our local competitors, which we felt were too high compared to alternative funding sources. Instead of matching the high interest rates, in 2008, we began utilizing brokered time deposits because they had interest rates meaningfully lower than rates in the local marketplace at that time. We ended 2008 with a total of $79 million in brokered time deposits compared to none in 2007. In addition to the $79 million in brokered deposits at December 31, 2008, we also had $5 million in time deposits that we raised during the year from an internet posting service. In the June 2009 Cooperative acquisition, we assumed $43 million in brokered deposits and $162 million in internet time deposits in 2009. At June 30, 2009, we had a total of $109 million in brokered deposits and $169 million in internet time deposits. Since that time, due to relatively strong growth in core deposits that are generally paying lower interest rates, we have elected to pay off most brokered and internet deposits as they mature instead of renewing them. At December 31, 2009, our brokered deposits were down to $76 million and internet time deposits had been reduced to $128 million.

We routinely engage in activities designed to grow and retain deposits, such as (1) emphasizing relationship banking to new and existing customers, where borrowers are encouraged and normally expected to maintain deposit accounts with us, (2) pricing deposits at rate levels that will attract and/or retain deposits, and (3) continually working to identify and introduce new products that will attract customers or enhance our appeal as a primary provider of financial services.

Table 15 presents the average amounts of our deposits and the average yield paid for those deposits for the years ended December 31, 2009, 2008, and 2007.

As of December 31, 2009, we held approximately $816.5 million in time deposits of $100,000 or more. Table 16 is a maturity schedule of time deposits of $100,000 or more as of December 31, 2009. This table shows that 92% of our time deposits greater than $100,000 mature within one year.

At each of the past three year ends, we have no deposits issued through foreign offices, nor do we believe that we held any deposits by foreign depositors.

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Borrowings

We had borrowings outstanding of $176.8 million at December 31, 2009 compared to $367.3 million at December 31, 2008. As shown in Table 2, average borrowings decreased significantly in 2009 as a result of the low loan growth and strong deposit growth that provided funds to pay down our borrowings. In 2009, average loans outstanding were $358 million higher than in 2008, while average deposits increased by $564 million. Average borrowings increased from 2007 to 2008 as a result the need to fund loan growth that exceeded deposit growth, as well as $41 million in borrowings assumed in the acquisition of Great Pee Dee. In 2008, average loans outstanding were $309 million higher than in 2007, whereas average deposits increased by only $205 million.

At December 31, 2009, the Company had four sources of readily available borrowing capacity – 1) an approximately $687 million line of credit with the FHLB, of which $130 million was outstanding at December 31, 2009 and $265 million was outstanding at December 31, 2008, 2) a $50 million overnight federal funds line of credit with a correspondent bank, of which none was outstanding at December 31, 2009 and $35 million was outstanding at December 31, 2008, 3) an approximately $84 million line of credit through the Federal Reserve Bank of Richmond’s (FRB) discount window, none of which was outstanding at December 31, 2009 or 2008, and 4) a $20 million holding company line of credit with a commercial bank (none of which was outstanding at December 31, 2009, and $20 million was outstanding at December 31, 2008).

Our line of credit with the FHLB can be structured as either short-term or long-term borrowings, depending on the particular funding or liquidity need, and is secured by our FHLB stock and a blanket lien on most of our real estate loan portfolio. As of December 31, 2009, $100 million of the $130 million outstanding with the FHLB were overnight borrowings (daily renewable) with a weighted-average interest rate of 0.36%, with the remaining $30 million outstanding having a weighted average interest rate of 3.94% and maturity dates ranging from August 2010 to April 2012. For the year ended December 31, 2009, the average amount of FHLB borrowings outstanding was approximately $98 million and had a weighted average interest rate for the year of 1.77%. The maximum amount of short-term FHLB borrowings outstanding at any month-end during 2009 was $225 million.

In addition to the outstanding borrowings from the FHLB that reduce the available borrowing capacity of the line of credit, the borrowing capacity was further reduced by $170 million and $75 million at December 31, 2009 and 2008, respectively, as a result of the pledging letters of credit backed by the FHLB for public deposits at each of those dates.

In January 2010, we received the results of a collateral audit from the FHLB. Based primarily on a finding that we were not keeping certain original loan documents, but were instead imaging them and shredding the original documents, a significant portion of our collateral pledged to the FHLB was deemed to be ineligible for pledging purposes. As a result, our borrowing availability with the FHLB was reduced from $687 million to approximately $335 million. We have changed our document retention procedures and expect our borrowing availability to gradually increase as we make new loans and renew existing ones.

Our correspondent bank relationship allows us to purchase up to $50 million in federal funds on an overnight, unsecured basis (federal funds purchased). We had no borrowings outstanding under this line at December 31, 2009. We had $35 million borrowings outstanding under this line at December 31, 2008. This line of credit was not drawn upon during any of 2007. The maximum amount of federal funds purchased outstanding at any month-end during 2009 was $40 million.

We also have a line of credit with the FRB discount window. This line is secured by a blanket lien on a portion of our commercial and consumer loan portfolio (excluding real estate loans). Based on the collateral that we owned as of December 31, 2009, the available line of credit was approximately $84 million. At December,

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31, 2009 and 2008, we had no borrowings outstanding under this line. During 2009, we occasionally utilized this line of credit due to favorable interest rates offered. The maximum amount of FRB borrowings outstanding at any month-end during 2009 was $75 million.

At December 31, 2009 and 2008, we had a $20 million holding company line of credit with a correspondent bank that was secured by 100% of the common stock of our bank subsidiary. This line of credit expires and is subject to renewal in February of each year. The line of credit was not drawn at December 31, 2009, while at December 31, 2008, it was fully drawn. At the February 2010 renewal, the limit on the line of credit was reduced from $20 million to $10 million due to the correspondent bank's desire to reduce its exposure in this line of business.

In addition to the lines of credit described above, in which we had $130 million and $300 million outstanding as of December 31, 2009, and 2008, respectively, we also had a total of $46.4 million in trust preferred security debt outstanding at December 31, 2009 and 2008. We have initiated three trust preferred security issuances since 2002 totaling $67.0 million, with one of those issuances for $20.6 million being redeemed in 2007. These borrowings each have 30 year final maturities and were structured in a manner that allows them to qualify as capital for regulatory capital adequacy requirements. We may call these debt securities at par on any quarterly interest payment date five years after their issue date. We issued $20.6 million of this debt on October 29, 2002 (which we called in 2007), an additional $20.6 million on December 19, 2003, and $25.8 million on April 13, 2006. The interest rate on these debt securities adjusts on a quarterly basis at a rate of three-month LIBOR plus 2.70% for the securities issued in 2003, and three-month LIBOR plus 1.39% for the securities issued in 2006.

Liquidity, Commitments, and Contingencies

Our liquidity is determined by our ability to convert assets to cash or to acquire alternative sources of funds to meet the needs of our customers who are withdrawing or borrowing funds, and our ability to maintain required reserve levels, pay expenses and operate the Company on an ongoing basis. Our primary liquidity sources are net income from operations, cash and due from banks, federal funds sold and other short-term investments. Our securities portfolio is comprised almost entirely of readily marketable securities which could also be sold to provide cash.

As noted above, in addition to internally generated liquidity sources, we currently (March 2010) have the ability to obtain borrowings from the following four sources – 1) an approximately $335 million line of credit with the FHLB, 2) a $50 million overnight federal funds line of credit with a correspondent bank, 3) an approximately $84 million line of credit through the FRB's discount window and 4) a holding company line of credit with a limit of $10 million.

Our overall liquidity improved during 2009 compared to 2008. Excluding the Cooperative acquisition, we experienced $146 million in deposit growth, while loans decreased $160 million, thereby creating $306 million in additional liquidity. Additionally, the receipt of $65 million in proceeds from the January 2009 sale of preferred stock to the US Treasury improved our liquidity. There was no significant impact on our liquidity as a result of the Cooperative acquisition. Our liquid assets (cash and securities) as a percentage of our total deposits and borrowings increased from 16.5% at December 31, 2008 to 17.8% at December 31, 2009. In addition, the growth in our deposits has lessened our reliance on borrowings, which declined by $190 million during 2009.

As discussed above, in 2010 our FHLB line of credit was reduced from approximately $687 million to $335 million as a result of a recent collateral audit. However, we continue to believe our liquidity sources, including unused lines of credit, are at an acceptable level and remain adequate to meet our operating needs in the foreseeable future. We will continue to monitor our liquidity position carefully and will explore and implement strategies to increase liquidity if deemed appropriate.

In the normal course of business we have various outstanding contractual obligations that will require future

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cash outflows. In addition, there are commitments and contingent liabilities, such as commitments to extend credit, that may or may not require future cash outflows.

Table 18 reflects our contractual obligations and other commercial commitments outstanding as of December 31, 2009. Any of our $130 million in outstanding borrowings with the FHLB may be accelerated immediately by the FHLB in certain circumstances, including material adverse changes in our condition or if our qualifying collateral is less than the amount required under the terms of the borrowing agreement.

In the normal course of business there are various outstanding commitments and contingent liabilities such as commitments to extend credit, which are not reflected in the financial statements. As of December 31, 2009, we have outstanding unfunded loan and credit card commitments of $315,723,000, of which $274,817,000 were at variable rates and $40,906,000 were at fixed rates. Included in outstanding loan commitments were unfunded commitments of $214,249,000 on revolving credit plans, of which $183,410,000 were at variable rates and $30,839,000 were at fixed rates.

At December 31, 2009 and 2008, we had $7,646,000 and $8,297,000, respectively, in standby letters of credit outstanding. We had no carrying amount for these standby letters of credit at either of those dates. The nature of the standby letters of credit is that of a guarantee made on behalf of our customers to suppliers of the customers to guarantee payments owed to the supplier by the customer. The standby letters of credit are generally for terms of one year, at which time they may be renewed for another year if both parties agree. The payment of the guarantees would generally be triggered by a continued nonpayment of an obligation owed by the customer to the supplier. The maximum potential amount of future payments (undiscounted) we could be required to make under the guarantees in the event of nonperformance by the parties to whom credit or financial guarantees have been extended is represented by the contractual amount of the financial instruments discussed above. In the event that we are required to honor a standby letter of credit, a note, already executed by the customer, becomes effective providing repayment terms and any collateral. Over the past ten years, we have had to honor one standby letter of credit, which was repaid by the borrower without any loss to us. We expect any draws under existing commitments to be funded through normal operations.

It has been our experience that deposit withdrawals are generally replaced with new deposits, thus not requiring any net cash outflow. Based on that assumption, management believes that it can meet its contractual cash obligations and existing commitments from normal operations.

We are not involved in any legal proceedings that, in management's opinion, could have a material effect on the consolidated financial position of the Company.

Capital Resources and Shareholders' Equity

Shareholders' equity at December 31, 2009 amounted to $342.4 million compared to $219.9 million at December 31, 2008. The two basic components that typically have the largest impact on our shareholders' equity are net income, which increases shareholders' equity, and dividends declared, which decreases shareholders' equity. Additionally, any stock issuances can significantly increase shareholders' equity.

In 2009, the most significant item that impacted our equity was our issuance of $65 million in preferred stock to the U.S. Treasury in connection with our participation in the Treasury's Capital Purchase Program (see below). In addition, other significant factors were net income of $60.3 million, which increased equity, while common stock dividends declared of $5.3 million and preferred stock dividends declared of $3.2 million reduced equity. See the Consolidated Statements of Shareholders' Equity within the consolidated financial statements for disclosure of other less significant items affecting shareholders' equity.

In connection with our participation in the U.S. Treasury's Capital Purchase Program, in January 2009 we issued $65 million in preferred stock and $4.6 million in common stock warrants. We recorded a discount on the

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issuance of the preferred stock of $4.6 million, of which we amortized $0.8 million in 2009 as a reduction of retained earnings. Our issuance of the preferred stock to the U.S. Treasury has several restrictions and is generally assumed to be only a temporary source of capital, as it is expected that banks will redeem the preferred stock when they are able to do so.

We participated in the Capital Purchase Program for several reasons – 1) the capital markets were effectively closed, 2) without access to capital, our growth potential was limited, and 3) to provide an extra capital cushion in light of the worsening economy. In addition, the capital was offered by the government on attractive financial terms, with the 5% dividend being the most significant. By contrast, the market dividend rate for similar types of bank preferred stock was over 12%. In hindsight, we believe our participation turned out to be the correct decision, as it provided the capital we needed to bid on Cooperative and it also continues to serve as insurance against an economy that continues to struggle. In light of continued economic concerns, we have no immediate plans to redeem this stock. As we gain confidence in the economic recovery, we may elect to redeem this stock in installments. The favorable dividend rate of 5% is in effect for another four years before it increases to 9%. In addition to earnings, a common stock offering is a way that many banks have increased shareholders' equity. While we do not rule out the possibility of a common stock offering to provide proceeds for redemption of the preferred stock, we do not have any current plans for an offering. We are however, proposing to shareholders at this year's annual meeting to increase the number of shares authorized for issuance.

As previously noted, common stock dividends for 2009 amounted to $5.3 million, or $0.32 per share. This was a reduction from the 2008 amount of $12.2 million, or $0.76 per share. In February 2009, after careful deliberation, we reluctantly decided that it was necessary to reduce the Company's quarterly dividend from $0.19 per share to $0.08 per share. This decision was made in order to conserve capital amid worsening economic conditions.

In 2008, net income of $22.0 million increased equity, while dividends declared of $12.2 million reduced equity. We also issued $37.6 million in common stock in our acquisition of Great Pee Dee. In 2007, net income of $21.8 million increased equity, while dividends declared of $10.9 million reduced equity. See the consolidated financial statements for other less significant factors that impacted equity in 2007 and 2008.

We are not aware of any recommendations of regulatory authorities or otherwise which, if they were to be implemented, would have a material effect on our liquidity, capital resources, or operations.

The Company and the Bank must comply with regulatory capital requirements established by the FRB and the FDIC. Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional discretionary, actions by regulators that, if undertaken, could have a direct material effect on the Company's financial statements. These capital standards require the Company and the Bank to maintain minimum ratios of "Tier 1" capital to total risk-weighted assets ("Tier I Capital Ratio") and total capital to risk-weighted assets ("Total Capital Ratio") of 4.00% and 8.00%, respectively. Tier 1 capital is comprised of total shareholders' equity, excluding unrealized gains or losses from the securities available for sale, less intangible assets, and total capital is comprised of Tier 1 capital plus certain adjustments, the largest of which for the Company and the Bank is the allowance for loan losses. Risk-weighted assets refer to the on- and off-balance sheet exposures of the Company and the Bank, adjusted for their related risk levels using formulas set forth in FRB and FDIC regulations.

In addition to the risk-based capital requirements described above, the Company and the Bank are subject to a leverage capital requirement, which calls for a minimum ratio of Tier 1 capital (as defined above) to quarterly average total assets ("Leverage Ratio) of 3.00% to 5.00%, depending upon the institution's composite ratings as determined by its regulators. The FRB has not advised the Company of any requirement specifically applicable to it.

Table 21 presents our regulatory capital ratios as of December 31, 2009, 2008, and 2007. Our capital ratios

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were relatively consistent from 2007 to 2008, while in 2009 our capital ratios increased significantly, primarily as a result of the preferred stock issuance discussed above. All of our capital ratios have significantly exceeded the minimum regulatory thresholds for all periods covered by this report.

In addition to the minimum capital requirements described above, the regulatory framework for prompt corrective action also contains specific capital guidelines for a bank's classification as "well capitalized." The specific guidelines are as follows – Tier I Capital Ratio of at least 6.00%, Total Capital Ratio of at least 10.00%, and a Leverage Ratio of at least 5.00%. If a bank falls below "well capitalized" status in any of these three ratios, it must ask for FDIC permission to originate or renew brokered deposits. The Bank's regulatory ratios exceeded the threshold for "well-capitalized" status at December 31, 2009, 2008, and 2007 – see Note 15 to the consolidated financial statements for a table that presents the Bank's regulatory ratios.

In addition to shareholders' equity, we have supplemented our capital in past years with trust preferred security debt issuances, which because of their structure qualify as regulatory capital. This was necessary in past years because our balance sheet growth outpaced the growth rate of our capital. Additionally, we have frequently purchased bank branches over the years that resulted in our recording intangible assets, which negatively impacted regulatory capital ratios. As discussed in "Borrowings" above, we have issued a total of $67.0 million in trust preferred securities since 2002, with the most recent issuance being a $25.8 million issuance that occurred in April 2006. We currently have $46.4 million in trust preferred securities outstanding.

Our goal is to maintain our capital ratios at levels no less than the "well-capitalized" thresholds set for banks. At December 31, 2009, our total risk-based capital ratio was 15.14% compared to the 10.00% "well-capitalized" threshold.

See "Supervision and Regulation" under "Business" above and Note 15 to the consolidated financial statements for discussion of other matters that may affect our capital resources.

Off-Balance Sheet Arrangements and Derivative Financial Instruments

Off-balance sheet arrangements include transactions, agreements, or other contractual arrangements pursuant to which we have obligations or provide guarantees on behalf of an unconsolidated entity. We have no off-balance sheet arrangements of this kind other than repayment guarantees associated with our trust preferred securities.

Derivative financial instruments include futures, forwards, interest rate swaps, options contracts, and other financial instruments with similar characteristics. We have not engaged in derivatives activities through December 31, 2009 and have no current plans to do so.

Return on Assets and Equity

Table 20 shows return on assets (net income divided by average total assets), return on common equity (net income divided by average common shareholders' equity), dividend payout ratio (dividends per share divided by net income per common share) and shareholders' equity to assets ratio (average total shareholders' equity divided by average total assets) for each of the years in the three-year period ended December 31, 2009.

Interest Rate Risk (Including Quantitative and Qualitative Disclosures About Market Risk – Item 7A.)

Net interest income is our most significant component of earnings. Notwithstanding changes in volumes of loans and deposits, our level of net interest income is continually at risk due to the effect that changes in general market interest rate trends have on interest yields earned and paid with respect to our various categories of earning assets and interest-bearing liabilities. It is our policy to maintain portfolios of earning assets and interest-bearing liabilities with

maturities and repricing opportunities that will afford protection, to the extent practical,

against wide interest rate fluctuations. Our exposure to interest rate risk is analyzed on a regular basis by management using standard GAP reports, maturity reports, and an asset/liability software model that simulates future levels of interest income and expense based on current interest rates, expected future interest rates, and various intervals of "shock" interest rates. Over the years, we have been able to maintain a fairly consistent yield on average earning assets (net interest margin). Over the past five calendar years, our net interest margin has ranged from a low of 3.74% (realized in 2008) to a high of 4.33% (realized in 2005). During that five year period, the prime rate of interest has ranged from a low of 3.25% (which was the rate as of December 31, 2009) to a high of 8.25%. The consistency of the net interest margin is aided by the relatively low level of long-term interest rate exposure that we maintain. At December 31, 2009, approximately 88% of our interest-earning assets are subject to repricing within five years (because they are either adjustable rate assets or they are fixed rate assets that mature) and substantially all of our interest-bearing liabilities reprice within five years.

Table 17 sets forth our interest rate sensitivity analysis as of December 31, 2009, using stated maturities for all instruments except mortgage-backed securities (which are allocated in the periods of their expected payback) and securities and borrowings with call features that are expected to be called (which are shown in the period of their expected call). As illustrated by this table, at December 31, 2009, we had $1.04 billion more in interest-bearing liabilities that are subject to interest rate changes within one year than earning assets. This generally would indicate that net interest income would experience downward pressure in a rising interest rate environment and would benefit from a declining interest rate environment. However, this method of analyzing interest sensitivity only measures the magnitude of the timing differences and does not address earnings, market value, or management actions. Also, interest rates on certain types of assets and liabilities may fluctuate in advance of changes in market interest rates, while interest rates on other types may lag behind changes in market rates. In addition to the effects of "when" various rate-sensitive products reprice, market rate changes may not result in uniform changes in rates among all products. For example, included in interest-bearing liabilities subject to interest rate changes within one year at December 31, 2009 are deposits totaling $1.01 billion comprised of NOW, savings, and certain types of money market deposits with interest rates set by management. These types of deposits historically have not repriced with, or in the same proportion, as general market indicators.

Overall we believe that in the near term (twelve months), net interest income will not likely experience significant downward pressure from rising interest rates. Similarly, we would not expect a significant increase in near term net interest income from falling interest rates. Generally, when rates change, our interest-sensitive assets that are subject to adjustment reprice immediately at the full amount of the change, while our interest-sensitive liabilities that are subject to adjustment reprice at a lag to the rate change and typically not to the full extent of the rate change. In the short-term (less than six months), this results in us being asset-sensitive, meaning that our net interest income benefits from an increase in interest rates and is negatively impacted by a decrease in interest rates. However, in the twelve-month horizon, the impact of having a higher level of interest-sensitive liabilities lessens the short-term effects of changes in interest rates.

From September 2007 to December 2008, in response to the declining economy, the Federal Reserve announced a series of interest rate reductions with rate cuts totaling 500 basis points and rates reaching historic lows. As noted above, our net interest margin is negatively impacted, at least in the short-term, by reductions in interest rates. In addition to the initial normal decline in net interest margin that we experience when interest rates are reduced (as discussed above), the cumulative impact of the magnitude of 500 basis points in interest rate cuts has continued to negatively impact our net interest margin, primarily due to our inability to cut a large portion of our interest-bearing deposits by any significant amount due to their already near-zero interest rate. Also, for many of our deposit products, including time deposits that have recently matured, we have been unable to lower the interest rates we pay our customers by the full 500 basis point interest rate decrease due to competitive pressures. The impact of the declining rate environment was mitigated by an initiative we began in late 2007 to add interest rate floors to our adjustable rate loans. At December 31, 2008, adjustable rate loans totaling $651 million (53% of all adjustable rate loans) had

reached their contractual floors and no longer subjected us to risk in the event of further rate cuts. The net impact of those factors was that our net interest margin steadily declined for most of 2008 and was 3.74% for the full year. In 2009, the Federal Reserve made no changes to the interest rates, which resulted in our net interest margin increasing as we were able to renew

matured time deposits at lower rates with only a minimal decrease in our asset yields. Our net interest margin increased in each of the last three quarters of 2009 and was 3.81% for the full year, a seven basis point increase from 2008.

Based on our most recent interest rate modeling, which assumes no changes in interest rates for 2010 (federal funds rate = 0.25%, prime = 3.25%), we project that our 2010 net interest margin will remain relatively consistent with the net interest margins recently realized. We expect lower deposit yields as higher yielding time deposits continue to mature, while we expect asset yields to decline as a result lower average loan balances and higher levels of nonaccrual loan balances. In addition to the assumption regarding interest rates, the aforementioned modeling is dependent on many other assumptions that could vary significantly from actual results, including, but not limited to: prepayment assumptions on fixed rate loans, loan growth, mix of loan growth, deposit growth, mix of deposit growth, and our ability to manage changes in rates earned on loans and paid on deposits, which will depend largely on actions taken by our competitors.

We have no market risk sensitive instruments held for trading purposes, nor do we maintain any foreign currency positions. Table 19 presents the expected maturities of our other than trading market risk sensitive financial instruments. Table 19 also presents the estimated fair values of market risk sensitive instruments as estimated in accordance with FASB Accounting Standards Codification (ASC) 820, “Fair Value Measurements and Disclosures.” Our assets and liabilities have estimated fair values that do not materially differ from their carrying amounts.

See additional discussion regarding net interest income, as well as discussion of the changes in the annual net interest margin, in the section entitled “Net Interest Income” above.

Inflation

Because the assets and liabilities of a bank are primarily monetary in nature (payable in fixed determinable amounts), the performance of a bank is affected more by changes in interest rates than by inflation. Interest rates generally increase as the rate of inflation increases, but the magnitude of the change in rates may not be the same. The effect of inflation on banks is normally not as significant as its influence on those businesses that have large investments in plant and inventories. During periods of high inflation, there are normally corresponding increases in the money supply, and banks will normally experience above average growth in assets, loans and deposits. Also, general increases in the price of goods and services will result in increased operating expenses.

Current Accounting Matters

We prepare our consolidated financial statements and related disclosures in conformity with standards established by, among others, the Financial Accounting Standards Board (the “FASB”). Because the information needed by users of financial reports is dynamic, the FASB frequently issues new rules and proposes new rules for companies to apply in reporting their activities. See Note 1(t) to our consolidated financial statements for a discussion of recent rule proposals and changes.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

The information responsive to this Item is found in Item 7 under the caption “Interest Rate Risk.”

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Table 1 Selected Consolidated Financial Data

($ in thousands, except per share and nonfinancial data)	Year Ended December 31,				
	2009	2008	2007	2006	2005
Income Statement Data					
Interest income	$ 155,991	147,862	148,942	129,207	101,429
Interest expense	48,895	61,303	69,658	54,671	32,838
Net interest income	107,096	86,559	79,284	74,536	68,591
Provision for loan losses	20,186	9,880	5,217	4,923	3,040
Net interest income after provision	86,910	76,679	74,067	69,613	65,551
Noninterest income	89,518	20,657	17,217	14,310	15,004
Noninterest expense	78,551	62,211	56,324	53,198	47,636
Income before income taxes	97,877	35,125	34,960	30,725	32,919
Income taxes	37,618	13,120	13,150	11,423	16,829
Net income	60,259	22,005	21,810	19,302	16,090
Preferred stock dividends and accretion	(3,972)	—	—	—	—
Net income available to common shareholders	56,287	22,005	21,810	19,302	16,090
Earnings per common share – basic	3.38	1.38	1.52	1.35	1.14
Earnings per common share – diluted	3.37	1.37	1.51	1.34	1.12
Per Share Data (Common)					
Cash dividends declared - common	$ 0.32	0.76	0.76	0.74	0.70
Market Price					
High	19.00	20.86	26.72	23.90	27.88
Low	6.87	11.25	16.40	19.47	19.32
Close	13.97	18.35	18.89	21.84	20.16
Stated book value – common	16.59	13.27	12.11	11.34	10.94
Tangible book value – common	12.35	9.18	8.56	7.76	7.48
Selected Balance Sheet Data (at year end)					
Total assets	$ 3,545,356	2,750,567	2,317,249	2,136,624	1,801,050
Loans	2,652,865	2,211,315	1,894,295	1,740,396	1,482,611
Allowance for loan losses	37,343	29,256	21,324	18,947	15,716
Intangible assets	70,948	67,780	51,020	51,394	49,227
Deposits	2,933,108	2,074,791	1,838,277	1,695,679	1,494,577
Borrowings	176,811	367,275	242,394	210,013	100,239

Total shareholders' equity	342,383	219,868	174,070	162,705	155,728
Selected Average Balances					
Assets	$ 3,097,137	2,484,296	2,139,576	1,922,510	1,709,380
Loans – Non-covered	2,176,153	2,117,028	1,808,219	1,623,188	1,422,419
Loans – Covered	298,892	—	—	—	—
Loans – Total	2,475,045	2,117,028	1,808,219	1,623,188	1,422,419
Earning assets	2,833,167	2,329,025	1,998,428	1,793,811	1,593,554
Deposits	2,549,709	1,985,332	1,780,265	1,599,575	1,460,620
Interest-bearing liabilities	2,497,304	2,019,256	1,726,002	1,537,385	1,359,744
Shareholders' equity	313,173	210,810	170,857	163,193	154,871
Ratios					
Return on average assets	1.82 %	0.89 %	1.02 %	1.00 %	0.94 %
Return on average common equity	22.55 %	10.44 %	12.77 %	11.83 %	10.39 %
Net interest margin (taxable-equivalent basis)	3.81 %	3.74 %	4.00 %	4.18 %	4.33 %
Equity to assets at year end	9.66 %	7.99 %	7.51 %	7.62 %	8.65 %
Tangible common equity to tangible assets	5.94 %	5.67 %	5.43 %	5.34 %	6.08 %
Loans to deposits at year end	90.45 %	106.58 %	103.05 %	102.64 %	99.20 %
Allowance for loan losses to total loans	1.41 %	1.32 %	1.13 %	1.09 %	1.06 %
Allowance for loan losses to non-covered loans	1.75 %	1.32 %	1.13 %	1.09 %	1.06 %
Nonperforming assets to total assets at year end	7.27 %	1.29 %	0.47 %	0.39 %	0.17 %
Non-covered nonperforming assets to total non-covered assets at year end	3.10 %	1.29 %	0.47 %	0.39 %	0.17 %
Net charge-offs to average total loans	0.49 %	0.24 %	0.16 %	0.11 %	0.14 %
Net charge-offs to average non-covered loans	0.56 %	0.24 %	0.16 %	0.11 %	0.14 %
Efficiency ratio	39.79 %	57.67 %	58.03 %	59.54 %	56.68 %
Nonfinancial Data					
Number of branches	91	74	70	68	61
Number of employees – Full time equivalents	764	650	614	620	578

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Table 2 Average Balances and Net Interest Income Analysis

	Year Ended December 31,								
	2009			2008			2007		
($ in thousands)	Average Volume	Avg. Rate	Interest Earned or Paid	Average Volume	Avg. Rate	Interest Earned or Paid	Average Volume	Avg. Rate	Interest Earned or Paid
Assets									
Loans (1)	$2,475,045	5.98 %	$148,007	$2,117,028	6.56 %	$138,878	$1,808,219	7.70 %	$139,323
Taxable securities	167,041	3.94 %	6,580	152,246	4.82 %	7,333	131,035	4.92 %	6,453
Non-taxable securities (2)	23,018	7.29 %	1,677	16,258	7.98 %	1,298	13,786	8.09 %	1,115
Short-term investments, primarily overnight funds	168,063	0.32 %	545	43,493	2.32 %	1,011	45,388	5.74 %	2,605
Total interest-earning assets	2,833,167	5.53 %	156,809	2,329,025	6.38 %	148,520	1,998,428	7.48 %	149,496
Cash and due from banks	42,350			39,627			38,906		
Bank premises and equipment, net	52,789			49,815			45,398		
Other assets	168,831			65,829			56,844		
Total assets	$3,097,137			$2,484,296			$2,139,576		
Liabilities and Equity									
NOW accounts	$244,863	0.29 %	$720	$197,459	0.19 %	$377	$192,407	0.37 %	$712
Money market accounts	429,068	1.52 %	6,537	309,917	2.36 %	7,311	239,258	3.31 %	7,929
Savings accounts	137,142	1.08 %	1,487	124,460	1.65 %	2,048	106,357	1.62 %	1,727
Time deposits >$100,000	745,159	2.54 %	18,908	532,566	4.00 %	21,308	450,801	5.03 %	22,687
Other time deposits	736,358	2.43 %	17,866	586,235	3.79 %	22,197	567,572	4.67 %	26,498
Total interest-bearing deposits	2,292,590	1.99 %	45,518	1,750,637	3.04 %	53,241	1,556,395	3.83 %	59,553
Securities sold under agreements to repurchase	53,537	1.37 %	736	42,097	2.15 %	903	39,220	3.76 %	1,476
Borrowings	151,177	1.75 %	2,641	226,522	3.16 %	7,159	130,387	6.62 %	8,629
Total interest-bearing	2,497,304	1.96 %	48,895	2,019,256	3.04 %	61,303	1,726,002	4.04 %	69,658

liabilities								
Non-interest-bearing deposits	257,119			234,695			223,870		
Other liabilities	29,541			19,535			18,847		
Shareholders' equity	313,173			210,810			170,857		
Total liabilities and shareholders' equity	$3,097,137			$2,484,296			$2,139,576		
Net yield on interest- earning assets and net interest income		3.81 %	$107,914		3.74 %	$87,217		4.00 %	$79,838
Interest rate spread		3.57 %			3.34 %			3.44 %	
Average prime rate		3.25 %			5.09 %			8.05 %	

(1) Average loans include nonaccruing loans, the effect of which is to lower the average rate shown. Interest earned includes recognized loan fees in the amounts of $144,000, $405,000, and $836,000 for 2009, 2008, and 2007, respectively.

(2) Includes tax-equivalent adjustments of $818,000, $658,000, and $554,000 in 2009, 2008, and 2007, respectively, to reflect the federal and state benefit of the tax-exempt securities (using a 39% combined tax rate), reduced by the related nondeductible portion of interest expense.

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Table 3 Volume and Rate Variance Analysis

(In thousands)	Year Ended December 31, 2009 Change Attributable to			Year Ended December 31, 2008 Change Attributable to		
	Changes in Volumes	Changes in Rates	Total Increase (Decrease)	Changes in Volumes	Changes in Rates	Total Increase (Decrease)
Interest income (tax-equivalent):						
Loans	$22,448	(13,319)	9,129	22,026	(22,471)	(445)
Taxable securities	648	(1,401)	(753)	1,033	(153)	880
Non-taxable securities	516	(137)	379	199	(16)	183
Short-term investments, primarily overnight funds	1,650	(2,116)	(466)	(76)	(1,518)	(1,594)
Total interest income	25,262	(16,973)	8,289	23,182	(24,158)	(976)
Interest expense:						
NOW accounts	115	228	343	14	(349)	(335)
Money Market accounts	2,313	(3,087)	(774)	2,004	(2,622)	(618)
Savings accounts	173	(734)	(561)	296	25	321
Time deposits>$100,000	6,950	(9,350)	(2,400)	3,693	(5,072)	(1,379)
Other time deposits	4,663	(8,994)	(4,331)	789	(5,090)	(4,301)
Total interest-bearing deposits	14,214	(21,937)	(7,723)	6,796	(13,108)	(6,312)
Securities sold under agreements to repurchase	201	(368)	(167)	85	(658)	(573)
Borrowings	(1,849)	(2,669)	(4,518)	4,700	(6,170)	(1,470)
Total interest expense	12,566	(24,974)	(12,408)	11,581	(19,936)	(8,355)
Net interest income (tax-equivalent)	$12,696	8,001	20,697	11,601	(4,222)	7,379

Changes attributable to both volume and rate are allocated equally between rate and volume variances.

Table 4 Noninterest Income

(In thousands)	Year Ended December 31, 2009	2008	2007
Service charges on deposit accounts	$13,854	13,535	9,988
Other service charges, commissions, and fees	4,848	4,392	3,902
Fees from presold mortgages	1,505	869	1,135
Commissions from sales of insurance and financial products	1,524	1,552	1,511
Data processing fees	139	167	204
Total core noninterest income	21,870	20,515	16,740
Gain from acquisition	67,894	—	—
Securities gains (losses), net	(104)	(14)	487
Other gains (losses), net	(142)	156	(10)
Total	$89,518	20,657	17,217

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Table 5 Noninterest Expenses

(In thousands)	Year Ended December 31, 2009	2008	2007
Salaries	$30,745	28,127	26,227
Employee benefits	10,843	7,319	7,443
Total personnel expense	41,588	35,446	33,670
Occupancy expense	6,071	4,175	3,795
Equipment related expenses	4,334	4,105	3,809
Amortization of intangible assets	630	416	374
Acquisition expenses	1,343	—	—
FDIC insurance expense	5,500	1,157	100
Stationery and supplies	2,181	1,903	1,593
Telephone	1,847	1,349	1,246
Non-credit losses	255	200	204
Other operating expenses	14,802	13,460	11,533
Total	$78,551	62,211	56,324

Table 6 Income Taxes

(In thousands)	2009	2008	2007
Current - Federal	$11,190	11,978	11,625