2015 | Annual Report

Peoples Bancorp
OF NORTH CAROLINA, INC.

2015
ANNUAL REPORT

OUR VISION
To be the **Bank of Choice** in our **communities**, including **employees**, **customers** and **shareholders**.

Peoples Bancorp
OF NORTH CAROLINA, INC.

Lance A. Sellers
President and Chief Executive Officer

FROM THE PRESIDENT

For the one hundred and third year, Peoples Bancorp of North Carolina, Inc., is pleased to present an Annual Report of business activity. We are very aware that shareholder loyalty along with the outstanding performance of the Company's employees have made it possible for us to be successful for such a long time.

The highlight of this year's Annual Report would be our earnings, which were the highest annual earnings in the history of the Company. Net earnings for last year were $9.6 million. You'll see more performance results in the paragraphs below.

Year-to-date net earnings as of December 31, 2015 were $9.6 million, or $1.73 basic net earnings per share and $1.72 diluted net earnings per share, as compared to $9.4 million, or $1.67 basic net earnings per share and $1.66 diluted net earnings per share for the same period one year ago. The increase in year-to-date earnings is primarily attributable to an increase in net interest income and an increase in non-interest income, which were partially offset by a decrease in the credit to the provision for loan losses and an increase in non-interest expense. The Bank continues to make progress in addressing the issues identified in the FDIC Consent Order issued in August, 2015 and expects that it will be able to undertake and implement all required actions within the required time period.

An ongoing focus for us is the preservation of our capital base. We are committed to maintaining a capital ratio that exceeds regulatory guidelines and results in our designation as a "well-capitalized" financial institution. So we are glad to report, as of December 31, 2015 shareholders' equity was $104.9 million, or 10.1% of total assets, compared to $98.7 million, or 9.5% of total assets, as of December 31, 2014. This increase is primarily due to an increase in retained earnings due to net income, which was partially offset by a decrease in common stock due to 102,050 shares of common stock repurchased during 2015 under the Company's stock repurchase program implemented in September 2014.

Total assets were $1.0 billion as of December 31, 2015 and 2014. Non-performing assets declined to $9.2 million or 0.88% of total assets at December 31, 2015, compared to $12.7 million or 1.2% of total assets at December 31, 2014. The decline in non-performing assets is due to a $2.3 million decrease in non-accrual loans and a $1.3 million decrease in other real estate owned properties. The allowance for loan losses at December 31, 2015 was $9.6 million or 1.4% of total loans, compared to $11.1 million or 1.7% of total loans at December 31, 2014. Management believes the current level of the allowance for loan losses is adequate; however, there is no assurance that additional adjustments to the allowance will not be required because of changes in economic conditions, regulatory requirements or other factors.

Deposits amounted to $832.2 million as of December 31, 2015, compared to $814.7 million at December 31, 2014. Core deposits, which include noninterest-bearing demand deposits, NOW, MMDA, savings and non-brokered certificates of deposit of denominations less than $250,000, increased $45.4 million to $801.2 million at December 31, 2015, as compared to $755.8 million at December 31, 2014. We are pleased with the continued level of growth in core deposits as such deposits represent the most cost effective way to fund our earning assets. Certificates of deposit in amounts of $250,000 or more totaled $26.9 million at December 31, 2015, as compared to $47.9 million at December 31, 2014. The decrease in certificates of deposit in amounts of $250,000 or more is attributable to a $7.1 million decrease in wholesale certificates of deposit combined with a decrease in retail certificates of deposit which was expected as part of the Bank's pricing strategy to allow maturing high cost certificates of deposit to roll-off.

Our Bank's vision is to become "the Bank of Choice" in all the communities we serve. We're encouraged that our past performance indicates we are the right bank at the right time for many of the families and businesses in our footprint. We continue to make the investment in products, services and people to accomplish our mission, which is to provide exceptional customer service while selling to customer needs. Our employees consistently earn high marks from our customers, and I want to congratulate each of them for the hard work to make our Company a success.

The Directors of Peoples Bancorp play a direct and critical role in the success of our Company. They consistently look for ways to enhance shareholder value by their diligence and hard work. Please join me in thanking them for their commitment.

In addition to the Bank, which operates as a wholly owned subsidiary of the Company, we would like to remind you of our three subsidiary companies:

Peoples Investment Services, Inc., licensed financial advisors who provide access to investment products, which include stocks, bonds, mutual funds, annuities, and other suitable monetary investments through our affiliation with Raymond James Financial Services, Inc.

Real Estate Advisory Services, Inc., which provides real estate appraisals (both residential and commercial) to Peoples Bancorp's market area, thereby becoming a valued partner with respect to mortgage-related transactions.

Community Bank Real Estate Solutions, LLC, created in response to the Dodd-Frank Act to assist community banks across the country with appraisal management services.

The Annual Shareholders Meeting is scheduled for Thursday, May 5, 2016, at the Catawba Country Club beginning at 11:00 A.M. I hope each and every shareholder will attend the Annual Meeting. I want to express my appreciation for the loyalty and support of each of our shareholders, whom we hope will recommend our Bank and subsidiary companies to members of their communities.

Sincerely,

Lance A. Sellers

President and Chief Executive Officer

REPORT OF AUDIT

elliott davis decosimo

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders
Peoples Bancorp of North Carolina, Inc.
Newton, North Carolina

We have audited in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of Peoples Bancorp of North Carolina, Inc. and subsidiaries as of December 31, 2015, and the related consolidated statement of earnings, comprehensive income, shareholders' equity, and cash flow for the year then ended; and in our report dated March 14, 2016, we expressed an unqualified opinion on those consolidated financial statements.

In our opinion, the information set forth in the accompanying condensed consolidated financial statements is fairly stated, in all material respects, in relation to the consolidated financial statements from which it has been derived.

Elliott Davis Decosimo, PLLC

Charlotte, North Carolina
March 14, 2016

Elliott Davis Decosimo PLLC | Elliott Davis Decosimo LLC | www.elliottdavis.com

REPORT OF AUDIT

Porter Keadle Moore
CPAs | Advisors | www.pkm.com

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders
Peoples Bancorp of North Carolina, Inc.
Newton, North Carolina

We have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of Peoples Bancorp of North Carolina, Inc. as of December 31, 2014, and the related consolidated statements of earnings, comprehensive income (loss), changes in shareholders' equity and cash flows for the year ended (not presented herein); and in our report dated March 25, 2015, we expressed an unqualified opinion on those consolidated financial statements.

In our opinion, the information set forth in the accompanying 2014 condensed consolidated financial statements is fairly stated, in all material respects, in relation to the basic 2014 consolidated financial statements from which it has been derived.

Porter Keadle Moore, LLC

Atlanta, Georgia
March 25, 2015

235 Peachtree Street, NE | Suite 1800 | Atlanta, GA 30303 | Phone 404.588.4200 | 404.588.4222
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CONSOLIDATED BALANCE SHEETS

December 31, 2015 and 2014 (dollars in thousands)

		2015	2014
ASSETS			
Cash and due from banks, including reserve requirements of $14,587 at 12/31/15 and $12,569 at 12/31/14	$	29,194	51,213
Interest-bearing deposits		10,569	17,885
Cash and cash equivalents		39,763	69,098
Investment securities available for sale		268,530	281,099
Other investments		3,636	4,031
Total securities		272,166	285,130
Mortgage loans held for sale		4,149	1,375
Loans		689,091	651,891
Less allowance for loan losses		(9,589)	(11,082)
Net loans		679,502	640,809
Premises and equipment, net		16,976	17,000
Cash surrender value of life insurance		14,546	14,125
Other real estate		739	2,016
Accrued interest receivable and other assets		10,640	10,941
Total assets	$	1,038,481	1,040,494
LIABILITIES AND SHAREHOLDERS' EQUITY			
Deposits:			
Non-interest bearing demand	$	244,231	210,758
NOW, MMDA & savings		431,052	407,504
Time, $250,000 or more		26,891	47,872
Other time		130,001	148,566
Total deposits		832,175	814,700
Securities sold under agreements to repurchase		27,874	48,430
FHLB borrowings		43,500	50,000
Junior subordinated debentures		20,619	20,619
Accrued interest payable and other liabilities		9,449	8,080
Total liabilities		933,617	941,829
Commitments			
Shareholders' equity:			
Series A preferred stock, $1,000 stated value; authorized 5,000,000 shares; no shares issued and outstanding		—	—
Common stock, no par value; authorized 20,000,000 shares; issued and outstanding 5,510,538 shares at 12/31/15 and 5,612,588 shares at 12/31/14		46,171	48,088
Retained earnings		53,183	45,124
Accumulated other comprehensive income		5,510	5,453
Total shareholders' equity		104,864	98,665
Total liabilities and shareholders' equity	$	1,038,481	1,040,494

See Appendix A to the Peoples Bancorp of North Carolina, Inc. Proxy Statement, dated March 25, 2016, for a complete set of Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF EARNINGS

For the Years Ended December 31, 2015, 2014 and 2013
(dollars in thousands, except per share amounts)

		2015	2014	2013
INTEREST INCOME:				
Interest and fees on loans	$	31,098	30,305	30,194
Interest on due from banks		26	65	85
Interest on investment securities:				
U.S. Government sponsored enterprises		2,616	2,995	1,639
States and political subdivisions		4,600	4,677	4,427
Other		326	378	351
Total interest income		38,666	38,420	36,696
INTEREST EXPENSE:				
NOW, MMDA & savings deposits		432	499	732
Time deposits		870	1,188	1,650
FHLB borrowings		1,735	2,166	2,518
Junior subordinated debentures		402	389	398
Other		45	45	55
Total interest expense		3,484	4,287	5,353
Net interest income		35,182	34,133	31,343
(Reduction of) provision for loan losses		(17)	(699)	2,584
Net interest income after provision for loan losses		35,199	34,832	28,759
NON-INTEREST INCOME:				
Service charges		4,647	4,961	4,566
Other service charges and fees		931	1,080	1,172
Gain on sale of securities		—	266	614
Mortgage banking income		1,130	804	1,228
Insurance and brokerage commissions		714	701	661
Gain/(loss) on sales and write-downs of other real estate		245	(622)	(581)
Miscellaneous		5,645	4,974	4,992
Total non-interest income		13,312	12,164	12,652
NON-INTEREST EXPENSE:				
Salaries and employee benefits		18,285	17,530	16,851
Occupancy		6,288	6,251	5,539
Professional fees		1,468	1,401	1,088
Advertising		784	804	685
Debt card expense		988	905	823
FDIC insurance		681	739	864
Other		7,284	8,041	6,991
Total non-interest expense		35,778	35,671	32,841
Earnings before income taxes		12,733	11,325	8,570
Income tax expense		3,100	1,937	1,879
Net earnings		9,633	9,388	6,691
Dividends and accretion of preferred stock		—	—	656
Net earnings available to common shareholders	$	9,633	9,388	6,035
Basic net earnings per common share	$	1.73	1.67	1.08
Diluted net earnings per common share	$	1.72	1.66	1.07
Cash dividends declared per common share	$	0.28	0.18	0.12

See Appendix A to the Peoples Bancorp of North Carolina, Inc. Proxy Statement, dated March 25, 2016, for a complete set of Consolidated Financial Statements.

DIRECTORS AND OFFICERS

Peoples Bank and Peoples Bancorp Board of Directors

Robert C. Abernethy
Chairman of the Board
Peoples Bancorp of North Carolina, Inc.
and Peoples Bank
President, Secretary and Treasurer
Carolina Glove Company, Inc.

James S. Abernethy
President and Assistant Secretary
Midstate Contractors, Inc.

Douglas S. Howard
Vice President, Secretary and Treasurer
Denver Equipment of Charlotte, Inc.

John W. Lineberger, Jr.
President
Lincoln Bonded Warehouse Company

Gary E. Matthews
President and Director
Matthews Construction Company, Inc.

Billy L. Price, Jr., M.D.
Practitioner of Internal Medicine
BL Price Medical Consultants, PLLC

Larry E. Robinson
President and Chief Executive Officer
The Blue Ridge Distributing Company, Inc.

W. Gregory Terry
General Manager
Drum and Willis-Reynolds
Funeral Homes and Crematory

Dan Ray Timmerman, Sr.
Chairman of the Board and
Chief Executive Officer
Timmerman Manufacturing, Inc.

Benjamin I. Zachary
President, Treasurer, General Manager
and Director, Alexander Railroad
Company

Peoples Bancorp Officers

Lance A. Sellers
President and
Chief Executive Officer

A. Joseph Lampron, Jr.
Executive Vice President, Chief Financial
Officer, Corporate Treasurer and
Assistant Corporate Secretary

William D. Cable, Sr.
Executive Vice President,
Corporate Secretary and Assistant
Corporate Treasurer

Peoples Bank Officers

Lance A. Sellers
President and Chief Executive
Officer

A. Joseph Lampron, Jr.
Executive Vice President,
Chief Financial Officer

William D. Cable, Sr.
Executive Vice President,
Chief Operating Officer

Kimberly L. Boyd
Senior Vice President,
Chief Banking Support Officer

Jeffrey P. Gniadek
Senior Vice President, Area
Executive

Rafael Intriago
Senior Vice President,
Banco de la Gente Retail Director

Walter C. Joyce
Senior Vice President,
Chief Technology Director

James O. Perry
Senior Vice President,
Chief Retail Officer

David E. Reitzel
Senior Vice President,
Real Estate Administration

Daniel F. Richard
Senior Vice President,
Area Executive, Triangle

Mark W. Sigmon
Senior Vice President,
Area Executive, Denver

Timothy P. Turner
Senior Vice President,
Commercial Credit

Angela J. Abernethy
First Vice President, Treasury
Management Manager

Kimberly D. Bazzle
First Vice President,
Marketing Director

J. LaShae Bock
First Vice President,
Human Resources Director

David C. Brown
First Vice President,
Certified Financial Planner

George S. Earp
First Vice President, Finance
Director

Jan G. Griffin
First Vice President,
Loan Operations Director

Leslie D. Hambrick
First Vice President, Internal
Auditor

M. Beth LaBarbera
First Vice President,
Regional Sales Manager

Connie P. Ollis
First Vice President,
Compliance/Security Officer

Lucretia K. Rogers
First Vice President,
Regional Sales Manager

Carol S. Shinn
First Vice President, Deposit
Operations Director

Robert C. Sieg
First Vice President, BSA Officer

Kyle E. Sigmon
First Vice President, Consumer
Credit

Jody G. Street
First Vice President,
Area Executive, Newton

Ryan M. Waddle
First Vice President, Business
Development Officer, Mooresville

Carol R. Allen
Vice President, Business Center
Manager, Maiden

Suzanne I. Blackwell
Vice President, Mortgage Sales
Manager

Velvet L. Burton
Vice President, Service Center
Manager

Martha P. Connors
Vice President, Banco de la Gente,
Regional Sales Manager

Wendy E. Cordero
Vice President, Banco de la Gente
Mortgage Manager

Kay F. Deal
Vice President, Business Center
Manager, Conover

Roger G. Decato
Vice President, Business
Development Officer, Newton

Zachary M. Dellinger
Vice President, Business
Development Officer, Lincolnton

James R. Durham
Vice President, Financial Advisor

Heather N. Edwards
Vice President, Business Center
Manager, Mooresville

Barbara W. Erwin
Vice President, Commercial Credit

Tommie A. Hall
Vice President, Loan
Documentation

Lamona J. Harbinson
Vice President, Electronic Banking
Manager

Maria F. Hoyos
Vice President, Banco de la Gente,
Regional Sales Manager

Paul B. Jones
Vice President, Mortgage
Underwriter

David S. Lewis, Jr.
Vice President, Business
Development Officer, Viewmont

Brenda K. Mash
Vice President, Business Center
Manager, Denver

Bruce E. Meisner
Vice President, REAS Manager

Vickie E. Miller
Vice President, Retail Support
Coordinator

Tammy L. Mitchell
Vice President, Learning &
Development Manager

Wendy H. Moran
Vice President, Business
Development Officer, Cornelius

John J. Noonan
Vice President, CBRES Manager

Paula M. Parker
Vice President, Business Center
Manager, Catawba Valley Blvd

Wesley S. Pittman
Vice President, Business Center
Manager, Lincolnton/West Lincoln

Lynn H. Poole
Vice President, Business Center
Manager, Catawba

Krissy O. Price
Vice President, Assistant Corporate
Secretary

Andrew R. Puntch
Vice President, Application &
Project Management Manager

Jeanette R. Ringley
Vice President, Business Center
Manager, Newton

Sandra B. Shuford
Vice President, Data Management
Manager

Shawn D. Sigmon
Vice President, Mortgage
Department Manager

John W. Somers
Vice President, Business Center
Manager, Lincolnton

Robert D. Spencer
Vice President, Business Center
Manager, Viewmont

Dominick Vertorano
Vice President, Business Center
Manager, Cornelius

Allison J. Taylor
Vice President, Business Center
Manager, Springs Road

Lisa G. Treadaway
Vice President, Organizational
Architect

Adam P. Turbyfill
Vice President, Business
Development Officer, Triangle

SUBSIDIARIES

Peoples Bancorp Subsidiary Board of Directors and Officers

Community Bank Real Estate Solutions, LLC

Board of Directors
Robert C. Abernethy
David E. Reitzel
Dan Ray Timmerman, Sr.
Lance A. Sellers

Officers
David E. Reitzel - President
Lance A. Sellers - Vice President
John Noonan – Vice President
Krissy O. Price - Secretary
A. Joseph Lampron, Jr. – Treasurer

Peoples Bank Subsidiaries' Board of Directors and Officers

Peoples Investment Services, Inc.

Board of Directors
Robert C. Abernethy
Billy L. Price, Jr., M.D.
David C. Brown
Larry E. Robinson
Douglas S. Howard
Lance A. Sellers
William D. Cable, Sr.

Officers
Lance A. Sellers - President
David C. Brown - Vice President and Assistant Secretary
Krissy O. Price - Secretary
A. Joseph Lampron, Jr. – Treasurer

Real Estate Advisory Services, Inc.

Board of Directors
Robert C. Abernethy
Dan Ray Timmerman, Sr.
David E. Reitzel
Lance A. Sellers

Officers
David E. Reitzel – President
Lance A. Sellers – Vice President
Bruce Meisner – Vice President
Krissy O. Price – Secretary
A. Joseph Lampron, Jr. – Treasurer

SHAREHOLDER AND GENERAL INFORMATION

Annual Meeting

The Annual Meeting of Shareholders of Peoples Bancorp will be held at 11:00 a.m. on Thursday, May 5, 2016, at the Catawba Country Club located at 1154 Country Club Road, Newton, North Carolina.

Shareholders' Luncheon

Shareholders in attendance at the Annual Meeting are cordially invited to remain for a luncheon to be served immediately upon adjournment.

Common Stock

Peoples Bancorp common stock is listed on the NASDAQ (National Association of Securities Dealers Automated Quotations) Global Market, where our symbol is PEBK.

Dividend Reinvestment & Stock Purchase

Peoples Bancorp offers a Dividend Reinvestment and Stock Purchase Plan for the benefit of the Company's shareholders. The Plan provides for the full or partial reinvestment of cash dividends, optional cash purchases of the Company's stock, safekeeping of the share certificates, liquidation of shares, and gifting of shares and enrollment of the designated recipients.

Broadridge Corporate Issuer Solutions, Inc. is the Plan Administrator. For more information, one may call Peoples Bancorp at 828-464-5620 or 800-948-7195 or contact the Plan Administrator at 855-263-4988.

Shareholders of Peoples Bancorp are entitled to receive dividends when and as declared by the Board of Directors out of funds legally available therefore.

Such dividend payments are declared based upon the guidelines of North Carolina and federal banking law.

Corporate Office

Peoples Bancorp of North Carolina, Inc.
518 West C Street
PO Box 467
Newton, NC 28658
828-464-5620

Stock Transfer Agent & Registrar

Broadridge Corporate Issuer Solutions, Inc.
P.O. Box 1342
Brentwood, NY 11717
www.broadridge.com

Independent Auditors

Elliott Davis Decosimo, PLLC
700 East Morehead Street, Suite 400
Charlotte, NC 28202

Peoples Bancorp
OF NORTH CAROLINA, INC.

CORE VALUES

Employees
We are valued so we add value.

Integrity
We are fair and truthful.

Exceptional Customer Service
We surpass our customers' expectations.

Accountability
We are accountable for our own actions and each other.

Progressive and Positive
We see change as an opportunity.

Catawba
106 North Main Street
Catawba, NC 28609
(828) 241-3123

Catawba Valley Boulevard
2050 Catawba Valley Blvd. SE
Hickory, NC 28602
(828) 322-6372

Claremont
3261 East Main Street
Claremont, NC 28610
(828) 459-7152

Conover
213 1st Street West
Conover, NC 28613
(828) 464-8456

Cornelius
9624-I Bailey Road
Cornelius, NC 28031
(704) 237-9270

Denver
6125 Highway 16 South
Denver, NC 28037
(704) 483-3050

Hiddenite
5153 NC Highway 90 East
Hiddenite, NC 28636
(828) 632-0118
(704) 585-6631

Lincolnton
1910 East Main Street
Lincolnton, NC 28092
(704) 732-0097

Maiden
200 Island Ford Road
Maiden, NC 28650
(828) 428-9874

Mooresville
1074 River Highway
Mooresville, NC 28117
(704) 658-3600

Newton
420 West A Street
Newton, NC 28658
(828) 464-5663

Springs Road
3310 Springs Road NE
Hickory, NC 28601
(828) 256-9229

Triangle
142 Highway 16 South
Denver, NC 28037
(704) 483-7727
(704) 827-2370

Viewmont
1333 2nd Street NE
Hickory, NC 28601
(828) 345-6262

West Lincoln
760 Highway 27 West
Lincolnton, NC 28092
(704) 736-1447

Abernethy Laurels
Satellite Location
102 Leonard Avenue
Newton, NC 28658
(828) 464-3077

Denver Loan Production Office
3754 Highway 16 North
Denver, NC 28037
(704) 489-8940

Banco de la Gente
6350 South Boulevard
Charlotte, NC 28217
(704) 554-7494

Banco de la Gente
4451-A Central Avenue
Charlotte, NC 28205
(704) 531-4571

Banco de la Gente
501 West Roosevelt Boulevard
Monroe, NC 28110
(704) 261-2020

Banco de la Gente
3023-105 Capital Boulevard
Raleigh, NC 27604
(919) 747-8000

Banco de la Gente
Loan Production Office
2000 Avondale Drive
Durham, NC 27704
(919) 747-8003

Banco de la Gente
Loan Production Office
3015 Waughtown Street
Winston-Salem, NC 27107
(336) 602-9704

Peoples Bancorp Center
518 West C Street
PO Box 467
Newton, NC 28658
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TheRealPeoplesBank.com