NEW PEOPLES BANKSHARES INC

Financial Report

Second Quarter 2012

NEW PEOPLES BANKSHARES, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE SIX MONTHS ENDED JUNE 30, 2012 AND 2011
(IN THOUSANDS EXCEPT SHARE AND PER SHARE DATA)
(UNAUDITED)

	2012	2011
INTEREST AND DIVIDEND INCOME		
Loans including fees	$ 16,795	$ 21,402
Federal funds sold	1	9
Interest-earning deposits with banks	95	80
Investments	441	84
Dividends on equity securities (restricted)	55	50
Total Interest and Dividend Income	17,387	21,625
INTEREST EXPENSE		
Deposits		
Demand	54	89
Savings	120	324
Time deposits below $100,000	1,657	2,630
Time deposits above $100,000	1,112	1,574
FHLB Advances	331	444
Other borrowings	88	105
Trust Preferred Securities	247	200
Total Interest Expense	3,609	5,366
NET INTEREST INCOME	13,778	16,259
PROVISION FOR LOAN LOSSES	3,126	3,457
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	10,652	12,802
NONINTEREST INCOME		
Service charges	1,199	1,159
Fees, commissions and other income	1,188	1,019
Insurance and investment fees	232	191
Net realized gains on sale of investment securities	337	-
Life insurance investment income	145	176
Total Noninterest Income	3,101	2,545
NONINTEREST EXPENSES		
Salaries and employee benefits	7,107	7,859
Occupancy and equipment expense	2,184	2,144
Advertising and public relations	211	183
Data processing and telecommunications	889	798
FDIC insurance premiums	845	1,096
Other real estate owned and repossessed vehicles, net	3,247	2,490
Other operating expenses	2,756	2,660
Total Noninterest Expenses	17,239	17,230
LOSS BEFORE INCOME TAXES	(3,486)	(1,883)
INCOME TAX EXPENSE (BENEFIT)	1,587	(757)
NET LOSS	$ (5,073)	$ (1,126)
Loss Per Share		
Basic	$ (0.51)	$ (0.11)
Fully Diluted	$ (0.51)	$ (0.11)
Average Weighted Shares of Common Stock		
Basic	10,010,178	10,010,178
Fully Diluted	10,010,178	10,010,178

NEW PEOPLES BANKSHARES, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE THREE MONTHS ENDED JUNE 30, 2012 AND 2011
(IN THOUSANDS EXCEPT SHARE AND PER SHARE DATA)
(UNAUDITED)

	2012	2011
INTEREST AND DIVIDEND INCOME		
Loans including fees	$ 8,047	$ 10,514
Federal funds sold	1	-
Interest-earning deposits with banks	48	54
Investments	240	45
Dividends on equity securities (restricted)	29	28
Total Interest and Dividend Income	8,365	10,641
INTEREST EXPENSE		
Deposits		
Demand	28	44
Savings	58	138
Time deposits below $100,000	782	1,242
Time deposits above $100,000	525	769
FHLB Advances	150	223
Other borrowings	44	44
Trust Preferred Securities	125	92
Total Interest Expense	1,712	2,552
NET INTEREST INCOME	6,653	8,089
PROVISION FOR LOAN LOSSES	1,176	2,312
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	5,477	5,777
NONINTEREST INCOME		
Service charges	642	607
Fees, commissions and other income	573	445
Insurance and investment fees	123	93
Net realized gains on sale of investment securities	265	-
Life insurance investment income	31	89
Total Noninterest Income	1,634	1,234
NONINTEREST EXPENSES		
Salaries and employee benefits	3,509	3,946
Occupancy and equipment expense	1,085	1,119
Advertising and public relations	121	98
Data processing and telecommunications	450	392
FDIC insurance premiums	414	421
Other real estate owned and repossessed vehicles, net	1,273	2,246
Other operating expenses	1,400	1,395
Total Noninterest Expenses	8,252	9,617
LOSS BEFORE INCOME TAXES	(1,141)	(2,606)
INCOME TAX EXPENSE (BENEFIT)	1,397	(931)
NET LOSS	$ (2,538)	$ (1,675)
Loss Per Share		
Basic	$ (0.25)	$ (0.17)
Fully Diluted	$ (0.25)	$ (0.17)
Average Weighted Shares of Common Stock		
Basic	10,010,178	10,010,178
Fully Diluted	10,010,178	10,010,178

NEW PEOPLES BANKSHARES, INC.
CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS EXCEPT PER SHARE AND SHARE DATA)

ASSETS	June 30, 2012 (Unaudited)	December 31, 2011 (Audited)
Cash and due from banks	$ 16,957	$ 18,306
Interest-bearing deposits with banks	54,029	72,170
Federal funds sold	2	77
Total Cash and Cash Equivalents	70,988	90,553
Investment securities		
Available-for-sale	46,187	32,434
Loans receivable	554,103	597,816
Allowance for loan losses	(18,065)	(18,380)
Net Loans	536,038	579,436
Bank premises and equipment, net	32,763	33,141
Equity securities (restricted)	3,348	3,573
Other real estate owned	11,597	15,092
Accrued interest receivable	2,648	3,067
Life insurance investments	11,801	11,351
Goodwill and other intangibles	81	123
Deferred taxes	5,645	7,220
Other assets	4,519	4,394
Total Assets	$ 725,615	$ 780,384
LIABILITIES		
Deposits:		
Demand deposits:		
Noninterest bearing	$ 108,799	$ 109,629
Interest-bearing	63,326	58,459
Savings deposits	91,820	94,569
Time deposits	405,392	445,658
Total Deposits	669,337	708,315
Federal Home Loan Bank advances	7,158	17,983
Accrued interest payable	1,954	1,796
Accrued expenses and other liabilities	1,502	1,471
Other borrowings	5,450	5,450
Trust preferred securities	16,496	16,496
Total Liabilities	701,897	751,511
Commitments and contingencies	-	-
STOCKHOLDERS' EQUITY		
Common stock - $2.00 par value; 50,000,000 shares authorized; 10,010,178 shares issued and outstanding	20,020	20,020
Additional paid-in-capital	21,689	21,689
Retained earnings (deficit)	(18,158)	(13,085)
Accumulated other comprehensive income	167	249
Total Stockholders' Equity	23,718	28,873
Total Liabilities and Stockholders' Equity	$ 725,615	$ 780,384

Management's Discussion and Analysis of Financial Condition and Results of Operations

Caution About Forward Looking Statements
We make forward looking statements in this quarterly report that are subject to risks and uncertainties. These forward looking statements include statements regarding our profitability, liquidity, allowance for loan losses, interest rate sensitivity, market risk, business strategy, and financial and other goals. The words "believes," "expects," "may," "will," "should," "projects," "contemplates," "anticipates," "forecasts," "intends," or other similar words or terms are intended to identify forward looking statements.

Certain information contained in this discussion may include "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended and Section 21E of the Securities Exchange Act of 1934, as amended. These forward-looking statements contain the Company's expectations, plans, future financial performance, and other statements that are not historical facts. These forward-looking statements are generally identified by phrases such as "the Company expects," "the Company believes" or words of similar importance. Such forward-looking statements involve known and unknown risks including, but not limited to, changes in general economic and business conditions, interest rate fluctuations, competition within and from outside the banking industry, new products and services in the banking industry, risk inherent in making loans such as repayment risks and fluctuating collateral values, problems with technology utilized by the Company, changing trends in customer profiles and changes in laws and regulations applicable to the Company. Although the Company believes that its expectations with respect to the forward-looking statements are based upon reasonable assumptions within the bounds of its knowledge of its business and operations, there can be no assurance that actual results, performance or achievements of the Company will not differ materially from any future results, performance or achievements expressed or implied by such forward-looking statements.

Because of these uncertainties, our actual future results may be materially different from the results indicated by these forward looking statements. In addition, our past results of operations do not necessarily indicate our future results.

Overview - The Company had net loss for the quarter ended June 30, 2012 of $2.5 million as compared to a net loss of $1.7 million for the quarter ended June 30, 2011. Year-to-date June 30, 2012, the Company had a net loss of $5.1 million as compared to a net loss of $1.1 million for the same period in 2012. Basic net loss per share was $0.25 for the quarter ended June 30, 2012 as compared to basic net loss of $0.17 for the quarter ended June 30, 2011. Basic net loss per share was $0.51 for the six months ended June 30, 2012 as compared to net loss per share of $0.11 for the six months ended June 30, 2011. The net loss year-to-date is primarily the result of other real estate owned expenses of $3.2 million, of which $2.3 million is the result of other real estate owned properties writedowns, $3.1 million in loan loss provision, and a deferred tax valuation allowance of $2.9 million.

Total assets decreased to $725.6 million, or 7.02%, from $780.4 million at December 31, 2011. We intentionally are reducing our asset size in an attempt to improve our capital position and manage our net interest margin by reducing higher cost funding. We foresee total assets to continue shrinking in the near future as we manage to maintain a well-capitalized status under regulatory guidelines at the Bank level and return to well-capitalized on a consolidated basis. Depending upon the success of the common stock offering being conducted in the third and fourth quarters 2012, we may not shrink the Bank at the rate as in the recent past.

At June 30, 2012, the Company remained below the minimum capital requirement for regulatory well-capitalized status as a result of the Tier 1 leverage ratio decreasing to 3.72%, which was below the minimum requirement of 4.00%. At December 31, 2011, the ratio was 4.23%. The Tier 1 risk based ratio was 6.00% at June 30, 2012, compared to 6.57% at December 31, 2011. The Total risked based capital ratio was 9.07% at June 30, 2012, compared to 9.15% at December 31, 2011. We anticipate returning the Company to well capitalized status in the third quarter when we convert the $5.5 million notes payable to two Board members to common stock subject to regulatory approval which we anticipate receiving in the third quarter of 2012.

At June 30, 2012 the Bank remains well capitalized under the regulatory framework for prompt corrective action. The following ratios existed at June 30, 2012 for the Bank: Tier 1 leverage ratio of 5.82%, Tier 1 risk based capital ratio of 9.40%, and Total risk based capital ratio of 10.68%. The ratios were as follows at December 31, 2011: Tier 1 leverage ratio of 5.99%, Tier 1 risk based capital ratio of 9.28%, and Total risk based capital ratio of 10.56%.

In the second quarter of 2012, we experienced a decrease in our net interest margin to 4.02%, as compared to 4.28% for the same period in 2011. This is reflected in the $1.4 million decrease in net interest income during the second quarter of 2012 as compared to the same period in 2011 primarily related to the decreased loan portfolio and due to a one-time adjustment in which we reversed approximately $500 thousand in nonaccrual interest income from interest income and reduced the investment in nonaccrual loans.

Total loans decreased to $554.1 million at June 30, 2012 from $597.8 million at year end 2011. This is the result of charge offs of $3.6 million for the first half of 2012, resolution of problem loans, decreased loan demand, tighter underwriting guidelines, and the intentional shrinking of the loan portfolio to increase regulatory capital ratios. We continue to serve our customers, and although the total loan portfolio has shrunk, we have renewed existing credits and have made new loans to qualified borrowers as well. We anticipate continued decreases in the loan portfolio in the near future as we reduce our exposure to certain credit and market risks and decrease nonperforming loans. Increased focus is being made by the lending personnel to further develop new and existing lending relationships and will help slow the pace of total loans declining. Total deposits decreased $39.0 million from $708.3 million at December 31, 2011 to $669.3 million at June 30, 2012 as we have experienced shrinkage in time deposits due to the interest rate environment.

The deterioration of the residential and commercial real estate markets, as well as the extended recessionary period, have resulted in increases to our nonperforming assets. However, we are identifying potential problems early in an effort to minimize losses. The ratio of nonperforming assets to total assets is 7.69% at June 30, 2012 to 7.55% at December 31, 2011. Nonperforming assets, which include nonaccrual loans, other real estate owned and past due loans greater than 90 days still accruing interest, decreased to $56.0 million at June 30, 2012 from $58.9 million at December 31, 2011. The majority of these assets are real estate development projects and commercial real estate secured loans. We are working aggressively to reduce these totals primarily by working with the customer for additional collateral, or restructuring the debt. However, we also may have to foreclose, repossess collateral or take other prudent measures. We are uncertain how long these processes will take. We believe we are making good progress and the level of nonperforming assets slightly decreased in the second quarter. In the first six months of 2012, net charge offs were $3.4 million as compared to $9.9 million in the same period of 2011. The majority of the charge offs in the first six months of 2012 were related to real estate construction loans and commercial loans with collateral values that are dependent upon current market and economic conditions when these are ascertainable.

The provision for loan losses decreased $1.1 million, or 49.13%, to $1.2 million for the second quarter of 2012 as compared to $2.3 million in the same period for 2011. At June 30, 2012 our allowance for loan losses totaled $18.1 million, or 3.26% of total loans, as compared to $18.4 million, or 3.07% of total loans as of December 31, 2011. At June 30, 2011 our allowance for loan losses totaled $18.7 million, or 2.82% of total loans. The allowance for loan losses is being maintained at a level that management deems appropriate to absorb any potential future losses and known impairments within the loan portfolio whether or not the losses are actually ever realized. We continue to modify the allowance for loan loss model to best reflect the risks in the portfolio and the improvements made in our internal policies and procedures.

Critical Accounting Policies - For discussion of our significant accounting policies see our Annual Report on Form 10-K for the year ended December 31, 2011. Certain critical accounting policies affect the more significant judgments and estimates used in the preparation of our financial statements. Our most critical accounting policies relate to our provision for loan losses and the calculation of our deferred tax asset and valuation allowance.

Balance Sheet Changes - At June 30, 2012, total assets were $725.6 million, a decrease of $54.8 million, or 7.02%, over December 31, 2011. Total deposits decreased $39.0 million, or 5.50%, for the first six months of 2012 to $669.3 million from $708.3 million at December 31, 2011. Total loans decreased $43.7 million, or 7.49%, to $554.1 million at June 30, 2012 from $597.8 million at December 31, 2011.

Core deposits remained substantially at the same level as noninterest bearing deposits slightly decreased 0.76%, or $830 thousand, from $109.6 million at December 31, 2011 to $108.8 million at June 30, 2012. Overall, we continue to maintainecore deposits through attractive consumer and commercial deposit products and strong ties with our customer base and communities. We experienced an increase of $4.8 million in interest bearing deposits and a $2.8 million decrease in savings deposits during the first six months of 2012.

We experienced a decrease in time deposits of $40.3 million. This is the result of decreased interest rates offered in this very low interest rate environment. During 2012, interest rate sensitive deposits have withdrawn to seek other investment opportunities. We expect to continue to lose higher cost and rate sensitive deposits in the near future, but at a decreased pace than in the past. However, we monitor deposits to ensure that we maintain adequate liquidity levels. We believe despite the deposit decrease, we have adequate liquidity.

Total loans decreased to $554.1 million at June 30, 2012 from $597.8 million at year end 2011. This is the result of charge offs of $3.6 million for the first six months of 2012, lower loan demand, tighter underwriting criteria, and resolution of problem loans. We plan to decrease the loan portfolio as we manage our capital levels to maintain the Bank's and restore the Company's well-capitalized status, reduce certain risks to various industry sectors that have posed higher risks in recent times and resolve nonperforming loans. Even as we decrease our loan portfolio, we still are committed to serving our customers. We have hired commercial lending personnel, continue to train our loan officers to meet the needs of our customers, and are developing new business with qualified borrowers that will ensure a stronger loan portfolio in the future.

Other real estate owned decreased $3.5 million, or 23.16%, to $11.6 million at June 30, 2012 from $15.1 million at December 31, 2011. During the first half of 2012, we acquired $4.4 million in other real estate owned as a result of settlement of foreclosed loans, which was offset by sales of $5.3 million of our properties with losses of $201 thousand realized as a result of the sales. We also had to record writedowns on other real estate owned properties in the amount of $2.3 million for the first half of 2012. Future sales of these properties are contingent upon an economic recovery; consequently, it is difficult to estimate the duration of our ownership of these assets. We have designated employees to monitor other real estate owned properties to ensure proper fair market values of these assets and to ensure that maintenance and improvements are made to make these properties more marketable.

Net Interest Income and Net Interest Margin - Net interest income decreased $1.4 million, or 17.75%, to $6.7 million for the second quarter of 2012 from $8.1 million for the same period in 2011. Our net interest margin decreased to 4.02% in the second quarter of 2012 as compared to 4.28% for the same period in 2011. This is the result of the level of nonaccrual loans of $41.3 million at June 30, 2012 which negatively affects the net interest margin as these loans are nonearning assets. It is also affected by the decreased volume of loans, which are typically higher earning assets. In addition, the adjustment related to nonaccrual interest accounting recognition resulted in a one-time reduction of interest income of approximately $500 thousand. We do not foresee this reoccurring.

Noninterest Income - Noninterest income increased $400 thousand, or 32.41%, to $1.6 million in the second quarter of 2012 from $1.2 million for the same period in 2011. The increase is the result of a $265 thousand realized gain on the sale of investment securities and a $128 thousand increase in fees, commission, and other income. We expect noninterest income to remain flat throughout 2012 as a result of regulatory changes; however, we continue to seek opportunities to improve noninterest income.

Noninterest Expense - Noninterest expense totaled $8.3 million for the second quarter of 2012 as compared to $9.6 million for the second quarter of 2011. The primary contributor to the decrease in noninterest expenses for the quarter is the decrease in other real estate owned expenses of $973.

Salaries and benefits decreased $437 thousand in the quarter-to-quarter comparison from $3.9 million at June 30, 2011 to $3.5 million for the same period in 2012. We decreased staffing during 2011 and are now starting to realize the reduced expenses. Total full time equivalent employees have decreased to 287 at June 30, 2012 from 332 at June 30, 2011, a reduction of 45, or 13.55%. In addition, we have frozen salaries for the year 2012 in order to control this expense. In the year 2012, we also lowered the 401-k matching contribution from matching dollar for dollar on the 5% employee contribution to 3%. On May 31, 2012 we merged eight existing offices together to form four offices which reduced our total number of branches to 23. We anticipate annual pre-tax savings from these consolidations to be approximately $1.0 million. In the future, we are continuing to focus on reducing salary and benefits expenses.

Our efficiency ratio, which is defined as noninterest expense divided by the sum of net interest income plus noninterest income, was 99.58% for the second quarter of 2012 as compared to 103.15% for the same period in 2011. Included in this calculation are the other real estate owned write-downs which significantly and negatively impact the ratio. We anticipate this ratio to improve in 2012 as we realize cost savings from staff reductions and the branch mergers that occurred in the second quarter of 2012. We believe that other real estate owned write-downs may reduce from the past as these have been primarily related to construction and development type properties that have been significantly impacted due to recent market valuation trends. Our level of these properties is much lower and reflect current market values.

Provision for Loan Losses - The calculation of the allowance for loan losses is considered a critical accounting policy. The adequacy of the allowance for loan losses is based upon management's judgment and analysis. The following factors are included in our evaluation of determining the adequacy of the allowance: risk characteristics of the loan portfolio, current and historical loss experience, concentrations and internal and external factors such as general economic conditions.

The allowance for loan losses decreased modestly to $18.1 million at June 30, 2012 as compared to $18.4 million at December 31, 2011. Even so, the allowance for loan losses at June 30, 2012 was approximately 3.26% of total loans as compared to 3.07% at December 31, 2011 and 2.82% at June 30, 2011. Net loans charged off for the first six months of 2012 were $3.4 million, or 1.20% of average loans, and $9.9 million, or 2.89% of average loans, for the first six months of 2011. The provision for loan losses was $1.2 million for the second quarter of 2012 as compared with $2.3 million in the same period for 2011.

Loans delinquent greater than 90 days still accruing interest and loans in non-accrual status present higher risks of default and loan losses. At June 30, 2012, there were 148 loans in non-accrual status totaling $41.3 million, or 7.46% of total loans. At December 31, 2011, there were 170 loans in non-accrual status totaling $42.3 million, or 7.08% of total loans. The amounts of interest that would have been recognized on these loans were $777 thousand and $1.1 million for the six months ended June 30, 2012, 2012 and 2011, respectively. There were 39 loans past due 90 days or greater and still accruing interest totaling $3.0 million, or 0.55% of total loans at June 30, 2012. There were 47 loans past due 90 days or greater and still accruing interest totaling $1.5 million at year end 2011. It is our policy to stop accruing interest on a loan, and to classify that loan as non-accrual, under the following circumstances: (a) whenever we are advised by the borrower that scheduled payment or interest payments cannot be met, (b) when our best judgment indicates that payment in full of principal and interest can no longer be expected, or (c) when any such loan or obligation becomes delinquent for 90 days unless it is both well secured and in the process of collection. There were $26.8 million in loans classified as troubled debt restructurings as of June 30, 2012 as compared to $29.1 million in loans classified as troubled debt restructurings as of December 31, 2011. Of the loans classified as troubled debt restructurings at June 30, 2012, $7.8 million were in non-accrual status, compared to $8.2 million at December 31, 2011. We do not have any commitments to lend additional funds to non-performing debtors.

Certain risks exist in the Bank's loan portfolio. Historically, we had experienced significant annual loan growth until the past couple of years. Consequently there might be loans that have single pay maturities or demand loans that may be too new to have exhibited signs of weakness. A majority of our loans are collateralized by real estate located in our market area. It is our policy to sufficiently collateralize loans to help minimize loss exposures in case of default. The recent negative trends in the national real estate market and economy continue to pose threats to our portfolio. With the exception of real estate development type properties which have experienced more deterioration in market values, the local residential and commercial real estate market values have shown some deterioration but remain relatively stable. It is uncertain as to when or if local real estate values will be more significantly impacted. We do not believe that there will be a severely negative effect in our market area, but because of the uncertainty we deem it prudent to assign more of the allowance to these types of loans. Our market area is somewhat diverse, but certain areas are more reliant upon agriculture, coal mining and natural gas. As a result, increased risk of loan impairments is possible if these industries experience a significant downturn although we do not believe this to be likely at least in the near future. We consider these factors to be the primary higher risk characteristics of the loan portfolio.

Loans are initially risk rated by the originating loan officer. If deteriorations in the financial condition of the borrower and the capacity to repay the debt occur, along with other factors, the loan may be downgraded. This is to be determined by the loan officer. Guidance for the evaluation is established by the regulatory authorities who periodically review the Bank's loan portfolio for compliance. Classifications used by the Bank are exceptional, very good, standard, acceptable, transitory risk, other assets especially mentioned, substandard, doubtful and loss. For the year 2011, we engaged a third party loan review firm to conduct quarterly loan reviews and have engaged them to perform this function in 2012. Upon their review, loans risk ratings may change from the rating assigned by the respective lender. We have experienced fewer rating changes in more recent reviews indicating better risk identification for the loan portfolio in light of the experience from the severe recession.

All loans classified as special mention, substandard, doubtful and loss are individually reviewed for impairment. In determining impairment, collateral for loans classified as substandard, doubtful and loss is reviewed to determine if the collateral is sufficient for each of these credits, generally through obtaining an appraisal. We generally consider an appraisal to be outdated when the appraisal is greater than 12 months old and the credit exhibits signs of weakness that warrant the possibility of relying on the collateral for repayment. An independent appraisal department reviews each appraisal to ensure compliance with the Uniform Standards of Professional Appraisal Practice ("USPAP") requirements. The appraisal is further reviewed by the loan officer and Chief Credit Officer for reasonableness. If the appraisal value is questionable, an independent third party review of the appraisal is obtained. On adversely classified loans of all types, we may deem it necessary to obtain appraisals annually. If appraisals are obtained "as is," we further discount the appraisals with an estimated selling cost of 10% for commercial and development properties and 6% for residential mortgages. If a current appraisal has not been obtained, we generally discount the most recent appraisal value by age: greater than one year through two years – 10%; two years to three years – 20%; greater than 3 years – 30%. We are further evaluating these loans with standard discounts to determine if updated appraisals are necessary and if the discounts are still relevant related to the current distressed real estate market as compared to the timing of the most recent appraisal. It is possible, in some circumstances, that the discount may be inadequate due to the timing of the last evaluation and current circumstances. In determining the ASC 450 component of our allowance, we do not directly consider the potential for outdated appraisals since that portion of our allowance is based on the analysis of the performance of loans with similar characteristics, external and internal risk factors. We consider the overall quality of our underwriting process in our internal risk factors, but the need to update appraisals is associated with loans identified as impaired under ASC 310. If an appraisal is older than one year, a new external certified appraisal may be obtained and used to determine impairment. If an exposure exists, a specific allowance is directly made for the amount of the potential loss in addition to estimated liquidation and disposal costs. The evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available. Impaired loans decreased to $83.7 million with $30.6 million requiring a valuation allowance of $6.4 million at June 30, 2012 as compared to $91.8 million with $30.0 million requiring a valuation allowance of $6.0 million at December 31, 2011. Of the $83.7 million recorded as impaired loans, $40.5 million were nonperforming loans, which includes nonaccrual loans and past due 90 days or more. Management is aggressively working to reduce the impaired credits at minimal loss.

Deferred Tax Asset and Income Taxes - Due to timing differences between book and tax treatment of several income and expense items, a deferred tax asset of $5.6 million existed at June 30, 2012 as compared to a deferred tax asset of $7.2 million at December 31, 2011. During the first half of 2012 a $2.9 million deferred tax asset valuation allowance was recorded, which increased the total valuation allowance to $5.6 million at June 30, 2012, compared to $2.7 million at December 31, 2011. Management reviewed the June 30, 2012 deferred tax calculation to determine the need for a valuation allowance. Based on the trend of reduced levels of earning assets and net interest income, we modified the projections of taxable income over the next three years and determined that an additional deferred tax asset valuation allowance was required. A valuation allowance is provided when it is more likely than not that some portion of the deferred tax asset will not be realized. In management's opinion, based on a three year taxable income projection, tax strategies which would result in potential securities gains and the effects of off-setting deferred tax liabilities, it is more likely than not that all the deferred tax assets, net of the $5.6 million allowance, would be realizable. Included in deferred tax assets are the tax benefits derived from net operating loss carryforwards totaling $3.8 million. Management expects to utilize all of these carryforwards prior to expiration. Direct charge-offs contributed to a reduction of the tax asset and are permitted as tax deductions. In addition, writedowns on other real estate owned property are expensed for book purposes but are not deductible for tax purposes until disposition of the property. Goodwill expense also was realized for book purposes in 2011 but continues to only be tax deductible based on the statutory requirements; thus, creating a deferred tax asset. When, and if, taxable income increases in the future and during the net operating loss carryforward period, this valuation allowance may be reversed and used to decrease tax obligations in the future. Our income tax expense was computed at the normal corporate income tax rate of 34% of taxable income included in net income. We do not have significant nontaxable income or nondeductible expenses.

Capital Resources - Total capital at the end of the second quarter of 2012 was $23.7 million as compared to $29.0 million at the end of December 31, 2011. The decrease was due to the net loss of $5.1 million for the first half of 2012, which was primarily the result of other real estate owned expenses and writedowns, loan loss provisions and the deferred tax asset valuation allowance expense. The Bank was well capitalized as of June 30, 2012, as defined by the capital guidelines of bank regulations, however, the Company continued to be below the minimum capital requirements as a result of the Tier 1 leverage ratio decreasing to 3.72%, which was below the minimum requirement of 4.00%. Subject to the conversion of the director notes, we expect to return to well-capitalized status at the holding company level in 2012. The Company's capital as a percentage of total assets was 3.27% at June 30, 2012 compared to 3.70% at December 31, 2011.

Total assets decreased during the first half of 2012 and we anticipate further decreasing assets to be the trend in 2012. We developed a new strategic plan and capital plan in 2011. Under current economic conditions, we believe it is prudent to increase capital to absorb potential losses that may occur if asset quality deteriorates further. We are aware that capital needs and requirements are affected by the level of problem assets, growth, earnings and other factors. Retained earnings are not alone sufficient to provide for this economic cycle and we believe we will need access to additional sources of capital. As part of our initiative to improve regulatory capital ratios, we are further reducing our higher risk assets, which results in a shrinking loan portfolio. Deposit growth is primarily focused on growing core deposits, which are mainly transaction accounts, commercial relationships and savings products. We are focused on improving earnings by maintaining a strong net interest margin and decreasing overhead expenses. These options we are fully implementing to increase capital. However, these efforts alone may not provide us adequate capital if further loan losses are realized.

No cash dividends have been paid historically and none are anticipated in the foreseeable future.

Off Balance Sheet Items and Contractual Obligations - There have been no material changes during the quarter ended June 30, 2012 to the off-balance sheet items and the contractual obligations disclosed in our annual report on Form 10-K for the fiscal year ended December 31, 2011.

For a copy of the Second Quarter 2012 SEC 10Q Filing

To obtain a copy of our Second Quarter 2012 10Q, visit our website at www.npbankshares.com/investor relations -SEC Filings, or by written request to New Peoples Bankshares, Inc. ATTN: Todd Asbury, EVP & CFO, 67 Commerce Drive, Honaker, Virginia 24260.