STONERIDGE INC
Form 10-K
March 14, 2016

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, 2015

Commission file number: 001-13337

STONERIDGE, INC.

(Exact name of registrant as specified in its charter)

Ohio (*State or other jurisdiction of incorporation or organization)*	**34-1598949** *(I.R.S. Employer Identification No.)*
9400 East Market Street, Warren, Ohio *(Address of principal executive offices)*	**44484** *(Zip Code)*

(330) 856-2443
Registrant's telephone number, including area code

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Shares, without par value	**New York Stock Exchange**

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.

o 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 Act.

o 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 Securities Exchange Act of 1934 during the preceding 12 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 o No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

x Yes o No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

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 definition of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o Accelerated filer x Non-accelerated filer o Smaller reporting company o
(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). o Yes x No

As of June 30, 2015, the aggregate market value of the registrant's Common Shares held by non-affiliates of the registrant was approximately $310.1 million. The closing price of the Common Shares on June 30, 2015 as reported on the New York Stock Exchange was $11.71 per share. As of June 30, 2015, the number of Common Shares outstanding was 27,913,194.

The number of Common Shares outstanding as of February 29, 2016 was 27,786,978.

DOCUMENTS INCORPORATED BY REFERENCE

Definitive Proxy Statement for the Annual Meeting of Shareholders to be held on May 10, 2016, into Part III, Items 10, 11, 12, 13 and 14.

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Forward-Looking Statements

Portions of this report on Form 10-K contain “forward-looking statements” under the Private Securities Litigation Reform Act of 1995. These statements appear in a number of places in this report and may include statements regarding the intent, belief or current expectations of the Company, with respect to, among other things, our (i) future product and facility expansion, (ii) acquisition strategy, (iii) investments and new product development, (iv) growth opportunities related to awarded business and (v) operation expectations. Forward-looking statements may be identified by the words “will,” “may,” “should,” “designed to,” “believes,” “plans,” “projects,” “intends,” “expects,” “estimate “anticipates,” “continue,” and similar words and expressions. The forward-looking statements are subject to risks and uncertainties that could cause actual events or results to differ materially from those expressed in or implied by the statements. Important factors that could cause actual results to differ materially from those in the forward-looking statements include, among other factors:

- the reduced purchases, loss or bankruptcy of a major customer;
- the costs and timing of facility closures, business realignment, or similar actions;
- a significant change in automotive, commercial, motorcycle, off-highway or agricultural vehicle production;
- competitive market conditions and resulting effects on sales and pricing;
- the impact on changes in foreign currency exchange rates on sales, costs and results, particularly the Brazilian real, euro, Argentinian peso, Mexican peso and Swedish krona;
- our ability to achieve cost reductions that offset or exceed customer-mandated selling price reductions;
- a significant change in general economic conditions in any of the various countries in which we operate;
- labor disruptions at our facilities or at any of our significant customers or suppliers;
- the ability of our suppliers to supply us with parts and components at competitive prices on a timely basis;
- the amount of our indebtedness and the restrictive covenants contained in the agreements governing our indebtedness, including our revolving credit facility;
- customer acceptance of new products;
- capital availability or costs, including changes in interest rates or market perceptions;
- the failure to achieve the successful integration of any acquired company or business; and
- the items described in Part I, Item IA (“Risk Factors”).

In addition, the forward-looking statements contained herein represent our estimates only as of the date of this filing and should not be relied upon as representing our estimates as of any subsequent date. While we may elect to update these forward-looking statements at some point in the future, we specifically disclaim any obligation to do so, whether to reflect actual results, changes in assumptions, changes in other factors affecting such forward-looking statements or otherwise.

PART I

Item 1. Business.

Overview

Founded in 1965, Stoneridge, Inc. (the “Company”) is a global designer and manufacturer of highly engineered electrical and electronic components, modules and systems for the automotive, commercial, motorcycle, off-highway and agricultural vehicle markets. Our products and systems are critical elements in the management of mechanical and electrical systems to improve overall vehicle performance, convenience and monitoring in areas such as emissions control, fuel efficiency, safety, security and infotainment. Our extensive footprint encompasses 27 locations in 12 countries and enables us to supply global and regional automotive, commercial, motorcycle, off-highway and agricultural vehicle manufacturers around the world.

Our custom-engineered products and systems are used to activate equipment and accessories, monitor and display vehicle performance and control, distribute electrical power and signals and provide vehicle security and convenience. Our product offerings consist of (i) sensors, (ii) application-specific actuators, switches and valves (iii) vehicle and driver information systems, (iv) vehicle management electronics, (v) power and switch distribution modules and telematics, (vi) security alarms and vehicle tracking devices and monitoring services and (vii) convenience accessories. We supply the majority of our products, predominantly on a sole-source basis, to many of the world’s leading commercial vehicle and automotive original equipment manufacturers (“OEMs”), agricultural manufacturers and select non-vehicle OEMs, as well as certain commercial vehicle and automotive tier one suppliers. Our customers are increasingly utilizing electronic technology to comply with more stringent regulations (particularly emissions and safety) and to meet end-user demand for improved vehicle performance and greater convenience. As a result, per-vehicle electronic content has been increasing. Our technology and our partnership-oriented approach to product design and development enables us to develop next-generation products.

Segments and Products

We conduct our business in three reportable segments which are the same as our operating segments: Control Devices, Electronics and PST.

Control Devices. Our Control Devices segment designs and manufactures products that monitor, measure or activate specific functions within a vehicle. This segment includes product lines such as sensors, switches, valves and actuators. Sensor products are employed in major vehicle systems such as the emissions, safety, powertrain, braking, climate control, steering and suspension systems. Switches transmit signals that activate specific functions. Our switch technology is principally used in two capacities, user-activated and hidden. User-activated switches are used by a vehicle's operator or passengers to manually activate, rear defrosters and other accessories. Hidden switches are not typically visible to vehicle operators or passengers and are engaged to activate or deactivate selected functions as part of normal vehicle operations, such as brake lights. In addition, our Control Devices segment designs and manufactures actuator products that enable OEMs to deploy power functions in a vehicle and can be designed to integrate switching and control functions including our shift by wire product. We sell these products principally to the automotive market as well as the commercial vehicle and agricultural markets.

Electronics. Our Electronics segment designs and manufactures electronic instrument clusters, electronic control units and driver information systems. These products collect, store and display vehicle information such as speed, pressure, maintenance data, trip information, operator performance, temperature, distance traveled and driver messages related to vehicle performance. In addition, power distribution modules and systems regulate, coordinate, monitor and direct the operation of the electrical system within a vehicle. These products use state-of-the-art hardware, software and multiplexing technology and are sold principally to the commercial vehicle market.

PST. Our PST segment, which primarily serves the South American market, specializes in the design, manufacture and sale of in-vehicle audio and video devices, electronic vehicle security alarms, convenience accessories, vehicle tracking devices and monitoring services primarily for the automotive and motorcycle markets. This segment includes product lines such as alarms, convenience applications, vehicle monitoring and tracking devices and infotainment systems. These products improve the performance, safety and convenience features of our customers' vehicles. PST sells its products through the aftermarket distribution channel, to factory authorized dealer installers, also referred to as original equipment services, direct to OEMs and through mass merchandisers.

The following table sets forth for the periods indicated, the percentage of net sales attributable to our reportable segments and product categories of each for the years ended December 31:

Segment	Product Category	2015	2014	2013
Control Devices	Sensors, switches, valves and actuators	52 %	47 %	44 %
Electronics	Electronic instrument clusters, electronic control units and driver information systems	33 %	32 %	29 %
PST	Security alarms, vehicle tracking devices and monitoring services and convenience accessories	15 %	21 %	27 %

Our products and systems are sold to numerous OEM and tier one supplier customers, as well as aftermarket distributors and mass merchandisers, for use on many different vehicle platforms. We supply multiple parts to many of our principal OEM and tier one customers under requirements contracts for a particular vehicle model. These contracts range in duration from one year to the production life of the model, which commonly extends for three to seven years.

The following table sets forth for the periods indicated, the percentage of net sales derived from our principal end markets for the years ended December 31:

Principal End Markets	2015	2014	2013
Automotive	42 %	37 %	35 %
Commercial vehicle	37	36	33
Aftermarket distributors and mass merchandisers	15	21	27
Agricultural and other	6	6	5

For further information related to our reportable segments and financial information about geographic areas, see Note 12 to the consolidated financial statements.

Sale of Wiring Business

We sold substantially all of the assets and liabilities of our Wiring business on August 1, 2014. As a result, the Wiring business has been classified as discontinued operations for all periods presented in the Company's financial statements herein, and therefore has been excluded from continuing operations, segment results and other information herein for all periods presented. The Wiring business designed and manufactured wiring harness products and assembled instruments panels for sale principally to the commercial, agricultural and off-highway vehicle markets.

Production Materials

The principal production materials used in the manufacturing process for our reportable segments include: molded plastic components and resins, copper, precious metals and certain electrical components such as printed circuit boards, semiconductors, microprocessors, memory devices, resistors, capacitors, fuses, relays and infotainment devices. We purchase such materials pursuant to both annual contract and spot purchasing methods. Such materials are available from multiple sources, but we generally establish collaborative relationships with a qualified supplier for each of our key production materials in order to lower costs and enhance service and quality. As global demand for our production materials increases, we may have difficulties obtaining adequate production materials from our suppliers to satisfy our customers. Any extended period of time for which we cannot obtain adequate production material or which we experience an increase in the price of production material could materially affect our results of operations and financial condition.

Patents, Trademarks and Intellectual Property

We maintain and have pending various U.S. and foreign patents, trademarks and other rights to intellectual property relating to the reportable segments of our business, which we believe are appropriate to protect the Company's interests in existing products, new inventions, manufacturing processes and product developments. We do not believe any single patent is material to our business, nor would the expiration or invalidity of any patent have a material adverse effect on our business or ability to compete. We are not currently engaged in litigation related to material infringement claims other than one matter related to our Electronics segment which we believe is without merit. See additional details of the alleged patent infringement in Note 10 to the consolidated financial statements.

Industry Cyclicality and Seasonality

The markets for products in our reportable segments have been cyclical. Because these products are used principally in the production of vehicles for the automotive, commercial, motorcycle, off-highway and agricultural vehicle markets, revenues and therefore results of operations, are significantly dependent on the general state of the economy and other factors, like the impact of environmental regulations on our customers, which affect these markets. A decline in automotive, commercial, motorcycle, off-highway and agricultural vehicle production of our principal customers could adversely impact the Company. Also, our PST business is significantly dependent on the overall state of the Brazilian economy. Our Electronics and Control Devices segments are typically not affected by seasonality, however the demand for our PST segment consumer products is typically higher in the second half of the year, the fourth quarter in particular.

Customers

We have several customers which account for a significant percentage of our sales. The loss of any significant portion of our sales to these customers, or the loss of a significant customer, would have a material adverse impact on our financial condition and results of operations. We supply numerous different products to each of our principal customers. Contracts with several of our customers provide for supplying their requirements for a particular model, rather than for manufacturing a specific quantity of products. Such contracts range from one year to the life of the model, which is generally three to seven years. These contracts are subject to potential renegotiation from time to time, which may affect product pricing and generally may be terminated by our customers at any time. Therefore, the loss of a contract for a major model or a significant decrease in demand for certain key models or group of related models sold by any of our major customers could have a material adverse impact on the Company. We may also enter into contracts to supply parts, the introduction of which may then be delayed or cancelled. We also compete to supply products for successor models, and are therefore subject to the risk that the customer will not select the Company to produce products on any such model, which could have a material adverse impact on our financial condition and results of operations. In addition, we sell products to other customers that are ultimately sold to our principal customers.

Because of the competitive nature of the markets we serve, we face pricing pressures from our customers in the ordinary course of business. In response to these pricing pressures we have been able to effectively manage our production costs by the combination of lowering certain costs and limiting the increase of others, the net impact of which has not been material. However, if we are unable to effectively manage production costs in the future to mitigate future pricing pressures, our results of operations would be adversely affected.

The following table presents our principal customers, as a percentage of net sales:

Years ended December 31	2015	2014	2013
Ford Motor Company	14 %	11 %	10 %
Scania Group	7	8	8
Daimler	6	6	6
Volvo	6	5	4
General Motors Company	5	5	6
Other	62	65	66

Backlog

Our products are produced from readily available materials and have a relatively short manufacturing cycle; therefore our products are not on backlog status. Each of our production facilities maintains its own inventories and production schedules. Production capacity is adequate to handle current requirements and can be expanded to handle increased growth if needed.

Competition

The markets for our products in our reportable segments are highly competitive. We compete based on technological innovation, price, quality, performance, service and delivery. We compete for new business both at the beginning of the development of new models and upon the redesign of existing models for OEM customers. New model development generally begins two to five years before the marketing of such models to the public. Once a supplier has been selected to provide parts for a new program, an OEM customer will usually continue to purchase those parts from the selected supplier for the life of the program, although not necessarily for any model redesigns. We compete for aftermarket and mass merchandiser sales based on price, product functionality, quality and service.

Our diversity in products creates a wide range of competitors, which vary depending on both market and geographic location. We compete based on strong customer relations and a fast and flexible organization that develops technically effective solutions at or below target price. We compete against the following primary competitors:

Control Devices. Our primary competitors include Bosch, Continental AG, Delphi Automotive PLC, Denso Corporation, Electricfil, Hella KGaA Hueck & Co., Methode Electronics, Inc., NTK Technologies, Inc., TE Connectivity Ltd. and Sensata.

Electronics. Our primary competitors include Actia Group, Bosch, Continental AG, Delphi Automotive PLC, Dongfeng Electronics Technology Co., Ltd., Hella KGaA Hueck & Co., Magneti Marelli S.p.A. and Yazaki Corporation.

PST. Our primary competitors include Ceabs, Cerruns, Ituran, JVC/Kenwood Corporation, Lennox, M. Magneti Marelli S.p.A., MultiLaser, Quantum, Olimpus, Pioneer Corporation, Michelin and Sascar.

Product Development

Our research and development efforts for our reportable segments are largely product design and development oriented and consist primarily of applying known technologies to customer requests. We work closely with our customers to solve customer requests using innovative approaches. The majority of our development expenses are related to customer-sponsored programs where we are involved in designing custom-engineered solutions for specific applications or for next generation technology. To further our vehicle platform penetration, we have also developed collaborative relationships with the design and engineering departments of key customers. These collaborative efforts have resulted in the development of new and complimentary products and the enhancement of existing products.

While our engineering and product development departments are organized by market, our segments interact and collaborate on new products. The product development operations are complimented by technology groups in Canton, Massachusetts; Lexington, Ohio; Stockholm, Sweden; Pune, India; Manaus, Brazil; São Paulo, Brazil; and Shanghai, China.

We use efficient and quality oriented work processes to address our customers’ high standards. Our product development technical resources include a full complement of computer-aided design and engineering (“CAD/CAE”) software systems, including (i) virtual three-dimensional modeling, (ii) functional simulation and analysis capabilities and (iii) data links for rapid prototyping. These systems enable us to expedite product design and the manufacturing process to shorten the development time and ultimately time to market.

We have further strengthened our electrical engineering competencies through investment in equipment such as (i) automotive electro-magnetic compliance test chambers, (ii) programmable automotive and commercial vehicle transient generators, (iii) circuit simulators and (iv) other environmental test equipment. Additional investment in 3-D printing product machining equipment has allowed us to fabricate new product samples in a fraction of the time required historically. Our product development and validation efforts are supported by full service, on-site test labs at most manufacturing facilities, thus enabling cross-functional engineering teams to optimize the product, process and system performance before tooling initiation.

We have invested, and will continue to invest heavily in technology to develop new products for our customers. Product development costs incurred in connection with the development of new products and manufacturing methods, to the extent not recoverable from the customer, are expensed as incurred. Such costs amounted to approximately $38.8 million, $41.6 million and $40.4 million for 2015, 2014 and 2013, respectively, or 6.0%, 6.3% and 6.1% of net sales for these periods.

We will continue to prioritize investment spending toward the design and development of new products over sustaining existing product programs for specific customers, which allows us to sell our products to multiple customers. The typical product development process takes three to five years to show tangible results. As part of our effort to evaluate our investment spending, we review our current product portfolio and adjust our spending to either accelerate or eliminate our investment in these products based on our position in the market and the potential of the market and product.

Environmental and Other Regulations

Our operations are subject to various federal, state, local and foreign laws and regulations governing, among other things, emissions to air, discharge to water and the generation, handling, storage, transportation, treatment and disposal of waste and other materials. We believe that our business, operations and facilities have been and are being operated in compliance, in all material respects, with applicable environmental and health and safety laws and regulations, many of which provide for substantial fines and criminal sanctions for violations.

Employees

As of December 31, 2015, we had approximately 4,100 employees, approximately 62% of whom were located outside the United States. Although we have no collective bargaining agreements covering U.S. employees, a significant number of employees located in Brazil, Estonia, Mexico, Sweden, and the United Kingdom either (i) are represented by a union and are covered by a collective bargaining agreement, or (ii) are covered by works council or other employment arrangements required by law. We believe that relations with our employees are good.

Equity Investments and Joint Ventures

We make equity investments and form joint ventures in various global markets in order to achieve several strategic objectives including (i) diversifying our business by expanding in high-growth regions, (ii) employing complementary design processes, growth technologies and intellectual capital, and (iii) realizing cost savings from combined sourcing.

We have a 49% noncontrolling equity interest in India, Minda Stoneridge Instruments Ltd. (“Minda”) for the years ending December 31, 2015, 2014 and 2013. Minda manufactures electromechanical/electronic instrumentation equipment and sensors primarily for the automotive, motorcycle and commercial vehicle markets. We leverage our investment in Minda by sharing our knowledge and expertise in electrical components and systems and expanding Minda’s product offering through the joint development of our products designed for the market in India.

We also have a 74% controlling interest in PST Eletrônica Ltda. (“PST”), which is a consolidated subsidiary, for the years ending December 31, 2015, 2014 and 2013. PST was previously a joint venture in Brazil. We made our initial investment in PST in October 1997 acquiring a 50% interest and subsequently acquired an additional 24% interest on December 31, 2011. Prior to the acquisition of the additional interest on December 31, 2011 , PST was accounted for using the equity method of accounting.

Executive Officers of the Company

Each executive officer of the Company serves the Board of Directors at its pleasure. The Board of Directors appoints corporate officers annually. The executive officers for reporting purposes under the Securities and Exchange Act of 1934, as amended, of the Company are as follows:

Name	**Age**	**Position**
Jonathan B. DeGaynor	49	President, Chief Executive Officer and Director
George E. Strickler	68	Executive Vice President, Chief Financial Officer and Treasurer
Richard P. Adante	69	Vice President of Operations
Thomas A. Beaver	62	Vice President of the Company and President of Global Sales
Sergio de Cerqueira Leite	52	Director President of PST Eletrônica Ltda.
Peter Kruk	47	President of the Electronics Division
Alisa A. Nagle	48	Chief Human Resources Officer
Michael D. Sloan	59	Vice President of the Company and President of the Control Devices Division

Jonathan B. DeGaynor, President, Chief Executive Officer and Director. Mr. DeGaynor was appointed as President and Chief Executive Officer in March 2015. He has served as a director since May 2015. Prior to joining Stoneridge, Mr. DeGaynor served as the Vice President of Strategic Planning and Innovation of Guardian Industries Corp., ("Guardian"), from October 2014 until March 2015. Mr. DeGaynor served as Vice President of Business Development, Managing Director Asia for SRG Global, Inc., a Guardian company from 2008 through September 2014. Mr. DeGaynor served as Chief Operating Officer, International for Autocam Corporation from 2005 to 2008. Prior to that, Mr. DeGaynor held positions of increasing responsibility with Delphi Corporation from 1993 to 2005.

George E. Strickler, Executive Vice President, Chief Financial Officer and Treasurer. Mr. Strickler has served as Executive Vice President and Chief Financial Officer since joining the Company in January 2006. Mr. Strickler was appointed Treasurer of the Company in February 2007. Prior to his employment with the Company, Mr. Strickler served as Executive Vice President and Chief Financial Officer for Republic Engineered Products, Inc. ("Republic"), from February 2004 to January 2006. Mr. Strickler currently serves as a director, Board member and Chairman of the Nominating and Governance Committees of TCP International Holdings Ltd., a manufacturer and distributor of energy efficient lighting technologies.

Richard P. Adante, Vice President of Operations. Mr. Adante has served as Vice President of Operations since May 2011. From November 2009 until his appointment at Stoneridge, Mr. Adante was consulting through his personal consulting firm, RMA Management Consultants. From July 2006 to November 2009, Mr. Adante served as the President of Hawthorn Manufacturing, now known as Crowne Group.

Thomas A. Beaver, Vice President of the Company and President of Global Sales. Mr. Beaver has served as Vice President of the Company and President of Global Sales since May 2012. Prior to that, Mr. Beaver served as Vice President of the Company and Vice President of Global Sales and Systems Engineering from January 2005 to May 2012. From January 2000 to January 2005, Mr. Beaver served as Vice President of Stoneridge Sales and Marketing.

Sergio de Cerqueira Leite, Director President of PST Eletrônica Ltda. Mr. Leite is a founding partner of PST. He has held the Director President position since 1997.

Peter Kruk, President of the Electronics Division. Mr. Kruk has served as President of the Electronics Division since August 2012. Mr. Kruk joined the Company in October 2009 as the Managing Director of Stoneridge Electronics – Europe. Prior to that, he served as President of HEXPOL Wheels and Managing Director of Stellana AB from 2007 to 2009.

Alisa A. Nagle, Chief Human Resources Officer. Ms. Nagle has served as Chief Human Resources Officer since joining the Company in November 2015. From 2007 until her employment with the Company, Ms. Nagle served as Vice President of Human Resources – Global Aftermarket and Original Equipment Groups and Global Central Functions at Johnson Controls, Inc.

Michael D. Sloan, Vice President of the Company and President of the Control Devices Division. Mr. Sloan has served as President of the Control Devices Division since July 2009 and Vice President of the Company since December 2009. Prior to that, Mr. Sloan served as Vice President and General Manager of Stoneridge Hi-Stat from February 2004 to July 2009.

Available Information

We make available, free of charge through our website (www.stoneridge.com), our Annual Report on Form 10-K (“Annual Report”), Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, all amendments to those reports, and other filings with the U.S. Securities and Exchange Commission (“SEC”), as soon as reasonably practicable after they are filed with the SEC. Our Corporate Governance Guidelines, Code of Business Conduct and Ethics, Code of Ethics for Senior Financial Officers, Whistleblower Policy and Procedures and the charters of the Board of Director’s Audit, Compensation and Nominating and Corporate Governance Committees are posted on our website as well. Copies of these documents will be available to any shareholder upon request. Requests should be directed in writing to Investor Relations at Stoneridge, Inc., 9400 East Market Street, Warren, Ohio 44484.

The SEC maintains a website (www.sec.gov) that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC, including the Company. The public may also read and copy any materials we file with the SEC at the SEC’s Public Reference Room at 100 F. Street, NE, Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330.

Item 1A. Risk Factors.

Our business is cyclical and a downturn in the automotive, commercial, motorcycle, off-highway and agricultural vehicle markets as well as overall economic conditions could reduce the sales and profitability of our business.

The demand for products in our Control Devices and Electronics segments are largely dependent on the domestic and foreign production of automotive, commercial, motorcycle, off-highway and agricultural vehicles. The markets for our products have been cyclical, because new vehicle demand is dependent on, among other things, consumer spending and is tied closely to the overall strength of the economy. Because the majority of our products are used principally in the production of vehicles for the automotive, commercial, motorcycle, off-highway and agricultural vehicle markets, our net sales, and therefore our results of operations, are significantly dependent on the general state of the economy and other factors which affect these markets. A decline in commercial, automotive, agricultural, motorcycle and off-highway vehicle production, or a material decline in market share by our significant customers, could adversely affect our results of operations and financial condition. Also, the demand for our PST segment products are significantly dependent on the general state of the Brazilian economy and automotive market.

In 2015, approximately 85% of our net sales were derived from automotive, commercial, motorcycle, off-highway and agricultural vehicle markets while approximately 15% were derived from aftermarket distributors, mass merchandisers and monitoring services markets.

We have foreign currency translation and transaction risks that may materially adversely affect our operating results, financial condition and liquidity.

The financial position and results of operations of our international subsidiaries are initially recorded in various foreign currencies and then translated into U.S. dollars at the applicable exchange rate for inclusion in our consolidated financial statements. The strengthening of the U.S. dollar against these foreign currencies ordinarily has a negative effect on our reported sales and operating margin (and conversely, the weakening of the U.S. dollar against these foreign currencies has a positive impact). The volatility of currency exchange rates may materially adversely affect our operating results, including foreign currency forward contracts. To mitigate a portion of our exposure to fluctuations in foreign currency exchange rates we use derivative financial instruments, including foreign currency contracts, to reduce the effect of such fluctuations on foreign currency denominated intercompany transactions, inventory purchases and other foreign currency exposures.

We are subject to risks related to our international operations.

Approximately 43% of our net sales in 2015 were derived from sales outside of North America. At December 31, 2015, significant concentrations of net assets outside of North America included $51.3 million in South America and $71.4 million in Europe and Other. Non-current assets outside of North America accounted for approximately 55% of our non-current assets as of December 31, 2015. International sales and operations are subject to significant risks, including, among others:

- political and economic instability;
- restrictive trade policies;
- economic conditions in local markets;
- currency exchange controls;
- labor unrest;
- difficulty in obtaining distribution support and potentially adverse tax consequences; and
- the imposition of product tariffs and the burden of complying with a wide variety of international and U.S. export laws.

We may not realize sales represented by awarded business.

We base our growth projections, in part, on business awards made by our customers. These business awards generally renew annually during a program life cycle. Failure of actual production orders from our customers to approximate these business awards could have a material adverse effect on our business, financial condition or results of operations.

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The prices that we can charge some of our customers are predetermined and we bear the risk of costs in excess of our estimates, in addition to the risk of adverse effects resulting from general customer demands for cost reductions and quality improvements.

Our supply agreements with some of our customers require us to provide our products at predetermined prices. In some cases, these prices decline over the course of the contract and may require us to meet certain productivity and cost reduction targets. In addition, our customers may require us to share productivity savings in excess of our cost reduction targets. The costs that we incur in fulfilling these contracts may vary substantially from our initial estimates. Unanticipated cost increases or the inability to meet certain cost reduction targets may occur as a result of several factors, including increases in the costs of labor, components or materials. In some cases, we are permitted to pass on to our customers the cost increases associated with specific materials. However, cost overruns that we cannot pass on to our customers could adversely affect our business, financial condition or results of operations.

OEM customers have exerted and continue to exert considerable pressure on component suppliers to reduce costs, improve quality and provide additional design and engineering capabilities and continue to demand and receive price reductions and measurable increases in quality through their use of competitive selection processes, rating programs and various other arrangements. We may be unable to generate sufficient production cost savings in the future to offset required price reductions. Additionally, OEMs have generally required component suppliers to provide more design engineering input at earlier stages of the product development process, the costs of which have, in some cases, been absorbed by the suppliers. Future price reductions, increased quality standards and additional engineering capabilities required by OEMs may reduce our profitability and have a material adverse effect on our business, financial condition or results of operations.

Our business is very competitive and increased competition could reduce our sales and profitability.

The markets for our products are highly competitive. We compete based on technological innovation, price, quality, performance, service and delivery. Many of our competitors are more diversified and have greater financial and other resources than we do. In addition, with respect to certain products, some of our competitors are divisions of our OEM customers. We cannot assure that our business will not be adversely affected by competition or that we will be able to maintain our profitability if the competitive environment changes.

The loss or insolvency of any of our principal customers would adversely affect our future results.

We are dependent on several principal customers for a significant percentage of our net sales. In 2015, our top three customers were Ford Motor Company, Scania Group and Daimler which comprised 14%, 7% and 6% of our net sales, respectively. In 2015, our top ten customers accounted for 54% of our net sales. The loss of any significant portion of our sales to these customers would have a material adverse effect on our results of operations and financial condition. The contracts we have entered into with many of our customers provide for supplying the customers' requirements for a particular model, rather than for manufacturing a specific quantity of products. Such contracts range from one year to the life of the model, which is generally three to seven years. These contracts are subject to renegotiation, which may affect product pricing and generally may be terminated by our customers at any time. Therefore, the loss of a contract for a major model or a significant decrease in demand for certain key models or any group of related models sold by any of our major customers could have a material adverse effect on our results of operations and financial condition by reducing cash flows and our ability to spread costs over a larger revenue base. We also compete to supply products for successor models and are subject to the risk that the customer will not select us to produce products on any such model, which could have a material adverse impact on our business, financial condition or results of operations. In addition, we have significant receivable balances related to these customers and other major customers that would be at risk in the event of their bankruptcy.

Consolidation among vehicle parts customers and suppliers could make it more difficult for us to compete successfully.

The vehicle part supply industry has undergone a significant consolidation as OEM customers have sought to lower costs, improve quality and increasingly purchase complete systems and modules rather than separate components. As a result of the cost focus of these major customers, we have been, and expect to continue to be, required to reduce prices. Because of these competitive pressures, we cannot assure you that we will be able to increase or maintain gross margins on product sales to our customers. The trend toward consolidation among vehicle parts suppliers is resulting in fewer, larger suppliers who benefit from purchasing and distribution economies of scale. If we cannot achieve cost savings and operational improvements sufficient to allow us to compete successfully in the future with these larger, consolidated companies, our business, financial condition or results of operations could be adversely affected.

We rely on independent dealers and distributors to sell certain products in the aftermarket sales channel and a disruption to this channel would harm our business.

Because we sell certain products such as security accessories and driver information products to independent dealers and distributors, we are subject to many risks, including risks related to their inventory levels and support for our products. If dealers and distributors do not maintain sufficient inventory levels to meet customer demand, our sales could be negatively impacted.

Our dealer network also sells products offered by our competitors. If our competitors offer our dealers more favorable terms, those dealers may de-emphasize or decline to carry our products. In the future, we may not be able to retain or attract a sufficient number of qualified dealers and distributors. If we are unable to maintain successful relationships with dealers and distributors, or to expand our distribution channels, our business will suffer.

We are dependent on the availability and price of raw materials and other supplies.

We require substantial amounts of raw materials and other supplies, and substantially all such materials we require are purchased from outside sources. The availability and prices of raw materials and other supplies may be subject to curtailment or change due to, among other things, new laws or regulations, suppliers' allocations to other purchasers and interruptions in production by suppliers, weather emergencies, natural disasters, commercial disputes, acts of terrorism or war, changes in exchange rates and worldwide price levels. If demand for raw materials increases, we may have difficulties obtaining adequate raw materials and other supplies from our suppliers to satisfy our customers. At times, we have experienced difficulty obtaining adequate supplies of semiconductors and memory chips for our Control Devices, Electronics and PST segments. In addition, there have been challenges at times in obtaining timely supply of nylon and resins for our Control Devices segment and audio component parts for our PST segment. If we cannot obtain adequate raw materials and other supplies, or if we experience an increase in the price of raw materials and other supplies, our business, financial condition or results of operations could be materially adversely affected.

We use a variety of commodities, including copper, zinc, resins and certain other commodities. Increasing commodity costs could have a negative impact on our results. We have sought at times to alleviate the effect of increasing costs by selectively hedging a portion of our exposure. The inability to effectively hedge them may have a material adverse effect on our business, financial condition or results of operations.

We must implement and sustain a competitive technological advantage in producing our products to compete effectively.

Our products are subject to changing technology, which could place us at a competitive disadvantage relative to alternative products introduced by competitors. Our success will depend on our ability to continue to meet customers' changing specifications with respect to technological innovation, price, quality, performance, service and delivery by implementing and sustaining competitive technological advances. Our business may, therefore, require significant recurring additional capital expenditures and investment in product development and manufacturing and management information systems. We cannot assure that we will be able to achieve the technological advances or introduce new products that may be necessary to remain competitive. Our inability to continuously improve existing products, to develop new products and to achieve technological advances could have a material adverse effect on our business, financial condition or results of operations.

PST's Global Positioning Systems ("GPS") products depend upon satellites maintained by the United States Department of Defense. If a significant number of these satellites become inoperable, unavailable or are not replaced, or if the policies of the United States government for the use of the GPS without charge are changed, our business will suffer.

The GPS is a satellite-based navigation and positioning system consisting of a constellation of orbiting satellites. The satellites and their ground control and monitoring stations are maintained and operated by the United States Department of Defense. The Department of Defense does not currently charge users for access to the satellite signals. These satellites and their ground support systems are complex electronic systems subject to electronic and mechanical failures and possible sabotage.

If a significant number of satellites were to become inoperable, unavailable or are not replaced, it would impair the current utility of our GPS products and the growth of market opportunities. In addition, there can be no assurance that the U.S. government will remain committed to the operation and maintenance of GPS satellites over a long period, or that the policies of the U.S. government that provide for the use of the GPS without charge and without accuracy degradation will remain unchanged. Because of the increasing commercial applications of the GPS, other U.S. government agencies may become involved in the administration or the regulation of the use of GPS signals. Any of the foregoing factors could affect the willingness of buyers of our products to select GPS-based products instead of products based on competing technologies, which could adversely affect our operational revenues and our financial condition.

We may incur material product liability costs.

We may be subject to product liability claims in the event that the failure of any of our products results in personal injury or death and we cannot assure that we will not experience material product liability losses in the future. We cannot assure that our product liability insurance will be adequate for liabilities ultimately incurred or that it will continue to be available on terms acceptable to us. In addition, if any of our products prove to be defective, we may be required to participate in government-imposed or customer OEM-instituted recalls involving such products. A successful claim brought against us that exceeds available insurance coverage or a requirement to participate in any product recall could have a material adverse effect on our business, financial condition or results of operations.

Increased or unexpected product warranty claims could adversely affect us.

We typically provide our customers a warranty covering workmanship, and in some cases materials, on products we manufacture. Our warranty generally provides that products will be free from defects and adhere to customer specifications. If a product fails to comply with the warranty, we may be obligated or compelled, at our expense, to correct any defect by repairing or replacing the defective product. We maintain warranty reserves in an amount based on historical trends of units sold and payment amounts, combined with our current understanding of the status of existing claims. To estimate the warranty reserves, we must forecast the resolution of existing claims, as well as expected future claims on products previously sold. The amounts estimated to be due and payable could differ materially from what we may ultimately be required to pay. An increase in the rate of warranty claims or the occurrence of unexpected warranty claims could have a material adverse effect on our customer relations and our financial condition or results of operations.

If we fail to protect our intellectual property rights or maintain our rights to use licensed intellectual property or are found liable for infringing the rights of others, our business could be adversely affected.

Our intellectual property, including our patents, trademarks, copyrights, trade secrets and license agreements, are important in the operation of our businesses, and we rely on the patent, trademark, copyright and trade secret laws of the United States and other countries, as well as nondisclosure agreements, to protect our intellectual property rights. We may not, however, be able to prevent third parties from infringing, misappropriating or otherwise violating our intellectual property, breaching any nondisclosure agreements with us, or independently developing technology that is similar or superior to ours and not covered by our intellectual property. Any of the foregoing could reduce any competitive advantage we have developed, cause us to lose sales or otherwise harm our business. We cannot assure that any intellectual property will provide us with any competitive advantage or will not be challenged, rejected, cancelled, invalidated or declared unenforceable. In the case of pending patent applications, we may not be successful in securing issued patents, or securing patents that provide us with a competitive advantage for our businesses. In addition, our competitors may design products around our patents that avoid infringement and violation of our intellectual property rights.

We cannot be certain that we have rights to use all intellectual property used in the conduct of our businesses or that we have complied with the terms of agreements by which we acquire such rights, which could expose us to infringement, misappropriation or other claims alleging violations of third party intellectual property rights. Third parties have asserted and may assert or prosecute infringement claims against us in connection with the services and products that we offer, and we may or may not be able to successfully defend these claims. Litigation, either to enforce our intellectual property rights or to defend against claims regarding intellectual property rights of others, could result in substantial costs and a diversion of our resources. Any such claims and resulting litigation could require us to enter into licensing agreements (if available on acceptable terms or at all), pay damages and cease making or selling certain products and could result in a loss of our intellectual property protection. Moreover, we may need to redesign some of our products to avoid future infringement liability. We also may be required to indemnify customers or other third parties at significant expense in connection with such claims and actions. Any of the foregoing could have a material adverse effect on our business, financial condition or results of operations.

Our debt obligations could limit our flexibility in managing our business and expose us to risks.

As of December 31, 2015, there was $100.0 million in borrowings outstanding on our revolving credit facility (the "Credit Facility"). In addition, we are permitted under our Credit Facility to incur additional debt, subject to specified limitations. Our leverage and the terms of our indebtedness may have important consequences including the following:

- we may have difficulty satisfying our obligations with respect to our indebtedness, and if we fail to comply with these requirements, an event of default could result;
- we may be required to dedicate a substantial portion of our cash flow from operations to required payments on indebtedness, thereby reducing the availability of cash flow for working capital, capital expenditures and other general corporate activities;
- covenants relating to our debt may limit our ability to obtain additional financing for working capital, capital expenditures and other general corporate activities;
- covenants relating to our debt may limit our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate;
- we may be more vulnerable than our competitors to the impact of economic downturns and adverse developments in our business; and
- we may be placed at a competitive disadvantage against any less leveraged competitors.

These and other consequences of our leverage and the terms of our indebtedness could have a material adverse effect on our business, financial condition or results of operations.

Covenants in our Credit Facility may limit our ability to pursue our business strategies.

Our Credit Facility limits our ability to, among other things:

- incur additional debt and guarantees;
- pay dividends and repurchase our shares;

- make other restricted payments, including investments;
- create liens;
- sell or otherwise dispose of assets, including capital shares of subsidiaries;
- enter into agreements that restrict dividends from subsidiaries;
- consolidate, merge or sell or otherwise dispose of all or substantially all of our assets; and
- substantially change the nature of our business.

The agreement governing our Credit Facility requires us to maintain a maximum leverage ratio of 3.00 to 1.00, and a minimum interest coverage ratio of 3.50 to 1.00 and places a maximum annual limit on capital expenditures. Our ability to comply with these covenants as well as the restrictive covenants under the terms of our indebtedness, may be affected by events beyond our control.

A breach of any of the restrictive covenants under our indebtedness or our inability to comply with the leverage and interest ratio requirements in the Credit Facility could result in a default. If a default occurs, the lenders under the Credit Facility could elect to declare all outstanding borrowings, together with accrued interest and other fees, to be immediately due and payable and terminate any commitments they have to provide further borrowings, and the Credit Facility lenders could pursue foreclosure and other remedies against us and our assets.

We have limited or no redundancy for certain of our manufacturing facilities, and therefore damage or disruption to those facilities could interrupt our operations, increase our costs of doing business and impair our ability to deliver our products on a timely basis.

If certain of our existing production facilities become incapable of manufacturing products for any reason, we may be unable to meet production requirements, we may lose revenue and we may not be able to maintain our relationships with our customers. Without operation of certain existing production facilities, we may be limited in our ability to deliver products until we restore the manufacturing capability at the particular facility, find an alternative manufacturing facility or arrange an alternative source of supply. Although we carry business interruption insurance to cover lost revenue and profits in an amount we consider adequate, this insurance does not cover all possible situations. Also, our business interruption insurance would not compensate us for the loss of opportunity and potential adverse impact on relations with our existing customers resulting from our inability to produce products for them.

A failure of our information technology (IT) networks and systems, or the inability to successfully implemeE="font-family:Times New Roman" SIZE="2">1,128

Net Income

$722 $1,096 $2,683 $2,940

Less: net income attributable to noncontrolling interest in subsidiary	3	3	10	10
Net Income Attributable to First Capital, Inc.	$719	$1,093	$2,673	$2,930

Earnings per common share attributable to First Capital, Inc.

Basic

$0.26	$0.39	$0.96	$1.05

Diluted

$0.26	$0.39	$0.96	$1.05

Dividends per share				
	$0.19	$0.19	$0.57	$0.57

See accompanying notes to consolidated financial statements.

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PART I FINANCIAL INFORMATION

FIRST CAPITAL, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

	Three Months Ended September 30, 2012	Three Months Ended September 30, 2011	Nine Months Ended September 30, 2012	Nine Months Ended September 30, 2011
	(In thousands)			
Net Income	$ 722	$ 1,096	$ 2,683	$ 2,940
OTHER COMPREHENSIVE INCOME				
Unrealized gains on securities available for sale:				
Unrealized holding gains arising during the period	128	711	207	2,148
Income tax expense	(51)	(282)	(82)	(851)
Net of tax amount	77	429	125	1,297
Less: reclassification adjustment for realized (gains) losses included in net income	(29)	(11)	(29)	8
Income tax (expense) benefit	12	4	12	(3)
Net of tax amount	(17)	(7)	(17)	5
Other Comprehensive Income, net of tax	60	422	108	1,302
Comprehensive Income	$ 782	$ 1,518	$ 2,791	$ 4,242

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PART I FINANCIAL INFORMATION

FIRST CAPITAL, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY

(Unaudited)

(In thousands, except share data)	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Treasury Stock	Noncontrolling Interest	Total
Balances at January 1, 2011	$ 32	$ 24,313	$ 30,442	$ 391	$ (7,285)	$ 111	$ 48,004
Net income	0	0	2,930	0	0	10	2,940
Change in unrealized gain on securities available for sale,net of reclassification adjustments and tax effect	0	0	0	1,302	0	0	1,302
Cash dividends	0	0	(1,588)	0	0	(13)	(1,601)
Purchase of 1,608 treasury shares	0	0	0	0	(27)	0	(27)
Balances at September 30, 2011	$ 32	$ 24,313	$ 31,784	$ 1,693	$ (7,312)	$ 108	$ 50,618
Balances at January 1, 2012	$ 32	$ 24,313	$ 32,297	$ 1,612	$ (7,312)	$ 111	$ 51,053
Net income	0	0	2,673	0	0	10	2,683
Change in unrealized gain on securities available for sale, net of reclassification adjustments and tax effect	0	0	0	108	0	0	108
Cash dividends	0	0	(1,589)	0	0	(13)	(1,602)
Purchase of 692 treasury shares	0	0	0	0	(14)	0	(14)
Balances at September 30, 2012	$ 32	$ 24,313	$ 33,381	$ 1,720	$ (7,326)	$ 108	$ 52,228

See accompanying notes to consolidated financial statements.

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PART I FINANCIAL INFORMATION

FIRST CAPITAL, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Nine Months Ended September 30, 2012	2011
	(In thousands)	
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 2,683	$ 2,940
Adjustments to reconcile net income to net cash and cash equivalents provided by operating activities:		
Amortization of premiums and accretion of discounts on securities, net	721	695
Depreciation and amortization expense	576	608
Deferred income taxes	(508)	(54)
Increase in cash value of life insurance	(138)	(154)
Provision for loan losses	1,125	1,325
(Gain) loss on sale of securities	(29)	8
Proceeds from sales of loans	29,144	18,343
Loans originated for sale	(27,829)	(14,270)
Gain on sale of loans	(712)	(394)
(Increase) decrease in accrued interest receivable	19	(47)
Decrease in accrued interest payable	(93)	(195)
Net change in other assets/liabilities	1,668	499
Net Cash Provided By Operating Activities	6,627	9,304
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of securities available for sale	(54,833)	(27,542)
Proceeds from maturities of securities available for sale	27,825	14,355
Proceeds from maturities of securities held to maturity	0	14
Proceeds from sales of securities available for sale	2,927	1,399
Principal collected on mortgage-backed obligations	11,632	7,124
Net (increase) decrease in loans receivable	(6,693)	7,389
Proceeds from sale of foreclosed real estate	889	559
Proceeds from redemption of Federal Home Loan Bank stock	0	374
Purchase of premises and equipment	(416)	(323)
Net Cash Provided By (Used In) Investing Activities	(18,669)	3,349
CASH FLOWS FROM FINANCING ACTIVITIES		
Net increase (decrease) in deposits	19,693	(15,878)
Net increase (decrease) in advances from Federal Home Loan Bank	(2,250)	496
Net decrease in retail repurchase agreements	(13)	(2,379)
Purchase of treasury stock	(14)	(27)
Dividends paid	(1,602)	(1,602)
Net Cash Provided By (Used In) Financing Activities	15,814	(19,390)
Net Increase (Decrease) in Cash and Cash Equivalents	3,772	(6,737)
Cash and cash equivalents at beginning of period	18,923	21,575

Cash and Cash Equivalents at End of Period	$ 22,695	$ 14,838

See accompanying notes to consolidated financial statements.

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FIRST CAPITAL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Presentation of Interim Information

First Capital, Inc. (Company) is the savings and loan holding company for First Harrison Bank (Bank). The information presented in this report relates primarily to the Bank s operations. First Harrison Investments, Inc. and First Harrison Holdings, Inc. are wholly-owned Nevada corporate subsidiaries of the Bank that jointly own First Harrison, LLC, a Nevada limited liability corporation that holds and manages an investment portfolio. First Harrison REIT, Inc. (REIT) was incorporated as a wholly-owned subsidiary of First Harrison Holdings, Inc. to hold a portion of the Bank s real estate mortgage loan portfolio. On January 21, 2009, the REIT issued 105 shares of 12.5% redeemable cumulative preferred stock with an aggregate liquidation value of $105,000 in a private placement offering in order to satisfy certain ownership requirements to qualify as a real estate investment trust. At September 30, 2012, this noncontrolling interest represented 0.2% ownership of the REIT.

In the opinion of management, the unaudited consolidated financial statements include all normal adjustments considered necessary to present fairly the financial position as of September 30, 2012, and the results of operations for the three and nine months ended September 30, 2012 and cash flows for the nine months ended September 30, 2012 and 2011. All of these adjustments are of a normal, recurring nature. Such adjustments are the only adjustments included in the unaudited consolidated financial statements. Interim results are not necessarily indicative of results for a full year.

The accompanying unaudited consolidated financial statements and notes have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial statements and are presented as permitted by the instructions to Form 10-Q. Accordingly, they do not contain certain information included in the Company s annual audited consolidated financial statements and related footnotes for the year ended December 31, 2011 included in the Form 10-K.

The unaudited consolidated financial statements include the accounts of the Company and its subsidiaries. All material intercompany balances and transactions have been eliminated in consolidation.

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FIRST CAPITAL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

2. Investment Securities

Debt and equity securities have been classified in the consolidated balance sheets according to management s intent. Investment securities at September 30, 2012 and December 31, 2011 are summarized as follows:

(In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
September 30, 2012				
Securities available for sale:				
Agency mortgage-backed securities	$ 22,022	$ 538	$ 9	$ 22,551
Agency CMO	24,278	169	90	24,357
Privately-issued CMO	666	19	28	657
Other debt securities:				
Agency notes and bonds	42,119	330	1	42,448
Municipal obligations	28,331	1,750	20	30,061
Subtotal debt securities	117,416	2,806	148	120,074
Mutual funds	3,263	56	18	3,301
Total securities available for sale	$ 120,679	$ 2,862	$ 166	$ 123,375
Securities held to maturity:				
Agency mortgage-backed securities	$ 14	$ 0	$ 0	$ 14
Total securities held to maturity	$ 14	$ 0	$ 0	$ 14
December 31, 2011				
Securities available for sale:				
Agency mortgage-backed securities	$ 11,689	$ 542	$ 11	$ 12,220
Agency CMO	23,196	152	60	23,288
Privately-issued CMO	896	16	32	880
Other debt securities:				
Agency notes and bonds	41,971	395	3	42,363
Municipal obligations	25,800	1,501	0	27,301
Subtotal debt securities	103,552	2,606	106	106,052
Mutual funds	5,369	52	33	5,388
Total securities available for sale	$ 108,921	$ 2,658	$ 139	$ 111,440
Securities held to maturity:				
Agency mortgage-backed securities	$ 16	$ 0	$ 0	$ 16

Total securities held to maturity	$	16	$	0	$	0	$	16

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FIRST CAPITAL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(2 continued)

Agency notes and bonds, agency mortgage-backed securities and agency collateralized mortgage obligations (CMO) include securities issued by the Government National Mortgage Association (GNMA), a U.S. government agency, and the Federal National Mortgage Association (FNMA), the Federal Home Loan Mortgage Corporation (FHLMC) and the Federal Home Loan Bank (FHLB), which are government-sponsored enterprises. Privately-issued CMOs are issued by special-purpose entities that are generally collateralized by first position residential mortgage loans and first position residential home equity loans.

The amortized cost and fair value of debt securities as of September 30, 2012, by contractual maturity, are shown below. Expected maturities of mortgage-backed securities may differ from contractual maturities because the mortgages underlying the obligations may be prepaid without penalty.

	Securities Available for Sale		Securities Held to Maturity	
(In thousands)	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	$ 832	$ 835	$ 0	$ 0
Due after one year through five years	6,537	6,669	0	0
Due after five years through ten years	19,406	19,859		
Due after ten years	43,675	45,146	0	0
	70,450	72,509	0	0
Mortgage-backed securities and CMO	46,966	47,565	14	14
	$ 117,416	$ 120,074	$ 14	$ 14

Information pertaining to investment securities available for sale with gross unrealized losses at September 30, 2012, aggregated by investment category and the length of time that individual investment securities have been in a continuous position, follows:

(Dollars in thousands)	Number of Investment Positions	Fair Value	Gross Unrealized Losses
Continuous loss position less than twelve months:			
Agency notes and bonds	3	$ 3,049	$ 1
Agency CMO	10	9,798	86
Agency mortgage-backed securities	1	2,075	9
Muncipal obligations	5	1,638	20
Total less than twelve months	19	16,560	116

Continuous loss position more than twelve months:			
Privately-issued CMO	1	202	28
Agency CMO	2	1,105	4
Mutual fund	1	374	18
Total more than twelve months	4	1,681	50
Total securities available for sale	23	$ 18,241	$ 166

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FIRST CAPITAL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(2 continued)

Management evaluates securities for other-than-temporary impairment at least quarterly, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recover in fair value.

At September 30, 2012, the 21 U.S. government agency debt securities, including agency notes and bonds, mortgage-backed securities and CMO, and municipal obligations in a loss position had depreciated approximately 0.7% from the amortized cost basis. All of the U.S. government agency securities and municipal obligations are issued by U.S. government agencies, government-sponsored enterprises and municipal governments, or are secured by first mortgage loans and municipal project revenues. These unrealized losses related principally to current interest rates for similar types of securities. In analyzing an issuer s financial condition, management considers whether the securities are issued by the federal government, its agencies or other governments, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuer s financial condition. As the Company has the ability to hold the debt securities until maturity, or the foreseeable future if classified as available for sale, no declines are deemed to be other-than-temporary.

At September 30, 2012, the privately-issued CMO in a loss position had depreciated approximately 12.2% from the amortized cost basis. The Company evaluates the existence of a potential credit loss component related to the decline in fair values of the privately-issued CMO portfolio each quarter using an independent third party analysis. At September 30, 2012, the privately-issued CMO in a loss position had an amortized cost of $230,000 and a fair value of $202,000, and had been downgraded to a substandard regulatory classification in 2009 due to a downgrade of the security s credit quality by various rating agencies. Based on the independent third party analysis performed in September 2012, the Company did not recognize an other-than-temporary impairment loss during the quarter ended September 30, 2012. While management did not anticipate a credit-related impairment loss at September 30, 2012, any future deterioration in market and economic conditions may have an adverse impact on the credit quality in future periods.

3. Loans and Allowance for Loan Losses

The Company s loan and allowance for loan loss policies are as follows:

Loans are stated at unpaid principal balances, less net deferred loan fees and the allowance for loan losses. The Company grants real estate mortgage, commercial business and consumer loans. A substantial portion of the loan portfolio is represented by mortgage loans to customers in southern Indiana. The ability of the Company s customers to honor their loan agreements is dependent upon the real estate and general economic conditions in this area.

Loan origination and commitment fees, as well as certain direct costs of underwriting and closing loans, are deferred and amortized as a yield adjustment to interest income over the lives of the related loans using the interest method. Amortization of net deferred loan fees is discontinued when a loan is placed on nonaccrual status.

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FIRST CAPITAL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(3 continued)

The recognition of income on a loan is discontinued and previously accrued interest is reversed, when interest or principal payments become ninety (90) days past due unless, in the opinion of management, the outstanding interest remains collectible. Past due status is determined based on contractual terms. Generally, by applying the cash receipts method, interest income is subsequently recognized only as received until the loan is returned to accrual status. The cash receipts method is used when the likelihood of further loss on the loan is remote. Otherwise, the Company applies the cost recovery method and applies all payments as a reduction of the unpaid principal balance until the loan qualifies for return to accrual status. Interest income on impaired loans is recognized using the cost recovery method, unless the likelihood of further loss on the loan is remote.

A loan is restored to accrual status when all principal and interest payments are brought current and the borrower has demonstrated the ability to make future payments of principal and interest as scheduled, which generally requires that the borrower demonstrate a period of performance of at least six consecutive months.

The Company s practice is to charge-off any loan or portion of a loan when the loan is determined by management to be uncollectible due to the borrower s failure to meet repayment terms, the borrower s deteriorating or deteriorated financial condition, the depreciation of the underlying collateral, the loan s classification as a loss by regulatory examiners, or for other reasons. A partial charge-off is recorded on a loan when the uncollectibility of a portion of the loan has been confirmed, such as when a loan is discharged in bankruptcy, the collateral is liquidated, a loan is restructured at a reduced principal balance, or other identifiable events that lead management to determine the full principal balance of the loan will not be repaid. A specific reserve is recognized as a component of the allowance for estimated losses on loans individually evaluated for impairment. Partial charge-offs on nonperforming and impaired loans are included in the Company s historical loss experience used to estimate the general component of the allowance for loan losses as discussed below. Specific reserves are not considered charge-offs in management s analysis of the allowance for loan losses because they are estimates and the outcome of the loan relationship is undetermined. At September 30, 2012, the Company had six loans on which partial charge-offs of $371,000 had been recorded.

Installment loans are typically charged off at 90 days past due, or earlier if deemed uncollectible, unless the loans are in the process of collection. Overdrafts are charged off after 45 days past due. Charge-offs are typically recorded on loans secured by real estate when the property is foreclosed upon.

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management s periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower s ability to repay, estimated value of any underlying collateral, and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

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FIRST CAPITAL, INC.

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(3 continued)

The allowance consists of specific and general components. The specific component relates to loans that are classified as doubtful, substandard, or special mention. For such loans that are also classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers non-classified loans and is based on historical loss experience adjusted for qualitative factors, as discussed below.

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower s prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan-by-loan basis by either the present value of expected future cash flows discounted at the loan s effective interest rate, the loan s obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Values for collateral dependent loans are generally based on appraisals obtained from independent licensed real estate appraisers, with adjustments applied for estimated costs to sell the property, costs to complete unfinished or repair damaged property and other known defects. New appraisals are generally obtained for all significant properties when a loan is identified as impaired. Generally, a property is considered significant if the value of the property is estimated to exceed $200,000. Subsequent appraisals are obtained as needed or if management believes there has been a significant change in the market value of the property. In instances where it is not deemed necessary to obtain a new appraisal, management would base its impairment and allowance for loan loss analysis on the original appraisal with adjustments for current conditions based on management s assessment of market factors and management s inspection of the property.

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(3 continued)

The following table provides the components of the Company s recorded investment in loans for each portfolio segment at September 30, 2012:

	Residential Real Estate	Land	Construction	Commercial Real Estate	Commercial Business	Home Equity & 2nd Mtg	Other Consumer	Total
				(In thousands)				
Recorded Investment in Loans:								
Principal loan balance	$ 111,594	$ 9,663	$ 11,878	$ 63,944	$ 19,146	$ 37,348	$ 31,796	$ 285,369
Accrued interest receivable	447	42	31	170	56	142	180	1,068
Net deferred loan origination fees and costs	64	2	(13)	(8)	(10)	154	0	189
Recorded investment in loans	$ 112,105	$ 9,707	$ 11,896	$ 64,106	$ 19,192	$ 37,644	$ 31,976	$ 286,626
Recorded Investment in Loans as Evaluated for Impairment:								
Individually evaluated for impairment	$ 2,698	$ 4	$ 394	$ 2,986	$ 1,809	$ 101	$ 0	$ 7,992
Collectively evaluated for impairment	109,407	9,703	11,502	61,120	17,383	37,543	31,976	278,634
Acquired with deteriorated credit quality	0	0	0	0	0	0	0	0
Ending balance	$ 112,105	$ 9,707	$ 11,896	$ 64,106	$ 19,192	$ 37,644	$ 31,976	$ 286,626

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(3 continued)

The following table provides the components of the Company s recorded investment in loans for each portfolio segment at December 31, 2011:

	Residential Real Estate	Land	Construction	Commercial Real Estate	Commercial Business	Home Equity & 2nd Mtg	Other Consumer	Total
				(In thousands)				
Recorded Investment in Loans:								
Principal loan balance	$ 116,338	$ 9,910	$ 6,963	$ 57,680	$ 20,722	$ 38,641	$ 29,832	$ 280,086
Accrued interest receivable	463	60	16	160	64	162	202	1,127
Net deferred loan origination fees and costs	67	2	0	0	(10)	84	0	143
Recorded investment in loans	$ 116,868	$ 9,972	$ 6,979	$ 57,840	$ 20,776	$ 38,887	$ 30,034	$ 281,356
Recorded Investment in Loans as Evaluated for Impairment:								
Individually evaluated for impairment	$ 2,281	$ 5	$ 247	$ 2,853	$ 1,928	$ 87	$ 0	$ 7,401
Collectively evaluated for impairment	114,587	9,967	6,732	54,987	18,848	38,800	30,034	273,955
Acquired with deteriorated credit quality	0	0	0	0	0	0	0	0
Ending balance	$ 116,868	$ 9,972	$ 6,979	$ 57,840	$ 20,776	$ 38,887	$ 30,034	$ 281,356

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FIRST CAPITAL, INC.

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An analysis of the allowance for loan losses as of September 30, 2012 is as follows:

	Residential Real Estate	Land	Construction	Commercial Real Estate	Commercial Business	Home Equity & 2nd Mtg	Other Consumer	Total
				(In thousands)				
Ending allowance balance attributable to loans:								
Individually evaluated for impairment	$ 267	$ 0	$ 0	$ 441	$ 914	$ 29	$ 0	$ 1,651
Collectively evaluated for impairment	943	102	60	520	185	824	306	2,940
Acquired with deteriorated credit quality	0	0	0	0	0	0	0	0
Ending balance	$ 1,210	$ 102	$ 60	$ 961	$ 1,099	$ 853	$ 306	$ 4,591

An analysis of the allowance for loan losses as of December 31, 2011 is as follows:

	Residential Real Estate	Land	Construction	Commercial Real Estate	Commercial Business	Home Equity & 2nd Mtg	Other Consumer	Total
				(In thousands)				
Ending allowance balance attributable to loans:								
Individually evaluated for impairment	$ 183	$ 0	$ 0	$ 539	$ 936	$ 0	$ 0	$ 1,658
Collectively evaluated for impairment	645	93	33	730	224	400	399	2,524
Acquired with deteriorated credit quality	0	0	0	0	0	0	0	0
Ending balance	$ 828	$ 93	$ 33	$ 1,269	$ 1,160	$ 400	$ 399	$ 4,182

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FIRST CAPITAL, INC.

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(3 continued)

An analysis of the changes in the allowance for loan losses for the three months and nine months ended September 30, 2012 is as follows:

	Residential Real Estate	Land	Construction	Commercial Real Estate	Commercial Business	Home Equity & 2nd Mtg	Other Consumer	Total
				(In thousands)				
Allowance for loan losses:								
Changes in Allowance for Loan Losses for the three-months ended September 30, 2012								
Beginning balance	$ 1,173	$ 102	$ 40	$ 826	$ 1,154	$ 840	$ 297	$ 4,432
Provisions for loan losses	51	0	20	135	(60)	158	46	350
Charge-offs	(15)	0	0	0	0	(154)	(90)	(259)
Recoveries	1	0	0	0	5	9	53	68
Ending balance	$ 1,210	$ 102	$ 60	$ 961	$ 1,099	$ 853	$ 306	$ 4,591
Changes in Allowance for Loan Losses for the nine-months ended September 30, 2012								
Beginning balance	$ 828	$ 93	$ 33	$ 1,269	$ 1,160	$ 400	$ 399	$ 4,182
Provisions for loan losses	697	12	27	(308)	(70)	765	2	1,125
Charge-offs	(327)	(4)	0	0	0	(330)	(236)	(897)
Recoveries	12	1	0	0	9	18	141	181
Ending balance	$ 1,210	$ 102	$ 60	$ 961	$ 1,099	$ 853	$ 306	$ 4,591

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(3 continued)

An analysis of the changes in the allowance for loan losses for the three months and nine months ended September 30, 2011 is as follows:

	Residential Real Estate	Land	Construction	Commercial Real Estate	Commercial Business	Home Equity & 2nd Mtg	Other Consumer	Total
				(In thousands)				
Allowance for loan losses:								
Changes in Allowance for Loan Losses for the three-months ended September 30, 2011								
Beginning balance	$ 1,217	$ 59	$ 26	$ 1,271	$ 1,020	$ 562	$ 406	$ 4,561
Provisions for loan losses	146	2	2	114	130	3	3	400
Charge-offs	(80)	0	0	0	0	(250)	(73)	(403)
Recoveries	5	0	3	0	36	16	45	105
Ending balance	$ 1,288	$ 61	$ 31	$ 1,385	$ 1,186	$ 331	$ 381	$ 4,663
Changes in Allowance for Loan Losses for the nine-months ended September 30, 2011								
Beginning balance	$ 1,024	$ 55	$ 21	$ 1,051	$ 1,251	$ 606	$ 465	$ 4,473
Provisions for loan losses	601	6	7	402	199	136	(26)	1,325
Charge-offs	(346)	0	0	(68)	(305)	(458)	(211)	(1,388)
Recoveries	9	0	3	0	41	47	153	253
Ending balance	$ 1,288	$ 61	$ 31	$ 1,385	$ 1,186	$ 331	$ 381	$ 4,663

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(3 continued)

At September 30, 2012 and December 31, 2011, for each loan portfolio segment management applied an overall qualitative factor of 1.15 to the Company s historical loss factors based on the most recent calendar quarters. The overall qualitative factor is derived from management s analysis of changes and trends in the following qualitative factors:

Underwriting Standards Management reviews the findings of periodic internal audit loan reviews, independent outsourced loan reviews and loan reviews performed by the banking regulators to evaluate the risk associated with changes in underwriting standards. At September 30, 2012 and December 31, 2011, management assessed the risk associated with this component as neutral, requiring no adjustment to the historical loss factors.

Economic Conditions Management analyzes trends in housing and unemployment data in the Harrison, Floyd and Clark counties of Indiana, the Company s primary market area, to evaluate the risk associated with economic conditions. Due to a decrease in new home construction and an increase in unemployment in the Company s primary market area, management assigned a risk factor of 1.20 for this component at September 30 2012 and December 31, 2011.

Past Due Loans Management analyzes trends in past due loans for the Company to evaluate the risk associated with delinquent loans. In general, past due loan ratios have remained at elevated levels compared to historical amounts since 2007, and management assigned a risk factor of 1.20 for this component at September 30, 2012 and December 31, 2011.

Other Internal and External Factors This component includes management s consideration of other qualitative factors such as loan portfolio composition. The Company has focused on the origination of commercial business and real estate loans in an effort to convert the Company s balance sheet from that of a traditional thrift institution to a commercial bank. In addition, the Company has increased its investment in mortgage loans in which it does not hold a first lien position. Commercial loans and second mortgage loans generally entail greater credit risk than residential mortgage loans secured by a first lien. As a result of changes in the loan portfolio composition, management assigned a risk factor of 1.20 for this component at September 30, 2012 and December 31, 2011.

Each of the four factors above was assigned an equal weight to arrive at an average for the overall qualitative factor of 1.15 at September 30, 2012 and December 31, 2011. The effect of the overall qualitative factor was to increase the estimated allowance for loan losses by $306,000 and $317,000 at September 30, 2012 and December 31, 2011, respectively.

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(Unaudited)

(3 continued)

The following table summarizes the Company s impaired loans by class of loans as of September 30, 2012 and for the three months and nine months ended September 30, 2012:

	At September 30, 2012			Three Months Ended September 30, 2012			Nine Months Ended September 30, 2012		
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized	Interest Recognized - Cash Method	Average Recorded Investment	Interest Income Recognized	Interest Recognized - Cash Method
					(In thousands)				
Loans with no related allowance recorded:									
Residential	$ 1,259	$ 1,531	$ 0	$ 1,152	$ 1	$ 1	$ 1,203	$ 2	$ 2
Land	4	5	0	23	0	0	23	0	1
Construction	394	402	0	330	0	0	293	0	0
Commercial real estate	1,220	1,511	0	1,229	0	0	1,231	0	0
Commercial business	0	0	0	0	0	0	0	0	0
Home Equity/2nd mortgage	0	0	0	43	0	0	64	2	1
Other consumer	0	0	0	0	1	0	0	1	0
	2,877	3,449	0	2,777	2	1	2,814	5	4
Loans with an allowance recorded:									
Residential	1,439	1,524	267	1,382	0	1	1,151	0	1
Land	0	0	0	0	0	0	0	0	0
Construction	0	0	0	0	0	0	0	0	0
Commercial real estate	1,766	1,845	441	1,630	0	0	1,602	0	0
Commercial business	1,809	1,909	914	1,826	0	0	1,877	0	0
Home Equity/2nd mortgage	101	102	29	128	0	0	111	0	0
Other consumer	0	0	0	0	0	0	0	0	0
	5,115	5,380	1,651	4,966	0	1	4,741	0	1
Total:									
Residential	2,698	3,055	267	2,534	1	2	2,354	2	3
Land	4	5	0	23	0	0	23	0	1
Construction	394	402	0	330	0	0	293	0	0
Commercial real estate	2,986	3,356	441	2,859	0	0	2,833	0	0
Commercial business	1,809	1,909	914	1,826	0	0	1,877	0	0
Home Equity/2nd mortgage	101	102	29	171	0	0	175	2	1

Other consumer	0	0	0	0	1	0	0	1	0
	$ 7,992	$ 8,829	$ 1,651	$ 7,743	$ 2	$ 2	$ 7,555	$ 5	$ 5

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(3 continued)

The following table summarizes the Company s impaired loans by class of loans for the three months and nine months ended September 30, 2011:

	Three Months Ended September 30, 2011			Nine Months Ended September 30, 2011		
	Average Recorded Investment	Interest Income Recognized	Interest Recognized - Cash Method	Average Recorded Investment	Interest Income Recognized	Interest Recognized - Cash Method
			(In thousands)			
Loans with no related allowance recorded:						
Residential	$ 820	$ 3	$ 2	$ 936	$ 13	$ 5
Land	6	1	3	5	1	3
Construction	331	0	0	264	0	0
Commercial real estate	241	9	9	339	9	9
Commercial business	25	0	0	17	0	0
Home Equity/2nd mortgage	16	2	1	18	4	2
Other consumer	3	2	0	6	3	1
	1,442	17	15	1,585	30	20
Loans with an allowance recorded:						
Residential	2,481	5	0	2,260	0	36
Land	0	0	0	0	0	0
Construction	0	0	0	70	0	0
Commercial real estate	1,004	0	0	1,101	0	0
Commercial business	1,981	0	0	2,063	0	0
Home Equity/2nd mortgage	265	0	0	352	0	0
Other consumer	0	0	0	6	0	0
	5,731	5	0	5,852	0	36
Total:						
Residential	3,301	8	2	3,196	13	41
Land	6	1	3	5	1	3
Construction	331	0	0	334	0	0
Commercial real estate	1,245	9	9	1,440	9	9
Commercial business	2,006	0	0	2,080	0	0
Home Equity/2nd mortgage	281	2	1	370	4	2
Other consumer	3	2	0	12	3	1
	$ 7,173	$ 22	$ 15	$ 7,437	$ 30	$ 56

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FIRST CAPITAL, INC.

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(3 continued)

The following table summarizes the Company s impaired loans by class of loans as of December 31, 2011:

	Recorded Investment	Unpaid Principal Balance	Related Allowance
		(In thousands)	
Loans with no related allowance recorded:			
Residential	$ 1,149	$ 1,507	$ 0
Land	5	6	0
Construction	247	249	0
Commercial real estate	1,215	1,280	0
Commercial business	0	0	0
HE/2nd mortgage	87	94	0
Other consumer	0	0	0
	2,703	3,136	0
Loans with an allowance recorded:			
Residential	1,132	1,233	183
Land	0	0	0
Construction	0	0	0
Commercial real estate	1,638	1,933	539
Commercial business	1,928	2,023	936
HE/2nd mortgage	0	0	0
Other consumer	0	0	0
	4,698	5,189	1,658
Total:			
Residential	2,281	2,740	183
Land	5	6	0
Construction	247	249	0
Commercial real estate	2,853	3,213	539
Commercial business	1,928	2,023	936
Home Equity/2nd mortgage	87	94	0
Other consumer	0	0	0
	$ 7,401	$ 8,325	$ 1,658

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Nonperforming loans consists of nonaccrual loans and loans over 90 days past due and still accruing interest. The following table presents the recorded investment in nonperforming loans by class of loans at September 30, 2012 and December 31, 2011:

	September 30, 2012			December 31, 2011		
	Nonaccrual Loans	Loans 90+ Days Past Due Still Accruing	Total Nonperforming Loans	Nonaccrual Loans	Loans 90+ Days Past Due Still Accruing	Total Nonperforming Loans
			(In thousands)			
Residential	$ 2,698	$ 67	$ 2,765	$ 2,281	$ 143	$ 2,424
Land	4	0	4	5	38	43
Construction	394	0	394	247	0	247
Commercial real estate	2,986	0	2,986	2,853	0	2,853
Commercial business	1,809	0	1,809	1,928	0	1,928
Home Equity/2nd mortgage	101	0	101	87	159	246
Other consumer	0	32	32	0	23	23
Total	$ 7,992	$ 99	$ 8,091	$ 7,401	$ 363	$ 7,764

The following table presents the aging of the recorded investment loans by class of loans at September 30, 2012:

	30-59 Days Past Due	60-89 Days Past Due	Over 90 Days Past Due	Total Past Due	Current	Total Loans
			(In thousands)			
Residential	$ 4,618	$ 1,377	$ 1,122	$ 7,117	$ 104,988	$ 112,105
Land	301	4	0	305	9,402	9,707
Construction	113	141	0	254	11,642	11,896
Commercial real estate	244	0	443	687	63,419	64,106
Commercial business	8	17	0	25	19,167	19,192
Home Equity/2nd mortgage	584	140	69	793	36,851	37,644
Other consumer	313	43	32	388	31,588	31,976
Total	$ 6,181	$ 1,722	$ 1,666	$ 9,569	$ 277,057	$ 286,626

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The following table presents the aging of the recorded investment in loans by class of loans at December 31, 2011:

	30-59 Days Past Due	60-89 Days Past Due	Over 90 Days Past Due	Total Past Due	Current	Total Loans
			(In thousands)			
Residential	$ 5,205	$ 1,068	$ 1,035	$ 7,308	$ 109,560	$ 116,868
Land	442	43	43	528	9,444	9,972
Construction	0	0	247	247	6,732	6,979
Commercial real estate	676	0	1,258	1,934	55,906	57,840
Commercial business	256	0	0	256	20,520	20,776
Home Equity/2nd mortgage	558	72	246	876	38,011	38,887
Other consumer	306	37	23	366	29,668	30,034
Total	$ 7,443	$ 1,220	$ 2,852	$ 11,515	$ 269,841	$ 281,356

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, public information, historical payment experience, credit documentation, and current economic trends, among other factors. The Company classifies loans based on credit risk at least quarterly. The Company uses the following regulatory definitions for risk ratings:

Special Mention: Loans classified as special mention have a potential weakness that deserves management s close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution s credit position at some future date.

Substandard: Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

Doubtful: Loans classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

Loss: Loans classified as loss are considered uncollectible and of such little value that their continuance on the institution s books as an asset, without establishment of a specific valuation allowance or charge-off, is not warranted.

Loans not meeting the criteria above that are analyzed individually as part of the described process are considered to be pass rated loans.

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(3 continued)

The following table presents the recorded investment in loans by risk category and class of loans as of the date indicated:

	Residential Real Estate	Land	Construction	Commercial Real Estate	Commercial Business	Home Equity & 2nd Mtg	Other Consumer	Total
				(In thousands)				
September 30, 2012								
Pass	$ 105,004	$ 7,306	$ 11,303	$ 53,670	$ 15,264	$ 37,009	$ 31,875	$ 261,431
Special Mention	2,113	268	199	4,917	1,526	136	55	9,214
Substandard	2,290	2,129	0	2,533	593	398	46	7,989
Doubtful	2,698	4	394	2,986	1,809	101	0	7,992
Loss	0	0	0	0	0	0	0	0
Ending balance	$ 112,105	$ 9,707	$ 11,896	$ 64,106	$ 19,192	$ 37,644	$ 31,976	$ 286,626
December 31, 2011								
Pass	$ 113,037	$ 7,578	$ 6,217	$ 46,544	$ 16,961	$ 38,513	$ 29,976	$ 258,826
Special Mention	862	255	307	5,392	1,462	63	44	8,385
Substandard	688	2,134	208	3,051	425	224	14	6,744
Doubtful	2,281	5	247	2,853	1,928	87	0	7,401
Loss	0	0	0	0	0	0	0	0
Ending balance	$ 116,868	$ 9,972	$ 6,979	$ 57,840	$ 20,776	$ 38,887	$ 30,034	$ 281,356

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The following table summarizes the Company s troubled debt restructurings (TDRs) by class of loan and accrual status as of September 30, 2012 and December 31, 2011:

	September 30, 2012				December 31, 2011			
	Accruing	Nonaccrual	Total	Related Allowance for Loan Losses	Accruing	Nonaccrual	Total	Related Allowance for Loan Losses
	(In thousands)							
Troubled debt restructurings:								
Residential real estate	$ 181	$ 690	$ 871	$ 102	$ 112	$ 516	$ 628	$ 11
Land	135	0	135	0	135	0	135	0
Construction	0	288	288	0	207	247	454	0
Commercial real estate	0	1,557	1,557	87	0	1,603	1,603	211
Commercial business	0	1,809	1,809	914	0	1,843	1,843	914
Home equity and 2nd mortgage	0	33	33	26	8	0	8	0
Consumer	0	0	0	0	0	0	0	0
Total	$ 316	$ 4,377	$ 4,693	$ 1,129	$ 462	$ 4,209	$ 4,671	$ 1,136

At September 30, 2012 and December 31, 2011, commitments to lend additional funds to debtors whose loan terms have been modified in a TDR (both accruing and nonaccruing) totaled $33,000 and $192,000, respectively. These commitments represent the undisbursed portion of construction loans to borrowers that have outstanding loans classified as TDRs.

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(Unaudited)

(3 continued)

The following table summarizes information in regard to TDRs that were restructured during the three and nine months ended September 30, 2012.

	Three months ended September 30, 2012			Nine months ended September 30, 2012		
	Number of Contracts	Pre-Modification Outstanding Balance	Post-Modification Outstanding Balance	Number of Contracts	Pre-Modification Outstanding Balance	Post-Modification Outstanding Balance
		(Dollars in thousands)			*(Dollars in thousands)*	
Troubled debt restructurings:						
Residential real estate	2	$ 190	$ 190	3	$ 281	$ 278
Home equity & 2nd mortgage	0	0	0	1	25	25
Construction	0	0	0	0	0	0
Commercial real estate	0	0	0	0	0	0
Commercial business	0	0	0	0	0	0
Construction	0	0	0	0	0	0
Consumer	0	0	0	0	0	0
Total	2	$ 190	$ 190	4	$ 306	$ 303

For the TDRs restructured during the three and nine months ended September 30, 2012, the terms of modification were related to the reduction of the stated interest rate and a maturity extension. There were no principal charge-offs recorded as a result of TDRs during the three and nine months ended September 30, 2012.

There were no TDRS modified within the previous 12 months for which there was a subsequent payment default (defined as the loan becoming more than 90 days past due, being moved to nonaccrual status, or the collateral being foreclosed upon) during the nine months ended September 30, 2012. In the event that a TDR subsequently defaults, the Company evaluates the restructuring for possible impairment. As a result, the related allowance for loan losses may be increased or charge-offs may be taken to reduce the carrying amount of the loan.

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4. Supplemental Disclosure for Earnings Per Share

	Three Months Ended		Nine Months Ended	
	September 30, 2012	September 30, 2011	September 30, 2012	September 30, 2011
	(Dollars in thousands, except for share and per share data)			
Basic and Diluted:				
Earnings:				
Net income attributable to First Capital, Inc.	$ 719	$ 1,093	$ 2,673	$ 2,930
Shares:				
Weighted average common shares outstanding	2,785,001	2,785,693	2,785,383	2,786,652
Net income attributable to First Capital, Inc. per common share, basic and diluted	$ 0.26	$ 0.39	$ 0.96	$ 1.05

5. Stock Option Plan

For the nine month periods ended September 30, 2012 and 2011, the Company did not recognize any compensation expense related to its stock option plans. Expense is recognized ratably over the five-year vesting period of the options. At September 30, 2012, there was no unrecognized compensation expense related to nonvested stock options to be recognized over the remaining vesting period. The Black-Scholes option pricing model was used to determine the fair value of the options granted in prior periods.

6. Supplemental Disclosures of Cash Flow Information

	Nine Months Ended September 30,	
	2012	2011
	(In thousands)	
Cash payments for:		
Interest	$ 2,020	$ 3,150
Taxes	976	1,041
Noncash investing activities:		
Transfers from loans to real estate acquired through foreclosure	868	775

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7. Fair Value Measurements

Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 820*, Fair Value Measurements,* provides the framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy under FASB ASC Topic 820 are described as follows.

Level 1: Inputs to the valuation methodology are quoted prices, unadjusted, for identical assets or liabilities in active markets. A quoted market price in an active market provides the most reliable evidence of fair value and shall be used to measure fair value whenever available.

Level 2: Inputs to the valuation methodology include quoted market prices for similar assets or liabilities in active markets; inputs to the valuation methodology include quoted market prices for identical or similar assets or liabilities in markets that are not active; or inputs to the valuation methodology that are derived principally from or can be corroborated by observable market data by correlation or other means.

Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement. Level 3 assets and liabilities include financial instruments whose value is determined using discounted cash flow methodologies, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

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A description of the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below. These valuation methodologies were applied to all of the Company s financial and nonfinancial assets carried at fair value or the lower of cost or fair value. The table below presents the balances of assets measured at fair value on a recurring and nonrecurring basis as of September 30, 2012 and December 31, 2011. The Company had no liabilities measured at fair value as of September 30, 2012 or December 31, 2011.

	Carrying Value			
	Level 1	Level 2	Level 3	Total
		(In thousands)		
September 30, 2012				
Assets Measured on a Recurring Basis				
Securities available for sale:				
Agency mortgage-backed securities	$ 0	$ 22,551	$ 0	$ 22,551
Agency CMO	0	24,357	0	24,357
Privately-issued CMO	0	657	0	657
Agency notes and bonds	0	42,448	0	42,448
Municipal obligations	0	30,061	0	30,061
Mutual funds	3,301	0	0	3,301
Total securities available for sale	$ 3,301	$ 120,074	$ 0	$ 123,375
Assets Measured on a Nonrecurring Basis				
Impaired loans	$ 0	$ 0	$ 6,341	$ 6,341
Loans held for sale	0	2,306	0	2,306
Foreclosed real estate	0	0	420	420
December 31, 2011				
Assets Measured on a Recurring Basis				
Securities available for sale:				
Agency mortgage-backed securities	$ 0	$ 12,220	$ 0	$ 12,220
Agency CMO	0	23,288	0	23,288
Privately-issued CMO	0	880	0	880
Agency notes and bonds	0	42,363	0	42,363
Municipal obligations	0	27,301	0	27,301
Mutual funds	5,388	0	0	5,388
Total securities available for sale	$ 5,388	$ 106,052	$ 0	$ 111,440
Assets Measured on a Nonrecurring Basis				
Impaired loans	$ 0	$ 0	$ 6,107	$ 6,107
Loans held for sale	0	2,909	0	2,909
Foreclosed real estate	0	0	661	661

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Fair value is based upon quoted market prices, where available. If quoted market prices are not available, fair value is based on internally developed models or obtained from third parties that primarily use, as inputs, observable market-based parameters or a matrix pricing model that employs the Bond Market Association s standard calculations for cash flow and price/yield analysis and observable market-based parameters. Valuation adjustments may be made to ensure that financial instruments are recorded at fair value, or the lower of cost or fair value. These adjustments may include unobservable parameters. Any such valuation adjustments have been applied consistently over time. The Company s valuation methodologies may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. While management believes the Company s valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

Securities Available for Sale. Securities classified as available for sale are reported at fair value on a recurring basis. These securities are classified as Level 1 of the valuation hierarchy where quoted market prices from reputable third-party brokers are available in an active market. If quoted market prices are not available, the Company obtains fair value measurements from an independent pricing service. These securities are reported using Level 2 inputs and the fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, U.S. government and agency yield curves, live trading levels, trade execution data, market consensus prepayment speeds, credit information, and the security s terms and conditions, among other factors. Changes in fair value of securities available for sale are recorded in other comprehensive income, net of income tax effect.

Impaired Loans. Impaired loans are carried at the present value of estimated future cash flows using the loan s existing rate or the fair value of collateral if the loan is collateral dependent. Impaired loans are evaluated and valued at the time the loan is identified as impaired at the lower of cost or market value. For collateral dependent impaired loans, market value is measured based on the value of the collateral securing these loans. Collateral may be real estate and/or business assets, including equipment, inventory and/or accounts receivable, and its fair value is generally determined based on real estate appraisals or other independent evaluations by qualified professionals. The appraisals are then discounted to reflect management s estimate of the fair value of the collateral given the current market conditions and the condition of the collateral Impaired loans are reviewed and evaluated on at least a quarterly basis for additional impairment and adjusted accordingly, based on the same factors identified above. Fair value of impaired loans is classified as Level 3 in the fair value hierarchy.

Loans Held for Sale. Loans held for sale are carried at the lower of cost or market value. The portfolio is comprised of residential real estate loans and fair value is based on specific prices of underlying contracts for sales to investors. These measurements are classified as Level 2.

Foreclosed Real Estate. Foreclosed real estate held for sale is reported at fair value less estimated costs to dispose of the property. The fair values are determined by real estate appraisals which are then discounted to reflect management s estimate of the fair value of the property given current market conditions. Fair value of foreclosed real estate held for sale is classified as Level 3 in the fair value hierarchy.

There were no transfers into or out of the Company s Level 3 financial assets for the nine months ended September 30, 2012. In addition, there were no transfers into or out of Levels 1 and 2 of the fair value hierarchy during the nine months ended September 30, 2012.

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GAAP requires disclosure of the fair value of financial assets and financial liabilities, whether or not recognized in the balance sheet. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. In that regard, the derived fair value estimates cannot be substantiated by comparison to independent markets and, in many cases, could not be realized in immediate settlement of the instruments. Accordingly, the aggregate fair value amounts presented do not represent the underlying value of the Company. The estimated fair values of the Company s financial instruments are as follows:

	September 30, 2012		December 31, 2011	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
	(In thousands)			
Financial assets:				
Cash and cash equivalents	$ 22,695	$ 22,695	$ 18,923	$ 18,923
Securities available for sale	123,375	123,375	111,440	111,440
Securities held to maturity	14	14	16	16
Loans held for sale	2,306	2,364	2,909	2,966
Loans, net	280,967	285,564	276,047	287,624
Federal Home Loan Bank stock	2,820	2,820	2,820	2,820
Accrued interest receivable	1,782	1,782	1,801	1,801
Financial liabilities:				
Deposits	384,067	385,147	364,374	367,359
Retail repurchase agreements	9,112	9,112	9,125	9,125
Advances from Federal Home Loan Bank	10,100	10,100	12,350	12,840
Accrued interest payable	320	320	413	413
Off-balance-sheet financial instruments:				
Asset related to commitments to extend credit	0	0	0	48

The carrying amounts in the preceding table are included in the consolidated balances sheets under the applicable captions. The following methods and assumptions were used to estimate the fair value of each class of financial instrument for which it is practicable to estimate that value:

Cash and Cash Equivalents

For cash and cash equivalents, including cash and due from banks, interest-bearing deposits with banks, and federal funds sold, the carrying amount is a reasonable estimate of fair value.

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Debt and Equity Securities

For marketable equity securities, the fair values are based on quoted market prices. For debt securities, the Company obtains fair value measurements from an independent pricing service and the fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, U.S. government and agency yield curves, live trading levels, trade execution data, market consensus prepayment speeds, credit information, and the security s terms and conditions, among other factors. For Federal Home Loan Bank stock, a restricted equity security, the carrying amount is a reasonable estimate of fair value because it is not marketable.

Loans

The fair value of loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. The carrying amount of accrued interest receivable approximates its fair value.

Deposits

The fair value of demand deposits, savings accounts, money market deposit accounts and other transaction accounts is the amount payable on demand at the balance sheet date. The fair value of fixed-maturity certificates of deposit is estimated by discounting the future cash flows using the rates currently offered for deposits of similar remaining maturities. The carrying amount of accrued interest payable approximates its fair value.

Borrowed Funds

The carrying amounts of retail repurchase agreements approximate their fair value. The fair value of advances from Federal Home Loan Bank is estimated by discounting the future cash flows using the current rates at which similar loans with the same remaining maturities could be obtained.

Commitments to Extend Credit

The majority of commitments to extend credit would result in loans with a market rate of interest if funded. The fair value of these commitments are the fees that would be charged to customers to enter into similar agreements. For fixed rate loan commitments, the fair value also considers the difference between current levels of interest rates and the committed rates.

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8. Recent Accounting Pronouncements

The following are summaries of recently issued accounting pronouncements that impact the accounting and reporting practices of the Company:

In December 2011, the FASB issued ASU No. 2011-11, *Balance Sheet (Topic 210)*. The update requires an entity to disclose information about offsetting and related arrangements to enable users of the financial statements to understand the effect of netting arrangements on the entity s financial position. The scope includes derivatives, sale and repurchase agreements and reverse sale and repurchase agreements, and securities borrowing and securities lending arrangements. The amendments in the update are effective for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods, with disclosures required by the amendments provided retrospectively for all comparative periods presented. The adoption of this update is not expected to have any impact on the Company s consolidated financial position or results of operations.

In October 2012, the FASB issued ASU No. 2012-06, *Subsequent Accounting for an Indemnification Asset Recognized at the Acquisition Date as a Result of a Government-Assisted Acquisition of a Financial Institution*. The update indicates that when a reporting entity initially recognizes an indemnification asset as a result of a government-assisted acquisition of a financial institution and subsequently a change in the cash flows expected to be collected on the indemnification asset occurs, the reporting entity should subsequently account for the change in the measurement of the indemnification asset on the same basis as the change in the assets subject to indemnification. Any amortization of changes in value should be limited to the contractual term of the indemnification agreement (that is, the lesser of the term of the indemnification agreement and the remaining life of the indemnified assets). The amendments in the update are effective for fiscal years, and interim periods within those years, beginning on or after December 15, 2012, and should be applied prospectively to any new indemnification assets acquired after the date of adoption and to indemnification assets existing as of the date of adoption. Early adoption is permitted. The adoption of this update is not expected to have any impact on the Company s consolidated financial position or results of operations.

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Safe Harbor Statement for Forward-Looking Statements

This report may contain forward-looking statements within the meaning of the federal securities laws. These statements are not historical facts; rather they are statements based on the Company s current expectations regarding its business strategies and their intended results and its future performance. Forward-looking statements are preceded by terms such as expects, believes, anticipates, intends and similar expressions.

Forward-looking statements are not guarantees of future performance. Numerous risks and uncertainties could cause or contribute to the Company s actual results, performance and achievements being materially different from those expressed or implied by the forward-looking statements. Factors that may cause or contribute to these differences include, without limitation, general economic conditions, including changes in market interest rates and changes in monetary and fiscal policies of the federal government; legislative and regulatory changes; the quality and composition of the loan and investment securities portfolio; loan demand; deposit flows; competition; and changes in accounting principles and guidelines. Additional factors that may affect our results are discussed in Part II of the Form 10-Q and in our Annual Report on Form 10-K for the year ended December 31, 2011 under Item 1A. Risk Factors. These factors should be considered in evaluating the forward-looking statements and undue reliance should not be placed on such statements. Except as required by applicable law or regulation, the Company assumes no obligation and disclaims any obligation to update any forward-looking statements.

Critical Accounting Policies

During the nine months ended September 30, 2012, there was no significant change in the Company s critical accounting policies or the application of critical accounting policies as disclosed in the Company s Annual Report on Form 10-K for the year ended December 31, 2011.

Financial Condition

Total assets increased from $438.9 million at December 31, 2011 to $458.4 million at September 30, 2012, an increase of 4.4%.

Net loans receivable (excluding loans held for sale) increased $4.9 million from $276.0 million at December 31, 2011 to $281.0 million at September 30, 2012. Commercial mortgage loans and construction loans increased $6.3 million and $4.9 million, respectively, during the nine months ended September 30, 2012. The Bank has actively pursued new commercial mortgage opportunities during the period. These increases were partially offset by a decrease of $4.7 million in residential mortgage loans, primarily due to loan payoffs that have not been replaced by new originations for the Bank s portfolio as the Bank has continued to sell fixed rate residential mortgage loans in the secondary market.

Securities available for sale increased $11.9 million from $111.4 million at December 31, 2011 to $123.4 million at September 30, 2012. Purchases of $54.8 million of securities classified as available for sale were made during the nine months ended September 30, 2012 and consisted primarily of U.S. government agency notes and bonds, CMOs and municipal bonds. Maturities, principal repayments and sales of available for sale securities totaled $27.8 million, $11.6 million and $2.9 million, respectively, during the nine months ended September 30, 2012.

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Cash and cash equivalents increased from $18.9 million at December 31, 2011 to $22.7 million at September 30, 2012, primarily due to an increase of $4.5 million in federal funds sold partially offset by a $2.5 million decrease in cash and due from banks.

Total deposits increased 5.4% from $364.4 million at December 31, 2011 to $384.1 million at September 30, 2012. Interest-bearing demand and savings accounts increased $15.2 million and noninterest-bearing checking accounts increased $14.2 million during the nine months ended September 30, 2012. This was partially offset by a $9.7 million decrease in time accounts due to customers not wanting to lock in to longer terms in the current low-rate environment.

Federal Home Loan Bank borrowings decreased from $12.4 million at December 31, 2011 to $10.1 million at September 30, 2012 due to repayments of $2.3 million during the period.

Retail repurchase agreements, which represent overnight borrowings from deposit customers, including businesses and local municipalities, totaled $9.1 million at both December 31, 2011 and September 30, 2012.

Total stockholders equity attributable to the Company increased from $50.9 million at December 31, 2011 to $52.1 million at September 30, 2012 primarily due to retained net income of $1.1 million.

Results of Operations

Net Income attributable to the Company for the nine-month periods ended September 30, 2012 and 2011. Net income attributable to the Company was $2.7 million ($0.96 per share diluted) for the nine months ended September 30, 2012 compared to $2.9 million ($1.05 per share diluted) for the same period in 2011. The decrease is primarily due to the Bank s previously announced voluntary early retirement program that was effective September 30, 2012. Fourteen employees participated in the program which resulted in a pre-tax charge of $693,000 during September 2012. Had this nonrecurring expense not occurred, the Company would have recognized net income of $3.1 million ($1.11 per share diluted) for the nine months ended September 30, 2012. The Company expects to save approximately $617,000 on a pre-tax basis in the first year following the effective date of the voluntary early retirement program due to lower compensation and benefits expense.

Net Income attributable to the Company for the three-month periods ended September 30, 2012 and 2011. Net income attributable to the Company was $719,000 ($0.26 per share diluted) for the three months ended September 30, 2012 compared to $1.1 million ($0.39 per share diluted) for the same period in 2011. Again, the decrease is primarily due to the expenses related to the voluntary early retirement program. Excluding that program, the Company would have reported net income of $1.1 million ($0.41 per share diluted) for the three months ended September 30, 2012.

Net interest income for the nine-month periods ended June 30, 2012 and 2011. Net interest income decreased $204,000 for the nine months ended September 30, 2012 compared to the same period in 2011 primarily due to a decrease in the interest rate spread between interest-earning assets and interest-bearing liabilities. This was partially offset by a decrease in the average balance of interest-bearing liabilities.

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Total interest income decreased $1.2 million for the nine months ended September 30, 2012 compared to the same period in 2011. For the nine months ended September 30, 2012, the tax-equivalent yield on interest-earning assets was 4.65%. During the same period in 2011, the tax-equivalent yield was 5.09%. The decrease in the tax-equivalent yield was due to a decrease in yields across all asset types due to interest rates remaining near historic low levels. The change in asset mix also contributed to the lower yield for 2012 as the average balance of loans receivable, which generally have higher yields than investment securities and other short-term investments, decreased from $293.8 million for the nine months ended September 30, 2011 to $280.0 million for the same period in 2012, while the average balance of investment securities increased from $107.7 million for 2011 to $116.7 million and the average balance of federal funds sold increased from $9.6 million to $18.0 million for 2012.

Total interest expense decreased $1.0 million for the nine months ended September 30, 2012 compared to the same period in 2011. The average balance of interest-bearing liabilities decreased from $348.4 million for 2011 to $341.7 million for 2012. The average rate paid on those liabilities decreased from 1.13% for the nine months ended September 30, 2011 to 0.75% for the same period in 2012 primarily as a result of the low rate environment previously discussed. As a result, the tax-equivalent interest rate spread decreased from 3.96% for the nine-month period ended September 30, 2011 to 3.90% for the same period in 2012.

Net interest income for the three-month periods ended September 30, 2012 and 2011. Net interest income decreased $57,000 for the three months ended September 30, 2012 compared to the same period in 2011 primarily due to a decrease in the interest rate spread.

Total interest income decreased $379,000 when comparing the two periods as the average tax-equivalent yield on interest-earning assets decreased from 5.12% for the quarter ended September 30, 2011 to 4.59% for the same period in 2012. This was partially offset by an increase in the average balance of interest-earning assets from $409.6 million for the quarter ended September 30, 2011 to $423.9 million for the quarter-ended September 30, 2012.

Total interest expense decreased $322,000 for the three months ended September 30, 2012 compared to the same period in 2011. The cost of interest-bearing liabilities decreased from 1.05% for the three months ended September 30, 2011 to 0.67% for the same period in 2012.

As a result of the changes described above, the tax-equivalent interest rate spread decreased from 4.07% for the quarter ended September 30, 2011 to 3.92% for the same period in 2012.

Provision for loan losses. The provision for loan losses decreased from $1.3 million for the nine-month period ended September 30, 2011 to $1.1 million for the same period in 2012, and from $400,000 for the three months ended September 30, 2011 to $350,000 for the three months ended September 30, 2012. Net charge offs amounted to $716,000 and $1.1 million for the nine-month periods ended September 30, 2012 and 2011, respectively. During the nine-month period ended September 30, 2012, gross loans receivable increased $5.3 million. As stated earlier in this report, commercial mortgage loans and construction loans increased $6.3 million and $4.9 million, respectively, while residential mortgage loans decreased $4.7 million during the nine months ended September 30, 2012. The decrease in the provision reflects the decrease in net charge-offs for 2012, partially offset by continued efforts to provide for inherent loss exposure due to weakened general economic conditions such as depreciating collateral values, job losses and continued pressures on household budgets in the Bank s market area.

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Provisions for loan losses are charges to earnings to maintain the total allowance for loan losses at a level considered adequate by management to provide for probable known and inherent loan losses based on management s evaluation of the collectibility of the loan portfolio, including the nature of the portfolio, credit concentrations, trends in historical loss experience, specified impaired loans and economic conditions. Although management uses the best information available, future adjustments to the allowance may be necessary due to changes in economic, operating, regulatory and other conditions that may be beyond the Bank s control. While the Bank maintains the allowance for loan losses at a level that it considers adequate to provide for estimated losses, there can be no assurance that further additions will not be made to the allowance for loan losses and that actual losses will not exceed the estimated amounts.

The methodology used in determining the allowance for loan losses includes segmenting the loan portfolio by identifying risk characteristics common to groups of loans, determining and measuring impairment of individual loans based on the present value of expected future cash flows or the fair value of collateral, and determining and measuring impairment for groups of loans with similar characteristics by applying loss factors that consider the qualitative factors which may affect the loss rates.

The allowance for loan losses was $4.6 million and $4.2 million at September 30, 2012 and December 31, 2011, respectively. Management has deemed these amounts as adequate on both dates based on its best estimate of probable known and inherent loan losses at each date. At September 30, 2012, nonperforming loans amounted to $8.1 million compared to $7.8 million at December 31, 2011. Included in nonperforming loans are loans over 90 days past due and still accruing interest which are secured by residential mortgage loans of $67,000 and consumer loans of $32,000. These loans are accruing interest because the estimated value of the collateral and collection efforts are deemed sufficient to ensure full recovery. At September 30, 2012 and December 31, 2011, nonaccrual loans amounted to $8.0 million and $7.4 million, respectively.

Noninterest income for the nine-month periods ended September 30, 2012 and 2011. Noninterest income for the nine months ended September 30, 2012 increased to $3.3 million compared to $3.0 million for the nine months ended September 30, 2011. Gains on the sale of loans, including residential mortgage and Small Business Administration (SBA) loans, increased $318,000 when comparing the two periods.

Noninterest income for the three-month periods ended September 30, 2012 and 2011. Noninterest income was $1.1 million for both of the quarters ended September 30, 2012 and September 30, 2011.

Noninterest expense for the nine-month periods ended September 30, 2012 and 2011. Noninterest expense for the nine months ended September 30, 2012 increased $722,000 compared to the nine months ended September 30, 2011. This increase was primarily due to a $577,000 increase in compensation and benefits expense, which was due to the previously mentioned $693,000 pre-tax charge for the voluntary early retirement program. Data processing expenses also increased $115,000 when comparing the two periods as a result of increased ATM processing fees and more customers using alternative delivery channels for retail products.

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Noninterest expense for the three-month periods ended September 30, 2012 and 2011. Noninterest expense for the quarter ended September 30, 2012 increased $652,000 compared to the quarter ended September 30, 2011. This increase was primarily due to a $588,000 increase in compensation and benefits expense related to the voluntary early retirement program.

Income tax expense. Income tax expense for the nine-month period ended September 30, 2012 was $1.0 million, for an effective tax rate of 27.3%, compared to $1.1 million, for an effective tax rate of 27.7% for the same period in 2011. For the three-month period ended September 30, 2012, income tax expense and the effective tax rate were $218,000 and 23.2%, respectively, compared to $451,000 and 29.2%, respectively, for the same period in 2011. The decrease in the effective tax rate for the quarter ended September 30, 2012 compared to the same period in 2011 was primarily the result of an increase in tax-exempt income as a percent of income before income taxes for 2012.

Liquidity and Capital Resources

The Bank s primary sources of funds are customer deposits, proceeds from loan repayments, maturing securities and FHLB advances. While loan repayments and maturities are a predictable source of funds, deposit flows and mortgage prepayments are greatly influenced by market interest rates, general economic conditions and competition. At September 30, 2012, the Bank had cash and cash equivalents of $22.7 million and securities available-for-sale with a fair value of $123.4 million. If the Bank requires funds beyond its ability to generate them internally, it has additional borrowing capacity with the FHLB of Indianapolis and additional collateral eligible for repurchase agreements.

The Bank s primary investing activity is the origination of one-to-four family mortgage loans and, to a lesser extent, consumer, multi-family, commercial real estate and residential construction loans. The Bank also invests in U.S. Government and agency securities and mortgage-backed securities issued by U.S. Government agencies.

The Bank must maintain an adequate level of liquidity to ensure the availability of sufficient funds to support loan growth and deposit withdrawals, to satisfy financial commitments and to take advantage of investment opportunities. Historically, the Bank has been able to retain a significant amount of its deposits as they mature.

The Bank is required to maintain specific amounts of capital pursuant to regulatory requirements. As of September 30, 2012, the Bank was in compliance with all regulatory capital requirements that were effective as of such date with tangible, core and risk-based capital ratios of 9.9%, 9.9% and 15.5%, respectively. The regulatory requirements at that date were 1.5%, 3.0% and 8.0%, respectively. At September 30, 2012, the Bank was considered well-capitalized under applicable regulatory guidelines.

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The Company is a separate legal entity from the Bank and must provide for its own liquidity. In addition to its operating expenses, the Company, on a stand-alone basis, is responsible for paying any dividends declared to its shareholders. The Company also has repurchased shares of its common stock. The Company s primary source of income is dividends received from the Bank. The amount of dividends that the Bank may declare and pay to the Company in any calendar year, without the receipt of prior approval from the Office of the Comptroller of the Currency (OCC) but with prior notice to the OCC, cannot exceed net income for that year to date plus retained net income (as defined) for the preceding two calendar years. On a stand-alone basis, the Company had liquid assets of $248,000 at September 30, 2012.

Off-Balance Sheet Arrangements

In the normal course of operations, the Company engages in a variety of financial transactions that, in accordance with GAAP, are not recorded on the Company s financial statements. These transactions involve, to varying degrees, elements of credit, interest rate and liquidity risk. Such transactions are primarily used to manage customers requests for funding and take the form of loan commitments and letters of credit. A further presentation of the Company s off-balance sheet arrangements is presented in the Company s 2011 Annual Report on Form 10-K for the year ended December 31, 2011.

For the nine months ended September 30, 2012, the Company did not engage in any off-balance sheet transactions reasonably likely to have a material effect on the Company s financial condition, results of operations or cash flows.

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QUANTITATIVE AND QUALITATIVE DISCLOSURES

ABOUT MARKET RISK

FIRST CAPITAL, INC.

For a discussion of the Company s asset and liability management policies, as well as the potential impact of interest rate changes upon the market value of the Company s portfolio equity, see Management s Discussion and Analysis of Financial Condition and Results of Operations -Market Risk Analysis in the Company s 2011 Annual Report Form 10-K for the year ended December 31, 2011. Management periodically reviews the impact of interest rate changes upon net interest income and the market value of the Company s portfolio equity. Based on such reviews, management believes that there have been no material changes in the market risk of the Company s asset and liability position since December 31, 2011.

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CONTROLS AND PROCEDURES

FIRST CAPITAL, INC.

Controls and Procedures

The Company s management, including the Company s principal executive officer and principal financial officer, have evaluated the effectiveness of the Company s disclosure controls and procedures, as such term is defined in Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended, (the Exchange Act). Based upon their evaluation, the principal executive officer and principal financial officer concluded that, as of the end of the period covered by this report, the Company s disclosure controls and procedures were effective for the purpose of ensuring that the information required to be disclosed in the reports that the Company files or submits under the Exchange Act with the SEC (1) is recorded, processed, summarized, and reported within the time periods specified in the SEC s rules and forms, and (2) is accumulated and communicated to the Company s management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure.

There have been no changes in the Company s internal control over financial reporting during the quarter ended September 30, 2012 that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

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PART II

OTHER INFORMATION

FIRST CAPITAL, INC.

Item 1. Legal Proceedings

The Company is not a party to any legal proceedings. Periodically, there have been various claims and lawsuits involving the Bank, mainly as a plaintiff, such as claims to enforce liens, condemnation proceedings on properties in which the Bank holds security interests, claims involving the making and servicing of real property loans and other issues incident to the Bank s business. The Bank is not a party to any pending legal proceedings that it believes would have a material adverse affect on its financial condition or operations.

Item 1A. Risk Factors

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2011, which could materially affect our business, financial condition or future results. There have been no material changes to the risk factors described in our Annual Report on Form 10-K, however these are not the only risks that we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds
Issuer Purchases of Equity Securities

On August 19, 2008, the board of directors authorized the repurchase of up to 240,467 shares of the Company s outstanding common stock. The stock repurchase program will expire upon the purchase of the maximum number of shares authorized under the program, unless the board of directors terminates the program earlier. There were no shares purchased under the stock repurchase program during the quarter ended September 30, 2012. The maximum number of shares that may yet be purchased under the plan is 189,582.

Item 3. Defaults upon Senior Securities

Not applicable.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

PART II

OTHER INFORMATION

FIRST CAPITAL, INC.

Item 6. Exhibits

3.1	Articles of Incorporation of First Capital, Inc. (1)
3.2	Fourth Amended and Restated Bylaws of First Capital, Inc. (2)
10.1	*Employment Agreement with M. Chris Frederick (4)
10.2	*Employee Severance Compensation Plan (3)
10.3	*Employment Agreement with William W. Harrod (4)
10.4	* First Capital, Inc. 2009 Equity Incentive Plan (5)
10.5	Statement Re: Computation of Per Share Earnings (incorporated by reference to Note 3 of the Unaudited Consolidated Financial Statements contained herein)
31.1	Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer
31.2	Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer
32.1	Section 1350 Certification of Chief Executive Officer
32.2	Section 1350 Certification of Chief Financial Officer
101.0**	The following materials from the Company s Quarterly Report on Form 10-Q for the quarter ended September 30, 2012, formatted in XBRL (Extensible Business Reporting Language): (i) the Consolidated Balance Sheets, (ii) the Consolidated Statements of Income, (iii) the Consolidated Statements of Comprehensive Income; (iv) the Consolidated Statements of Changes in Stockholders Equity; (v) the Consolidated Statements of Cash Flows and (vi) the Notes to the Consolidated Financial Statements.

* Management contract or compensatory plan, contract or arrangement.
** Furnished, not filed.
(1) Incorporated by reference from the Exhibits filed with the Registration Statement on Form SB-2, and any amendments thereto, Registration No. 333-63515.
(2) Incorporated by reference to the Current Report on Form 8-K filed with the Securities and Exchange Commission on August 22, 2007.
(3) Incorporated by reference to the Quarterly Report on Form 10-QSB for the quarter ended December 31, 1998.
(4) Incorporated by reference to the Annual Report on Form 10-KSB for the year ended December 31, 1999.
(5) Incorporated by reference to the appendix to the Company s definitive proxy materials on Schedule 14A filed with the Securities and Exchange Commission on April 9, 2009.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

	FIRST CAPITAL, INC.
	(Registrant)
Dated November 13, 2012	**BY**: /s/ William W. Harrod William W. Harrod President and CEO
Dated November 13, 2012	**BY**: /s/ Michael C. Frederick Michael C. Frederick Senior Vice President, CFO and Treasurer