

2013
SHAREHOLDER
UPDATE

Q2



TO OUR SHAREHOLDERS

Following is our report of results for the second quarter of 2013. During the quarter, we continued to focus on our “strategic services,” which include business services and residential broadband. We celebrated the opening of our Raleigh, NC area data center in July, as we are now turning up customers in this new facility. As well, we have announced plans for opening another data center in the Charlotte, NC area around mid-year 2014. Our press release on this announcement can be found under Press Releases in the Shareholder News section of our website. Highlighting the quarter were continued steady growth in our data center business revenue, growth in both our business and residential segments, growth in residential broadband connections and increased average revenue per customer on both the business and residential sides. Additional highlights include improved margins driven by stable, high margins from our data center business, as well as improved margins in residential broadband thanks to extensive work by our team addressing costs. Our EBITDA (Earnings Before Interest, Taxes & Depreciation and Amortization) margin of 41% improved 28% compared to the second quarter of last year. While we have done a good job controlling costs, our management team is committed to relentlessly pursuing growth by offering great products that help businesses prosper, such as our data management and premium collocation services, and products that enable and inspire people and households, such as our fiber-fast Internet and brilliant television, offered through an extraordinary and unique customer experience.

We appreciate your continued interest and support of North State.



J. Patrick Harman
Chairman and
Chief Executive Officer



Royster Tucker III
Vice Chairman, President
and Chief Operating Officer



Jonathan M. Cage
Vice President, Chief Financial Officer

2013 SECOND QUARTER CONSOLIDATED FINANCIAL HIGHLIGHTS

Consolidated net operating revenues were \$22.1 million in the second quarter of 2013, down slightly compared to \$22.3 million for the 2012 second quarter. Total operating revenues from strategic services, which includes business services and residential broadband, increased 8.4% compared to the year earlier quarter. Overall revenue growth for the quarter was tempered by a continued decline in wholesale revenue and a spike in churn related to disconnects for non-payment from residential customers. Total operating expenses were down 5.3% compared to the second quarter of 2012, leading to a 67% increase in income from continuing operations. Non-operating income was \$2.3 million compared to \$1.3 million, boosted by a 21.8% increase in equity in earnings of our Verizon wireless partnership and a \$0.7 million increase in other income, the result of a dividend distribution related to our participation in a cooperative vendor relationship. Net income was \$3.9 million, up 71% from \$2.3 million in the year earlier quarter. Earnings per share were \$1.69, up from \$0.98. EBITDA was \$11.5 million compared to \$9.0 million in the second quarter of 2012.

Net cash provided by operating activities was \$8.3 million for the second quarter of 2013 compared to \$6.1 million for the second quarter of 2012. Capital expenditures were \$5.0 million compared to \$7.9 million with the 2013 second quarter capital expenditures primarily related to the up-fit of our Raleigh, NC data center. Cash distributions from our wireless partnership with Verizon were \$1.9 million in the second quarter of 2013 compared to \$3.5 million in the second quarter of 2012, reflecting a timing difference of when the distributions were made. Free cash flow (cash from operating activities plus cash distributions from Verizon minus capital expenditures) was \$5.2 million in the second quarter of 2013 compared to \$1.6 million in the second quarter of 2012. Cash dividends were \$3.0 million in the second quarter of 2013, equal to dividends paid in the second quarter of 2012.

CONSOLIDATED FINANCIAL HIGHLIGHTS FOR THE FIRST HALF OF 2013

Net operating revenues for the first six months of 2013 were \$44.3 million compared to \$44.1 million for the first six months of 2012. Total operating expenses were down 3.8% for the period. Operating income from continuing operations was \$5.4 million, up from \$3.7 million. Income from continuing operations was \$5.5 million compared to \$3.9 million. Income from discontinued operations was \$2.0 million compared to \$1.3 million. Total non-operating income was \$3.4 million compared to \$2.5 million. Net income was \$7.5 million, up from \$5.2 million in the year earlier first six months. Earnings per share were \$3.25, up from \$2.26. EBITDA was \$22.5 million compared to \$19.0 million in the first half of 2012.

Net cash provided by operating activities was \$15.7 million for the first six months of 2013 compared to \$13.5 million for the first six months of 2012. Capital expenditures were \$7.3 million compared to \$18.1 million because investments have been focused on data center expansion and success-based capitalized costs of broadband sales for the first half of this year with targeted fiber builds planned for the second half of the year. Cash distributions from our wireless partnership with Verizon were \$3.7 million in the first half of 2013 compared to \$3.5 million in the first half of 2012. Free cash flow was \$12.1 million compared to a negative \$1.0 million in the first half of 2012. Cash dividends were \$6.0 million in the first half of 2013, equal to dividends paid in the first half of 2012.

BUSINESS SERVICES

Business services include Cloud Voice and integrated data products, broadband, traditional voice services and data center services for enterprise and small businesses. Total operating revenues from business services were \$9.0 million in the second quarter of 2013, up 5% from the second quarter of 2012 driven by growth in data center, Cloud Voice and broadband. Data center total operating revenues generated by DataChambers were \$3.0 million, up 15% from the year earlier quarter. Total operating revenues from business broadband, which

include Cloud Voice and broadband, were \$2 million in the second quarter of 2013 compared to \$1.9 million in the second quarter of 2012. Average monthly revenue per connected business unit was \$338.78 for the second quarter of 2013 compared to \$318.62 for the same period of 2012.

RESIDENTIAL SERVICES

Residential services include Plex Broadband Internet, Plex Advanced TV, Plex Voice and traditional voice services for households. Total operating revenues from residential services were \$9.1 million in the second quarter of 2013 compared to \$8.7 million in the second quarter of 2012. Residential broadband total operating revenues, which include video and broadband Internet, were \$5.4 million, up 14% from the second quarter of 2012 mainly due to increased video penetration and demand for faster broadband Internet speeds. At the end of the quarter, total residential broadband connections were 38,061, a 4% increase over the second quarter of 2012. Residential voice connections were 36,367, down 10% from second quarter of 2012 with broadband connections now surpassing voice connections, a sign of the continuing shift of the marketplace.

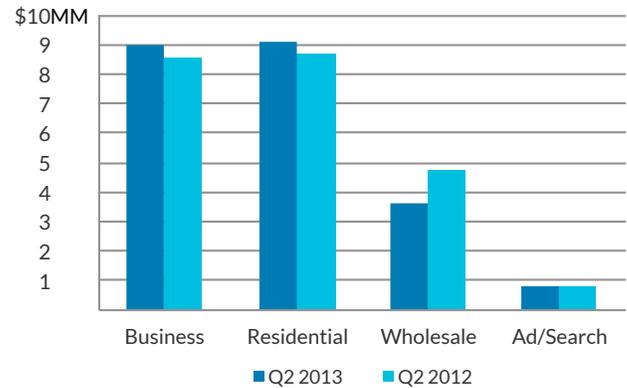
WHOLESALE SERVICES

Wholesale services, largely comprising access services, have been in decline for some time with the changing face of the industry. Wholesale total operating revenues were \$3.6 million in the second quarter of 2013 compared to \$4.7 million in the second quarter of 2012, reflecting reduced usage, the effects of national access reform programs and changes in access settlement formulas.

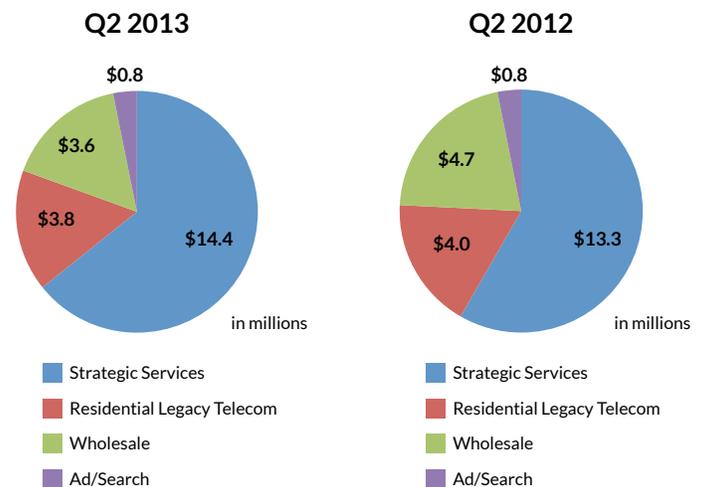
ADVERTISING & SEARCH

Advertising and search total operating revenues were \$0.8 million in the second quarter of 2013, up 1.6% from the second quarter of 2012 with a 19% increase in online search and advertising revenues offsetting a 7% decline in print advertising revenues during the quarter.

Q2 2013 vs Q2 2012
Total Operating Revenue



Strategic Revenues



Consolidated Balance Sheets—Unaudited

At June 30,	2013	2012
Assets		
Current assets:		
Cash and cash equivalents	\$ 3,393,175	\$ 2,406,234
Investment securities	399,099	2,616,900
Accounts receivable, net of allowance for doubtful accounts	8,254,360	10,122,392
Materials and supplies	4,639,647	6,190,097
Prepayments	1,529,866	1,595,316
Income taxes recoverable	2,423,604	2,422,315
Deferred income taxes	1,196,986	4,159,866
Assets held for sale, net of liabilities	10,128,837	11,511,887
Total current assets	31,965,574	41,025,007
Property, plant, and equipment	460,221,618	448,304,403
Less accumulated depreciation	314,306,333	301,577,556
Property, plant, and equipment, net	145,915,285	146,726,847
Other assets:		
Investment securities	4,311,359	3,639,364
Investments in unconsolidated entities	9,567,601	10,943,663
Intangibles, net of amortization	18,052,300	19,301,714
Goodwill	27,232,656	27,232,656
Other noncurrent assets	1,353,894	2,830,875
Total other assets	60,517,810	63,948,272
Total assets	\$ 238,398,669	\$ 251,700,126
Liabilities and Stockholders' Equity		
Current liabilities:		
Revolving credit note	\$ -	\$ 6,000,000
Current maturities of bank note	5,500,000	-
Accounts payable and payroll withholdings	2,833,423	3,609,117
Advance billings and customer deposits	3,357,295	3,203,054
Income taxes payable	184,196	-
Accrued expenses	5,154,203	5,914,530
Accrued taxes	965,406	959,936
Total current liabilities	17,994,523	19,686,637
Other liabilities:		
Bank note, net of current maturities	49,500,000	55,000,000
Deferred income taxes	21,093,726	22,576,596
Accrued pension benefits	42,796,696	37,919,007
Accrued postretirement benefits	1,522,487	1,609,753
Other liabilities and deferred credits	777,217	934,033
Total other liabilities	115,690,126	118,039,389
Total liabilities	133,684,649	137,726,026
Stockholders' equity:		
Preferred stock	1,961,400	1,980,600
Common stock	11,446,125	11,466,080
Paid in capital	47,422	45,808
Retained earnings	117,338,522	124,291,202
Accumulated other comprehensive loss	(26,079,449)	(23,809,590)
Total stockholders' equity	104,714,020	113,974,100
Total liabilities and stockholders' equity	\$ 238,398,669	\$ 251,700,126

Consolidated Statements of Net Income with Discontinued Operations—Unaudited

Six Months Ended June 30,	2013	2012
Operating revenues:		
Local service	\$ 12,088,461	\$ 12,633,565
Network access	8,248,675	10,513,503
Long distance	1,833,134	1,869,764
Miscellaneous	735,436	628,162
Legacy telecom	22,905,706	25,644,994
Broadband	14,761,904	12,628,614
Total wireline	37,667,610	38,273,608
Data center	5,854,483	5,172,806
Advertising and search	1,651,546	1,620,205
Total operating revenues	45,173,639	45,066,619
Less uncollectible revenue	894,226	940,780
Net operating revenues	44,279,413	44,125,839
Cost of sales and service:		
General support	2,454,619	2,366,093
Central office	4,553,605	5,932,654
Communication termination	5,122,780	5,408,671
Cable and wire facilities	2,127,177	2,796,012
Network operations	3,713,638	3,908,191
Total cost of sales and service	17,971,819	20,411,621
Gross margin	26,307,594	23,714,218
Depreciation and amortization expense	9,280,839	9,432,329
Selling, general, and administrative expense:		
Customer operations	7,505,193	7,087,928
Corporate operations	3,459,778	2,795,980
Taxes, other than income taxes	648,040	682,213
Total selling, general, and administrative expense	11,613,011	10,566,121
Net operating income	5,413,744	3,715,768
Nonoperating income (expense):		
Interest income	27,395	91,429
Interest expense, net of capitalized interest	(507,284)	(631,277)
Equity in earnings of unconsolidated entities	3,602,108	2,867,131
Net gain on sale of investment securities	-	184,293
Other income, net	310,216	29,588
Net nonoperating income	3,432,435	2,541,164
Income from continuing operations before income taxes	8,846,179	6,256,932
Income taxes from continuing operations	3,352,908	2,315,401
Income from continuing operations	5,493,271	3,941,531
Discontinued operations:		
Income from operations of discontinued business segment	3,264,395	2,095,612
Income taxes from discontinued operations	1,258,554	807,942
Income from discontinued operations	2,005,841	1,287,670
Net income	7,499,112	5,229,201
Preferred stock dividends	46,561	47,041
Net income available to common stockholders	\$ 7,452,551	\$ 5,182,160
Earnings per average common share	\$3.25	\$2.26
Weighted average common shares outstanding	2,290,724	2,294,778
Dividends per common share	\$2.60	\$2.60

Consolidated Statements of Comprehensive Income—Unaudited

Six Months Ended June 30,	2013	2012
Net income	\$ 7,499,112	\$ 5,229,201
Other comprehensive income, net of tax:		
Unrealized holding gains arising during the period, net of tax expense in 2013 of \$58,669 and tax expense in 2012 of \$101,529	89,919	155,603
Other comprehensive income, net of tax	89,919	155,603
Comprehensive income	\$ 7,589,031	\$ 5,384,804

Consolidated Statements of Stockholders' Equity—Unaudited

Six Months Ended June 30,	Preferred Stock	Common Stock	Paid in Capital	Retained Earnings	Accumulated Other Comprehensive Income			Total Stockholders' Equity
					Retirement Plans	Marketable Securities	Total	
Balance, January 1, 2012	\$ 1,985,100	\$ 11,478,450	\$ 43,718	\$ 125,264,278	\$ (23,822,385)	\$ (142,808)	\$ (23,965,193)	\$ 114,806,353
Acquisition of stock	(4,500)	(12,370)	2,090					(14,780)
Net income				5,229,201				5,229,201
Preferred stock dividends				(47,041)				(47,041)
Common stock dividends				(5,967,494)				(5,967,494)
Acquisition of common stock in excess of stated value				(187,742)				(187,742)
Unrealized gain on marketable securities, net of tax expense						155,603	155,603	155,603
Balance, June 30, 2012	\$ 1,980,600	\$ 11,466,080	\$ 45,808	\$ 124,291,202	\$ (23,822,385)	\$ 12,795	\$ (23,809,590)	\$ 113,974,100
Balance, January 1, 2013	\$ 1,965,600	\$ 11,463,565	\$ 45,658	\$ 116,084,044	\$ (26,160,721)	\$ (8,647)	\$ (26,169,368)	\$ 103,389,499
Acquisition of stock	(4,200)	(17,440)	1,764					(19,876)
Net income				7,499,112				7,499,112
Preferred stock dividends				(46,561)				(46,561)
Common stock dividends				(5,957,393)				(5,957,393)
Acquisition of common stock in excess of stated value				(240,680)				(240,680)
Unrealized gain on marketable securities, net of tax expense						89,919	89,919	89,919
Balance, June 30, 2013	\$ 1,961,400	\$ 11,446,125	\$ 47,422	\$ 117,338,522	\$ (26,160,721)	\$ 81,272	\$ (26,079,449)	\$ 104,714,020

Consolidated Statements of Cash Flows—Unaudited

Six Months Ended June 30,	2013	2012
Cash flows from operating activities:		
Net income	\$ 7,499,112	\$ 5,229,201
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	9,837,376	10,003,318
Gain on sale of investment securities	-	(184,293)
Donated land	372,414	-
Loss on sale, disposal, and abandonment of other assets	140,585	185,544
Equity in earnings of unconsolidated entities	(3,602,108)	(2,867,131)
Deferred income taxes	624,529	4,418,120
Deferred pension and postretirement benefits	1,260,248	1,012,648
Changes in operating assets and liabilities:		
Accounts receivable	646,587	(1,255,241)
Materials and supplies	884,068	(397,801)
Other assets	(1,557,507)	1,441,442
Accounts payable and payroll withholdings	(1,207,217)	(3,006,892)
Accrued expenses	307,893	375,197
Other liabilities	494,409	(1,471,649)
Net cash provided by operating activities	<u>15,700,389</u>	<u>13,482,463</u>
Cash flow from investing activities:		
Additions to property, plant, and equipment	(7,280,530)	(18,083,781)
Cost of removal of telephone plant, net of salvage	10,049	(15,544)
Proceeds from sale of investment securities	-	2,619,333
Purchases of investment securities	(397,742)	(455,854)
Distributions from equity investments	-	161,341
Distributions from unconsolidated entities	3,718,720	3,486,300
Net cash used in investing activities	<u>(3,949,503)</u>	<u>(12,288,206)</u>
Cash flows from financing activities:		
Proceeds (repayments) from revolving credit note, net	(6,000,000)	3,500,000
Loan origination fees	(5,397)	(4,210)
Acquisition of preferred stock	(2,436)	(2,410)
Acquisition of common stock	(258,120)	(200,112)
Cash dividends paid	(6,003,954)	(6,014,535)
Net cash used in financing activities	<u>(12,269,907)</u>	<u>(2,721,267)</u>
Net change in cash and cash equivalents	(519,021)	(1,527,010)
Cash and cash equivalents at beginning of year	3,912,196	3,933,244
Cash and cash equivalents at end of period	<u>\$ 3,393,175</u>	<u>\$ 2,406,234</u>
Short term investment securities at end of period	<u>\$ 399,099</u>	<u>\$ 2,616,900</u>
Total cash, cash equivalents, and short term investment securities	<u>\$ 3,792,274</u>	<u>\$ 5,023,134</u>
Supplemental cash flow information:		
Cash payments (refunds) of income taxes	<u>\$ 3,080,278</u>	<u>\$ (75,000)</u>
Cash paid for interest	<u>\$ 539,004</u>	<u>\$ 601,719</u>

I, Jonathan M. Cage, hereby certify that the accompanying unaudited consolidated balance sheets of North State Telecommunications Corporation and Subsidiaries as of June 30, 2013 and 2012 and the related unaudited consolidated statements of net income, comprehensive income, stockholders' equity, and cash flows for the six months then ended have been prepared from the Corporation's and Subsidiaries' accounting records. Internal accounting controls and review procedures provide assurance that these statements are materially accurate.

This is the 24th day of July 2013.



Jonathan M. Cage

Vice President, Chief Financial Officer, Secretary and Treasurer

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Royster Tucker III—Vice Chairman
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Jonathan M. Cage
William H. Dula

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Chief Executive Officer

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Corporate Administration

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and Chief Operating Officer

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Technology and Operations

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Vice President, Chief Financial Officer

Richard P. Worden
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Sales and Marketing

CORPORATE OFFICES

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