

BAKER BOYER BANCORP

THIRD QUARTER

REPORT

2006



Baker Boyer Bancorp

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Letter To Our Shareholders

October 23, 2006

Dear Baker Boyer Shareholders:

I am pleased to report that both our profits and our performance, as measured by our Return on Equity, increased over last year's third quarter. Net income through September is up 3.4% to \$3.265 million and Return on Equity has improved to 13.2%. We also saw impressive growth in our Investment Management and Trust assets and made important strides in providing tools to serve the growing number of customers using online banking and other internet services.

These results came as the competitive environment continued to be extremely challenging. Banks across the country are fiercely competing for loans and deposits, which is having a negative impact on net interest income and is putting pressure on earnings. Year-to-date net interest income declined 3% to \$11.4 million. To reverse this trend we must continue to grow loans while carefully managing deposit costs. Loans have increased in the past twelve months while we have consciously allowed high cost deposits such as general certificates of deposit to run-off. This has led to a decline in deposits, but the good news is core deposits are holding steady. I am also very proud of the continued improvement in the quality of our loan portfolio. This allowed for a smaller provision for loan losses, which offsets the net interest income decline. Net interest income after provision for loan losses was up \$140,000.

We are unique among community banks in the strength and size of our Investment Management and Trust Division and it continues to improve. Revenues provide nearly two thirds of the bank's total fee income and the division hit two milestones in the third quarter. First, assets under management were at an all time high of \$580 million. Second, assets at our new office in Yakima exceeded \$30 million.

The prospect for future growth in IMT revenues is strong. We offer a unique level of premier services and have a top performing team of portfolio managers. Our visibility has been enhanced by their frequent appearances on national business television shows, talking about stocks and economic issues. You can see video replays of these appearances at our website, www.bakerboyer.com, on the "In the News" page.

We are also pleased at the success our employees are having in introducing more Baker Boyer customers to our growing list of technology products. One example is our internet bill pay product, which is competitive with big league providers like Yahoo and major banks. In our case, it also comes with the personal service our clients expect. This month we kicked off a major bank-wide free bill pay campaign. By reaching out to clients, our employees were able to nearly double the number of bill pay accounts in just three weeks. This keeps us on track with our campaign goal to more than triple users by the end of November.

This is a true win-win for the bank and our customers. Industry research has shown that customers who use bill pay services keep higher balances and are more profitable. Internet payments via bill pay are also safer than direct internet transactions and clients love the convenience.

I want to thank our employees for making this campaign a success. If you haven't already signed up for Baker Boyer's free bill pay service, contact us and experience the advantage of no more checks, no more stamps, and no more hassles. As always, we greatly appreciate your referrals, comments and support as we continue to grow Baker Boyer and maintain our position as the state's oldest independent community bank.

We look forward to a busy and productive fourth quarter and hope you will take time to join us for one of our traditional holiday celebrations.

Sincerely,

Megan F. Clubb

Megan F. Clubb
President and CEO

Board of Directors

Megan F. Clubb, Chair
D.F. Baker
Jon S. Bren
David B. Campbell
Thomas W. Campbell

Stephen G. Kimball
Edward N. Lange
Susan C. Pratt
Robert R. Richards

Consolidated Balance Sheets

(Unaudited)

	September 30,		% Chg.
	2006	2005	
	(Dollars in Thousands)		
ASSETS			
Cash and due from banks	\$14,122	\$10,274	37.45
Federal funds sold and security resell agreements	1,730	-	-
Investment securities			
Held-to-maturity	25,407	32,048	(20.72)
Available-for-sale	49,329	66,341	(25.64)
	<u>74,736</u>	<u>98,389</u>	<u>(24.04)</u>
Other securities	1,880	1,690	11.24
Loans	261,738	257,405	1.68
Less: Allowance for loan losses	(3,595)	(3,088)	16.42
	<u>258,143</u>	<u>254,317</u>	<u>1.50</u>
Bank premises and equipment, net of accumulated depreciation	9,780	8,548	14.41
Accrued interest receivable	3,687	3,667	0.55
Other assets	1,137	925	22.92
TOTAL ASSETS	<u>\$365,215</u>	<u>\$377,810</u>	<u>(3.33)</u>
LIABILITIES AND SHAREHOLDERS' EQUITY			
Deposits			
Noninterest bearing	\$68,174	\$71,575	(4.75)
Interest bearing	256,091	258,827	(1.06)
TOTAL DEPOSITS	<u>324,265</u>	<u>330,402</u>	<u>(1.86)</u>
Federal funds purchased and security repurchase agreements	6,546	8,170	(19.88)
Other borrowed funds	-	5,000	(100.00)
Accrued interest payable	555	379	46.44
Other liabilities	489	1,247	(60.79)
TOTAL LIABILITIES	<u>331,855</u>	<u>345,198</u>	<u>(3.87)</u>
SHAREHOLDERS' EQUITY			
Common stock (no par value, \$3.125 stated value)			
	9/30/06	9/30/05	
Shares authorized	4,000,000	4,000,000	
Shares issued and outstanding	1,297,790	1,299,931	
Capital surplus	1,008	1,112	(9.35)
Retained earnings	28,846	27,753	3.94
Unearned shares - Long-Term Performance & Retention Plan	(334)	(245)	36.33
Accumulated other comprehensive income (loss)	(215)	(70)	207.14
TOTAL SHAREHOLDERS' EQUITY	<u>33,360</u>	<u>32,612</u>	<u>2.29</u>
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	<u>\$365,215</u>	<u>\$377,810</u>	<u>(3.33)</u>

Consolidated Statements of Income

(Unaudited)

	Nine Months Ending September 30,		% Chg.
	2006	2005	
	(Dollars in Thousands)		
Interest Income:			
Loans, including fees	\$14,093	\$12,670	11.23
Investment securities			
Taxable	1,162	1,390	(16.40)
Tax-exempt	1,068	1,141	(6.40)
	<u>2,230</u>	<u>2,531</u>	<u>(11.89)</u>
Other securities	20	23	(13.04)
Federal funds sold	110	25	340.00
TOTAL INTEREST INCOME	<u>16,453</u>	<u>15,249</u>	<u>7.90</u>
Interest Expense:			
Interest bearing deposits	4,894	3,272	49.57
Federal funds purchased and security repurchase agreements	105	154	(31.82)
Other borrowed funds	52	68	(23.53)
	<u>5,051</u>	<u>3,494</u>	<u>44.56</u>
TOTAL INTEREST EXPENSE	<u>5,051</u>	<u>3,494</u>	<u>44.56</u>
NET INTEREST INCOME	<u>11,402</u>	<u>11,755</u>	<u>(3.00)</u>
Provision for loan losses	<u>587</u>	<u>1,080</u>	<u>(45.65)</u>
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	<u>10,815</u>	<u>10,675</u>	<u>1.31</u>
Other Income:			
Investment Management and Trust fees	3,053	3,004	1.63
Service charges on deposits	831	857	(3.03)
Other service charges and fees	809	781	3.59
Investment securities gains/losses	-	(16)	(100.00)
Other operating income	164	210	(21.90)
	<u>4,857</u>	<u>4,836</u>	<u>0.43</u>
Other Expense:			
Salaries and wages	5,818	5,597	3.95
Retirement and employee benefits	1,796	1,829	(1.80)
Net occupancy expense	643	585	9.91
Furniture and equipment expense	533	527	1.14
Other operating expense	2,580	2,815	(8.35)
	<u>11,370</u>	<u>11,353</u>	<u>0.15</u>
INCOME BEFORE INCOME TAXES	<u>4,302</u>	<u>4,158</u>	<u>3.46</u>
Provision for income taxes	<u>1,037</u>	<u>999</u>	<u>3.80</u>
NET INCOME	<u>\$3,265</u>	<u>\$3,159</u>	<u>3.36</u>
Basic Earnings Per Common Share	<u>\$2.53</u>	<u>\$2.44</u>	<u>3.69</u>
Average number of shares outstanding	<u>1,289,816</u>	<u>1,294,087</u>	