# ASB FINANCIAL CORP.

# 2006 ANNUAL REPORT TO SHAREHOLDERS

Dear Fellow Shareholder:

We are pleased to present ASB Financial Corp.'s Annual Report to Shareholders covering the fiscal year ended June 30, 2006.

Net earnings for the fiscal year ended June 30, 2006, totaled $1.67 million, or $1.05 per diluted share, which represents a decrease of $482,000, compared to the record net earnings reported for fiscal year 2005. Total assets amounted to $198.5 million at June 30, 2006, an increase of $13.7 million, or 7.4% over June 30, 2005. The loan portfolio grew by a record $16.9 million or 11.6%, during fiscal 2006, while deposits increased by a record $9.2 million, or 6.4%, during the year.

The record growth we have experienced has come, in large part, from our branch network. Our Waverly office continues to provide us with growth in both loans and deposits and our newer Wheelersburg location has gotten off to a great start, exceeding our expectations for growth of its customer base in a short period of time.

In 2007 and beyond, our focus is to remain committed to serving our local community with personalized service and the best financial products available. In that vein, we are in the process of purchasing the South Shore, Kentucky, branch of Peoples Bank, which gives us access to a larger market area. This expansion into Kentucky allows us to better serve our existing customer base there and to expand our presence, giving our bank an opportunity to offer our products and services to individuals and businesses in Greenup and Lewis Counties in Kentucky.

Your Corporation remains committed to the enhancement of shareholder value, as evidenced by our reverse stock split and resulting buy-back in July of 2005 which allowed us to terminate our registration with the SEC. Along with de-listing from NASDAQ, we estimate this transaction has saved us approximately $200,000 per year and in so doing, you the shareholder will realize the savings as enhanced returns on your investment.

We wish to thank you as always for your continued support and patronage and look forward to continuing growth and increasing returns to our shareholders in 2007 and beyond.

Very truly yours,

ASB FINANCIAL CORP.

Robert M. Smith
President and Chief Executive Officer

## BUSINESS OF ASB FINANCIAL CORP.

ASB Financial Corp. ("ASB" or the "Corporation"), a unitary savings and loan holding company incorporated under the laws of the State of Ohio, owns all of the issued and outstanding common shares of American Savings Bank, fsb ("American" or the "Savings Bank"), a federal savings bank. Other than investing excess funds, ASB's activities have been limited primarily to holding the common shares of American.

Serving the Portsmouth, Ohio, area since 1892, American conducts business from its main office at 503 Chillicothe Street in Portsmouth, Ohio, and branch offices at 951 West Emmitt Avenue in Waverly, Ohio, 7920 Ohio River Road in Wheelersburg, Ohio and 347 James Hannah Drive in South Shore, Kentucky. The principal business of American is the origination of loans secured by one- to four-family residential real estate located in American's primary market area, which consists of the contiguous areas of Scioto and Pike Counties in Ohio and Lewis and Greenup Counties in Kentucky. American also originates loans secured by multifamily residences (over four units) and nonresidential real estate and purchases interests in loans originated by other lenders secured by multifamily real estate and nonresidential real estate located outside of American's primary market area. In addition to real estate lending, American invests in mortgage-backed securities, U.S. Government and agency obligations and other investments. Funds for lending and other investment activities are obtained primarily from deposits, which are insured up to applicable limits by the Federal Deposit Insurance Corporation (the "FDIC"), and from borrowings from the Federal Home Loan Bank (the "FHLB") of Cincinnati.

ASB is subject to regulation, supervision and examination by the Office of Thrift Supervision of the United States Department of the Treasury (the "OTS"). American is subject to regulation, supervision and examination by the OTS and the FDIC. American is also a member of the FHLB of Cincinnati.

ASB's office is located at 503 Chillicothe Street, Portsmouth, Ohio 45662. The telephone number is (740) 354-3177.

## MARKET PRICE OF ASB'S COMMON SHARES AND RELATED SHAREHOLDER MATTERS

There were 1,591,766 common shares of ASB outstanding on September 1, 2006, held of record by approximately 195 shareholders. Price information for ASB's common shares is quoted on the Pink Sheets Market under the symbol "ASBN."

The table below sets forth the high and low closing prices for the common shares of ASB, together with dividends declared per share, for each quarter of fiscal years ended June 30, 2006 and 2005.

| Quarter ended | High close | Low close | Cash dividends declared |
|---|---|---|---|
| **Fiscal 2006** | | | |
| September 30, 2005 | $23.00 | $20.25 | $0.16 |
| December 31, 2005 | $20.50 | $20.25 | $0.16 |
| March 31, 2006 | $20.75 | $20.50 | $0.16 |
| June 30, 2006 | $20.75 | $20.50 | $0.17 |
| **Fiscal 2005** | | | |
| September 30, 2004 | $24.51 | $21.88 | $0.15 |
| December 31, 2004 | $22.98 | $20.50 | $0.15 |
| March 31, 2005 | $23.00 | $19.89 | $0.15 |
| June 30, 2005 | $23.00 | $21.90 | $0.16 |

The income of ASB on an unconsolidated basis consists of interest and dividends on investment and mortgage-backed and related securities and dividends which may periodically be paid on the common shares of American held by ASB. In addition to certain federal income tax considerations, OTS regulations impose limitations on the payment of dividends and other capital distributions by savings associations.

# SELECTED CONSOLIDATED FINANCIAL INFORMATION AND OTHER DATA

The following tables set forth certain information concerning the consolidated financial condition, earnings and other data regarding ASB at the dates and for the periods indicated.

| **Selected consolidated financial condition data:** | **2006** | **2005** | **At June 30, 2004** (In thousands) | **2003** | **2002** |
|---|---|---|---|---|---|
| Total amount of: | | | | | |
| Assets | $198,499 | $184,812 | $166,371 | $152,755 | $148,272 |
| Cash and cash equivalents | 3,425 | 11,792 | 7,385 | 7,610 | 7,704 |
| Certificates of deposit in other financial institutions | 200 | 72 | 178 | 173 | 100 |
| Investment securities available for sale - at market | 12,343 | 9,038 | 12,487 | 13,005 | 20,866 |
| Mortgage-backed securities available for sale - at market | 10,021 | 9,556 | 11,768 | 12,130 | 7,091 |
| Loans receivable - net | 163,056 | 146,134 | 129,821 | 114,919 | 109,015 |
| Deposits | 152,495 | 143,278 | 136,761 | 130,780 | 126,872 |
| Advances from the FHLB | 27,496 | 20,284 | 10,899 | 4,188 | 4,223 |
| Shareholders' equity, restricted | 16,916 | 19,195 | 17,424 | 16,359 | 14,454 |

| **Selected consolidated operating data:** | **2006** | **2005** | **Year ended June 30, 2004** (In thousands, except per share data) | **2003** | **2002** |
|---|---|---|---|---|---|
| Interest income | $10,997 | $9,590 | $8,954 | $9,576 | $9,543 |
| Interest expense | 5,342 | 3,497 | 3,051 | 3,888 | 5,050 |
| Net interest income | 5,655 | 6,093 | 5,903 | 5,688 | 4,493 |
| Provision for losses on loans | 269 | 313 | 111 | 249 | 70 |
| Net interest income after provision losses on loans | 5,386 | 5,780 | 5,792 | 5,439 | 4,423 |
| Other income | 1,046 | 1,357 | 705 | 745 | 486 |
| General, administrative and other expense | 4,325 | 4,096 | 3,743 | 3,277 | 3,077 |
| Earnings before income taxes and extraordinary item | 2,107 | 3,041 | 2,754 | 2,907 | 1,832 |
| Federal income taxes | 434 | 886 | 744 | 846 | 548 |
| Earnings before extraordinary item | 1,673 | 2,155 | 2,010 | 2,061 | 1,284 |
| Extraordinary item - negative goodwill arising from Waverly acquisition - net of tax | - | - | - | - | 229 |
| Net earnings | $ 1,673 | $2,155 | $2,010 | $2,061 | $1,513 |
| Earnings per share | | | | | |
| Basic | $1.05 | $1.27 | $1.22 | $1.32 | $1.00 |
| Diluted | $1.05 | $1.27 | $1.18 | $1.30 | $.97 |

| **Selected financial ratios:** | **Year ended June 30,** **2006** | **2005** | **2004** | **2003** | **2002** |
|---|---|---|---|---|---|
| Return on average assets | .88% | 1.23% | 1.26% | 1.36% | 1.06% |
| Average interest rate spread during period | 2.98 | 3.51 | 3.68 | 3.50 | 2.84 |
| Net interest margin | 3.12 | 3.66 | 3.84 | 3.81 | 3.23 |
| Return on average equity | 10.03 | 11.77 | 12.99 | 12.61 | 11.48 |
| Equity to total assets at end of period | 8.52 | 10.42 | 10.47 | 10.71 | 10.42 |
| Average interest-earning assets to average interest-bearing liabilities | 104.79 | 107.59 | 108.11 | 112.16 | 110.90 |
| Net interest income to general, administrative and other expense | 130.75 | 148.29 | 157.71 | 173.57 | 146.02 |
| General, administrative and other expense to average total assets | 2.27 | 2.34 | 2.35 | 2.16 | 2.16 |
| Nonperforming assets to total assets | .45 | .40 | .60 | .80 | .48 |
| Loan loss allowance to nonperforming loans | 149.33 | 170.79 | 99.90 | 82.77 | 120.93 |
| Dividend payout ratio | 61.90 | 47.56 | 46.72 | 115.91 | 49.00 |

# MANAGEMENT'S DISCUSSION AND ANALYSIS
# OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

## GENERAL

ASB was incorporated for the purpose of owning the outstanding common shares of American. As a result, the discussion and analysis that follows focuses primarily on the financial condition and results of operations of American. The following discussion and analysis of the consolidated financial condition and results of operations of ASB and American should be read in conjunction with, and with reference to, the Consolidated Financial Statements and the Notes thereto presented in this Annual Report.

### Forward-Looking Statements are Subject to Change

Certain statements contained in this report that are not historical facts are forward looking statements that are subject to certain risks and uncertainties. When used herein, the terms "anticipates," "plans," "expects," "believes," and similar expressions as they relate to ASB or its management are intended to identify such forward looking statements. ASB's actual results, performance or achievements may materially differ from those expressed or implied in the forward-looking statements. Risks and uncertainties that could cause or contribute to such material differences include, but are not limited to, general economic conditions, interest rate environment, competitive conditions in the financial services industry, changes in law, governmental policies and regulations, and rapidly changing technology affecting financial services.

### Critical Accounting Policies

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to use judgments in making estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. The following critical accounting policy is based upon judgments and assumptions by management that includes inherent risks and uncertainties.

The allowance for loan losses is an accounting estimate of probable but unconfirmed asset impairment that has occurred in the Corporation's loan portfolio as of the date of the consolidated financial statements before losses have been confirmed resulting in a subsequent charge-off or write-down. It is the Corporation's policy to provide valuation allowances for estimated losses on loans based upon past loss experience, adjusted for changes in trends and conditions of certain items, including:

- Local market areas and national economic developments;
- Levels of and trends in delinquencies and impaired loans;
- Levels of and trends in recoveries of prior charge-offs;
- Adverse situations that may affect specific borrowers' ability to repay;
- Effects of any changes in lending policies and procedures;
- Credit concentrations;
- Volume and terms of loans; and
- Current collateral values, where appropriate.

When the collection of a loan becomes doubtful, or otherwise troubled, the Corporation records a loan loss provision equal to the difference between the fair value of the property securing the loan and the loan's carrying value. Major loans and major lending areas are reviewed periodically to determine potential problems at an early date. The allowance for loan losses is increased by charges to earnings and decreased by charge-offs (net of recoveries).

The Corporation accounts for its allowance for loan losses in accordance with Statement of Financial Accounting Standards ("SFAS") No. 5, "Accounting for Contingencies," and SFAS No. 114, "Accounting by Creditors for Impairment of a Loan." Both Statements require the Corporation to evaluate the collectibility of both contractual interest and principal loan payments. SFAS No. 5 requires the accrual of a loss when it is probable that a loan has been impaired and the amount of the loss can be reasonably estimated. SFAS No. 114 requires that impaired loans be measured based upon the present value of expected future cash flows discounted at the loan's effective interest rate or, as an alternative, at the loans' observable market price or fair value of the collateral.

A loan is defined as impaired under SFAS No. 114 when, based on current information and events, it is probable that a creditor will be unable to collect all amounts due according to the contractual terms of the loan agreement. In applying the provisions of SFAS No. 114, the Corporation considers its investment in one- to four-family residential loans and consumer loans to be homogeneous and therefore excluded from separate identification for evaluation of impairment. These homogeneous loan groups are evaluated for impairment in accordance with SFAS No. 5. With respect to the Corporation's investment in nonresidential real estate and other loans, and its evaluation of impairment thereof, management believes such loans are adequately collateralized and as a result impaired loans are carried as a practical expedient at the lower of cost or fair value.

It is the Corporation's policy to charge off unsecured credits that are more than ninety days delinquent. Similarly, once a collateral dependent loan becomes more than ninety days delinquent, it is considered to constitute more than a minimum delay in repayment and is evaluated for impairment under SFAS No. 114 at that time.

## CHANGES IN FINANCIAL CONDITION FROM JUNE 30, 2005 TO JUNE 30, 2006

ASB's total assets amounted to $198.5 million at June 30, 2006, an increase of $13.7 million, or 7.4%, over 2005 levels. The increase in assets was comprised primarily of increases of $16.9 million in loans, $3.3 million in investment securities and $465,000 in mortgage backed securities, which were partially offset by a decrease of $8.4 million in cash and cash equivalents. The increase in assets was funded by increases in deposits of $9.2 million and advances from the Federal Home Loan Bank of $7.2 million.

Cash and interest-bearing deposits totaled $3.4 million at June 30, 2006, a decrease of $8.4 million, or 71.0%, from 2005 levels. Investment securities totaled $12.3 million at June 30, 2006, an increase of $3.3 million, or 36.6%, compared to the balance at June 30, 2005. Mortgage-backed securities totaled $10.0 million at June 30, 2006, an increase of $465,000, or 4.9%, year to year. During fiscal 2006, purchases of investment and mortgage-backed securities totaling $8.7 million were partially offset by maturities and principal repayments of securities totaling $4.3 million, and a decrease in the market value of investment and mortgage-backed securities totaling $550,000.

Loans receivable totaled $163.1 million at June 30, 2006, an increase of $16.9 million, or 11.6%, compared to June 30, 2005. Growth in loans secured by residential real estate, including construction loans, totaled $5.0 million, or 4.8%, growth in loans secured by nonresidential real estate totaled $10.2 million, or 41.8%, and the consumer loan portfolio grew by $1.2 million, or 25.2%, year to year.

At June 30, 2006, American's allowance for loan losses was $1.3 million, representing .82% of total loans and 149.3% of nonperforming loans. At June 30, 2005, American's allowance for loan losses was $1.3 million, representing .87% of total loans and 170.8% of nonperforming loans. Nonperforming loans totaled $896,000 and $743,000 at June 30, 2006 and 2005, respectively. At June 30, 2006, nonperforming loans were comprised of $410,000 of loans secured by one- to four-family residential real estate, $425,000 of commercial loans and $61,000 of consumer loans. The allowance for loan losses is determined as outlined in the aforementioned "Critical Accounting Policy." To the best of management's knowledge, all known losses as of June 30, 2006, have been recorded.

Deposits increased by $9.2 million, or 6.4%, to a total of $152.5 million at June 30, 2006. The increase in deposits consisted primarily of an increase of $11.7 million in certificates of deposit, which was partially offset by decreases of $307,000 in NOW accounts, $2.0 million in passbook accounts and $194,000 in money market deposit accounts. Growth in deposits was generally used to fund new loan originations.

Shareholders' equity totaled $16.9 million at June 30, 2006, a decrease of $2.3 million, or 11.9%, compared to June 30, 2005 levels. The decrease resulted primarily from dividends declared of $1.0 million, cash paid in lieu of fractional shares in the Corporation's reverse stock split of $2.7 million and a $363,000 decrease in net unrealized gains on available for sale securities, which were partially offset by net earnings of $1.7 million, proceeds from stock option exercises of $37,000, and the effects of $114,000 of amortization related to stock benefit plans. During fiscal 2006, the Corporation paid quarterly dividends totaling $.65 per share.

## COMPARISON OF OPERATING RESULTS FOR THE YEARS ENDED JUNE 30, 2006 AND 2005

**General.** Net earnings were $1.7 million for the fiscal year ended June 30, 2006, a decrease of $482,000, or 22.4%, from fiscal 2005. The decrease in earnings resulted primarily from decreases of $311,000 in other income and $438,000 in net interest income and an increase of $229,000 in general, administrative and other expense, which were partially offset by decreases of $44,000 in provision for losses on loans, and $452,000 in the provision for federal income taxes.

**Net Interest Income.** Total interest income was $11.0 million for the fiscal year ended June 30, 2006, an increase of $1.4 million, or 14.7%, from fiscal 2005. Interest income on loans totaled $10.0 million in fiscal 2006, an increase of $1.3 million, or 14.6%. This increase was due primarily to a 16 basis point increase in the average yield, to 6.41% for the fiscal year ended June 30, 2006 and a $16.4 million, or 11.8%, increase in the weighted-average balance of loans outstanding. Interest income on mortgage-backed securities decreased by $3,000, or .8%, as a result of a $1.2 million, or 11.3%, decrease in the weighted-average balance outstanding year to year, which was offset by a 43 basis point increase in the average yield. Interest income on investment securities and interest-bearing deposits increased by $136,000, or 28.8%, due primarily to a 98 basis point increase in the average yield, to 3.94%, which was partially offset by a $531,000, or 3.3%, decrease in the weighted average balance outstanding year to year.

Interest expense totaled $5.3 million for the fiscal year ended June 30, 2006, an increase of $1.8 million, or 52.8%, from the $3.5 million total recorded in fiscal 2005. Interest expense on deposits increased by $1.3 million, or 42.8%, due primarily to a 75 basis point increase in the weighted-average cost of deposits, to 2.91% for fiscal 2006 and an $8.4 million, or 6.0%, increase in the weighted-average balance outstanding year to year. Interest expense on borrowings increased by $556,000, or 113.9%, due primarily to a $9.2 million, or 60.7%, increase in the weighted-average balance outstanding year to year and a 106 basis point increase in the average cost of borrowings, to 4.27% in fiscal 2006. Increases in the average yields on interest-earning assets and the average costs of interest-bearing liabilities were due primarily to the overall increase in interest rates in the economy.

As a result of the foregoing changes in interest income and interest expense, net interest income decreased by $438,000, or 7.2%, to a total of $5.7 million for the fiscal year ended June 30, 2006, compared to $6.1 million in fiscal 2005. The interest rate spread decreased by 53 basis points to 2.98% in fiscal 2006 from 3.51% in fiscal 2005, and the net interest margin decreased by 54 basis points to 3.12% in fiscal 2006 from 3.66% in fiscal 2005.

**Provision for Losses on Loans.** American charges a provision for losses on loans to earnings to bring the total allowance for loan losses to a level considered appropriate by management based on historical experience, the volume and type of lending conducted by American, the status of past due principal and interest payments, general economic conditions, particularly as such conditions relate to American's market area, and other factors related to the collectibility of American's loan portfolio. As a result of such analysis, management recorded a $269,000 provision for losses on loans during the fiscal year ended June 30, 2006, a decrease of $44,000, or 14.1%, from fiscal 2005. The decrease in the provision in fiscal 2006 was based upon management's analysis of the loan portfolio including nonperforming assets, as outlined in the "Critical Accounting Policies." There can be no assurance that the loan loss allowance will be adequate to absorb losses on known nonperforming assets or that the allowance will be adequate to cover losses on nonperforming assets in the future.

**Other Income.** Other income totaled $1.0 million for the fiscal year ended June 30, 2006, a decrease of $311,000, or 22.9%, from the $1.4 million recorded in fiscal 2005. The decrease resulted primarily from a $537,000 reduction in gain on redemption of investment securities, which was partially offset by a $264,000 increase in other operating income. The increase in other operating income was comprised primarily of increases in fees on loans and deposits transactions and earnings from bank owned life insurance.

**General, Administrative and Other Expense.** General, administrative and other expense totaled $4.3 million for the fiscal year ended June 30, 2006, an increase of $229,000, or 5.6%, over the total recorded in fiscal 2005. The increase resulted primarily from increases of $39,000, or 1.7%, in employee compensation and benefits, $12,000, or 6.7%, in franchise taxes and $186,000, or 21.2%, in other operating expenses. The increases in compensation and other operating expenses were due primarily to the opening of a new branch office. The increase in franchise taxes was due primarily to growth in ASB's equity year to year.

**Federal Income Taxes.** The provision for federal income taxes totaled $434,000 for the fiscal year ended June 30, 2006, a decrease of $452,000, or 51.0%, from the $886,000 recorded in fiscal 2005. The decrease was due primarily to the $934,000, or 30.7%, decrease in pre-tax earnings and the effect of available tax credits. ASB's effective tax rates were 20.6% and 29.1% for the fiscal years ended June 30, 2006 and 2005, respectively.

## AVERAGE BALANCE, YIELD, RATE AND VOLUME DATA

The following table sets forth certain information relating to ASB's average balance sheet and reflects the average yield on interest-earning assets and the average cost of interest-bearing liabilities for the periods indicated. Such yields and costs are derived by dividing income or expense by the average monthly balance of interest-earning assets or interest-bearing liabilities, respectively, for the periods presented. Average balances are derived from average monthly balances, which include nonaccruing loans in the loan portfolio, net of the allowance for loan losses.

| | Year ended June 30, | | | | | |
|---|---|---|---|---|---|---|
| | 2006 | | | 2005 | | |
| | Average outstanding balance | Interest earned/ paid | Yield/ rate | Average outstanding balance | Interest earned/ paid | Yield/ rate |
| | (Dollars in thousands) | | | | | |
| Interest-earning assets: | | | | | | |
| Loans receivable | $155,864 | $ 9,990 | 6.41% | $139,432 | $8,716 | 6.25% |
| Mortgage-backed securities | 9,702 | 399 | 4.11 | 10,937 | 402 | 3.68 |
| Investment securities and other interest-earning assets | 15,431 | 608 | 3.94 | 15,962 | 472 | 2.96 |
| Total interest-earning assets | 180,997 | 10,997 | 6.08 | 166,331 | 9,590 | 5.77 |
| Non-interest-earning assets | 9,640 | | | 8,517 | | |
| Total assets | $190,637 | | | $174,848 | | |
| Interest-bearing liabilities: | | | | | | |
| Deposits | $147,752 | 4,298 | 2.91 | $139,367 | 3,009 | 2.16 |
| Borrowings | 24,461 | 1,044 | 4.27 | 15,224 | 488 | 3.21 |
| Total interest-bearing liabilities | 172,213 | 5,342 | 3.10 | 154,591 | 3,497 | 2.26 |
| Non-interest-bearing liabilities | 1,738 | | | 2,094 | | |
| Total liabilities | 173,951 | | | 156,685 | | |
| Shareholders' equity | 16,686 | | | 18,163 | | |
| Total liabilities and shareholders' equity | $190,637 | | | $174,848 | | |
| Net interest income | | $ 5,655 | | | $6,093 | |
| Interest rate spread | | | 2.98% | | | 3.51% |
| Net interest margin (net interest income as a percent of average interest-earning assets) | | | 3.12% | | | 3.66% |
| Average interest-earning assets to average interest-bearing liabilities | | | 104.79% | | | 107.59% |

The table below describes the extent to which changes in interest rates and changes in volume of interest-earning assets and interest-bearing liabilities have affected ASB's interest income and expense during the years indicated. For each category of interest-earning assets and interest-bearing liabilities, information is provided on changes attributable to (i) changes in volume (change in volume multiplied by prior year rate), (ii) changes in rate (change in rate multiplied by prior year volume) and (iii) total changes in rate and volume. The combined effects of changes in both volume and rate, which cannot be separately identified, have been allocated proportionately to the change due to volume and the change due to rate.

| | Year ended June 30, 2006 vs. 2005 | | |
|---|---|---|---|
| | Increase (decrease) due to | | |
| | Volume | Rate | Total |
| | | (In thousands) | |
| Interest-earnings assets: | | | |
| Loans receivable | $1,047 | $ 227 | $1,274 |
| Mortgage-backed securities | (47) | 44 | (3) |
| Investment securities and interest-bearing assets | (16) | 152 | 136 |
| Total interest-earnings assets | 984 | 423 | 1,407 |
| Interest-bearing liabilities: | | | |
| Deposits | 190 | 1,099 | 1,289 |
| Borrowings | 361 | 195 | 556 |
| Total interest-bearing liabilities | 551 | 1,294 | 1,845 |
| Increase (decrease) in net interest income | $ 433 | $ (871) | $ (438) |

## ASSET AND LIABILITY MANAGEMENT

American, like other financial institutions, is subject to interest rate risk to the extent that its interest-earning assets reprice differently than its interest-bearing liabilities. As a part of its effort to monitor its interest rate risk, American reviews the reports of the OTS which set forth the application of the "net portfolio value" ("NPV") methodology used by the OTS.

Generally, NPV is the discounted present value of the difference between incoming cash flows on interest-earning and other assets and outgoing cash flows on interest-bearing liabilities. The methodology attempts to quantify interest rate risk as the change in the NPV which would result from theoretical changes in market interest rates.

The following table presents, at June 30, 2006 and 2005, an analysis of the interest rate risk of American, as measured by changes in NPV for instantaneous and sustained parallel shifts of 100 basis point movements in market interest rates. Decreases of greater than 200 basis points are not presented at June 30, 2005, due to the low interest rate environment in existence at that date.

| | | At June 30, 2006 | | At June 30, 2005 | |
|---|---|---|---|---|---|
| **Changes in interest rate (basis points)** | **Board limit % changes** | **NPV as a % of PV of Assets Ratio** | **Change in NPV** | **NPV as a % of PV of Assets Ratio** | **Change in NPV** |
| +300 | (6)% | 6.23% | (400)bp | 8.01% | (275)bp |
| +200 | (6) | 7.63 | (260) | 9.17 | (159) |
| +100 | (6) | 8.99 | (125) | 10.17 | (59) |
| - | - | 10.23 | - | 10.76 | - |
| -100 | 6 | 11.12 | 88 | 10.69 | (7) |
| -200 | 6 | 11.39 | 115 | - | - |

The model reflects that American's NPV is more sensitive to an increase in interest rates than a decrease in interest rates. This occurs principally because, as rates rise, the market values of the Savings Bank's investments, adjustable-rate mortgage loans, fixed-rate loans and mortgage-backed securities decline due to the rate increases. The values of the Savings Bank's deposits and borrowings change in approximately the same proportion in rising or falling rate scenarios.

If interest rates rise from current levels, American's net interest income could be negatively affected. Moreover, rising interest rates could negatively affect American's earnings due to diminished loan demand.

As with any method of measuring interest rate risk, certain shortcomings are inherent in the method of analysis presented in the foregoing table. For example, although certain assets and liabilities may have similar maturities or periods of repricing, they do not all reprice simultaneously and they may react in different degrees to changes in market interest rates. Also, the interest rates on certain types of assets and liabilities may fluctuate in advance of changes in market interest rates, while interest rates on other types may lag behind such changes. Additionally, certain assets, such as adjustable-rate loans, have features that restrict changes in interest rates on a short-term basis and over the life of the assets. Further, in the event of a change in interest rates, expected rates of prepayment on loans and early withdrawal from certificates could deviate significantly from those assumed in calculating the table.

## LIQUIDITY AND CAPITAL RESOURCES

Liquidity refers to the ability of an institution to generate sufficient cash to fund current loan demand, meet deposit withdrawals and pay operating expenses. Liquidity is influenced by financial market conditions, fluctuations in interest rates, general economic conditions and regulatory requirements. ASB's liquidity, primarily represented by cash and cash equivalents and investment securities available for sale, is a result of the operating, investing and financing activities of American. These activities are summarized below on a consolidated basis for the fiscal years ended June 30, 2006 and 2005:

| | Year ended June 30, 2006 | 2005 |
|---|---|---|
| Net cash from operating activities | $ 1,157 | $ 2,496 |
| Net cash from investing activities | (22,262) | (13,185) |
| Net cash from financing activities | 12,738 | 15,096 |
| Net change in cash and cash equivalents | (8,367) | 4,407 |
| Cash and cash equivalents at the beginning of the year | 11,792 | 7,385 |
| Cash and cash equivalents at the end of the year | $ 3,425 | $11,792 |

The following table sets forth information regarding the Bank's obligations and commitments to make future payments under contract as of June 30, 2006, at market rates:

| | Payments due by period | | | | |
|---|---|---|---|---|---|
| | Less than 1 year | 1-3 years | 3-5 years | More than 5 years | Total |
| | (In thousands) | | | | |
| Contractual obligations: | | | | | |
| Advances from the Federal Home Loan Bank | $ 7,828 | $10,206 | $ 4,628 | $4,834 | $ 27,496 |
| Certificates of deposit | 73,192 | 25,203 | 5,337 | - | 103,732 |
| | 81,020 | 35,409 | 9,965 | 4,834 | 131,228 |
| Amount of commitments expiration per period | | | | | |
| Commitments to originate mortgage loans: | | | | | |
| One- to four-family loans | 649 | - | - | - | 649 |
| Home equity lines of credit | 457 | 1,042 | 500 | 555 | 2,554 |
| Commercial lines of credit | 3,143 | - | - | - | 3,143 |
| Commercial letters of credit | 574 | - | - | - | 574 |
| Total contractual obligations | $85,843 | $36,451 | $10,465 | $5,389 | $138,148 |

It is management's belief that there are no known trends, known demands, commitments or events that are likely to result in a material change in the Corporation's liquidity position.

American is required by OTS regulations to maintain specified minimum amounts of capital. The following table sets forth the amount and percentage level of American's regulatory capital at June 30, 2006, and the minimum requirement amounts. Tangible and core capital are reflected as a percentage of adjusted total assets. Risk-based (or total) capital, which consists of core and supplementary capital, is reflected as a percentage of risk-weighted assets. At June 30, 2006, American met the definition of a "well capitalized" institution under OTS regulations.

| | June 30, 2006 | | | | | |
|---|---|---|---|---|---|---|
| | Regulatory capital | | Current requirement | | Excess of regulatory capital over current requirement | |
| | Amount | Percent | Amount | Percent | Amount | Percent |
| | (Dollars in thousands) | | | | | |
| Tangible capital | $16,717 | 8.4% | $ 2,994 | 1.5% | $13,723 | 6.9% |
| Core capital | $16,717 | 8.4% | $ 7,984 | 4.0% | $ 8,733 | 4.4% |
| Risk-based capital | $18,276 | 14.5% | $10,078 | 8.0% | $ 8,198 | 6.5% |

# REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Directors
ASB Financial Corp.

We have audited the accompanying consolidated statements of financial condition of ASB Financial Corp. as of June 30, 2006 and 2005, and the related consolidated statements of earnings, comprehensive income, shareholders' equity and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America as established by the Auditing Standards Board of the American Institute of Certified Public Accountants. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Corporation's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of ASB Financial Corp. as of June 30, 2006 and 2005, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Grant Thornton LLP

Cincinnati, Ohio
September 1, 2006

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## ASB FINANCIAL CORP.

## CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

**June 30, 2006 and 2005**
(In thousands, except share data)

| **ASSETS** | **2006** | **2005** |
|---|---|---|
| Cash and due from banks | $ 662 | $ 1,505 |
| Interest-bearing deposits in other financial institutions | 2,763 | 10,287 |
| Cash and cash equivalents | 3,425 | 11,792 |
| Certificates of deposit in other financial institutions | 200 | 72 |
| Investment securities available for sale - at market | 12,343 | 9,038 |
| Mortgage-backed securities available for sale - at market | 10,021 | 9,556 |
| Loans receivable - net of loan loss allowance of $1,338 and $1,269 at June 30, 2006 and 2005, respectively | 163,056 | 146,134 |
| Office premises and equipment - at depreciated cost | 2,646 | 2,160 |
| Federal Home Loan Bank stock - at cost | 1,219 | 1,154 |
| Accrued interest receivable on loans | 626 | 501 |
| Accrued interest receivable on mortgage-backed securities | 45 | 38 |
| Accrued interest receivable on investments and interest-bearing deposits | 90 | 69 |
| Prepaid expenses and other assets | 306 | 274 |
| Bank owned life insurance | 3,362 | 3,240 |
| Prepaid federal income taxes | 174 | - |
| Deferred federal income taxes | 986 | 784 |
| Total assets | **$198,499** | **$184,812** |
| **LIABILITIES AND SHAREHOLDERS' EQUITY** | | |
| Deposits | $152,495 | $143,278 |
| Advances from the Federal Home Loan Bank | 27,496 | 20,284 |
| Advances by borrowers for taxes and insurance | 208 | 193 |
| Accrued interest payable | 155 | 81 |
| Accrued federal income taxes | - | 580 |
| Other liabilities | 1,229 | 1,201 |
| Total liabilities | 181,583 | 165,617 |
| Commitments | - | - |
| Shareholders' equity | | |
| Preferred stock, 1,000,000 shares authorized, no par value; no shares issued | - | - |
| Common stock, 4,000,000 shares authorized, no par value; 1,848,004 and 1,963,158 shares issued at June 30, 2006 and 2005, respectively | - | - |
| Additional paid-in capital | 8,205 | 10,823 |
| Retained earnings, restricted | 11,617 | 10,978 |
| Shares acquired by stock benefit plan | - | (63) |
| Accumulated comprehensive income, unrealized gains on securities designated as available for sale, net of related tax effects | 179 | 542 |
| Less 256,980 shares of treasury stock - at cost | (3,085) | (3,085) |
| Total shareholders' equity | 16,916 | 19,195 |
| Total liabilities and shareholders' equity | **$198,499** | **$184,812** |

The accompanying notes are an integral part of these statements.

## ASB FINANCIAL CORP.

## CONSOLIDATED STATEMENTS OF EARNINGS

**For the years ended June 30, 2006, and 2005**
(In thousands, except per share data)

| | 2006 | 2005 |
|---|---|---|
| Interest income | | |
| Loans | $ 9,990 | $8,716 |
| Mortgage-backed securities | 399 | 402 |
| Investment securities | 470 | 403 |
| Interest-bearing deposits and other | 138 | 69 |
| Total interest income | 10,997 | 9,590 |
| Interest expense | | |
| Deposits | 4,298 | 3,009 |
| Borrowings | 1,044 | 488 |
| Total interest expense | 5,342 | 3,497 |
| Net interest income | 5,655 | 6,093 |
| Provision for losses on loans | 269 | 313 |
| Net interest income after provision for losses on loans | 5,386 | 5,780 |
| Other income (expense) | | |
| Gain on redemption of investment securities | 53 | 590 |
| Loss on sale of real estate acquired through foreclosure | (38) | - |
| Other operating | 1,031 | 767 |
| Total other income | 1,046 | 1,357 |
| General, administrative and other expense | | |
| Employee compensation and benefits | 2,358 | 2,319 |
| Occupancy and equipment | 255 | 262 |
| Franchise taxes | 190 | 178 |
| Data processing | 460 | 461 |
| Other operating | 1,062 | 876 |
| Total general, administrative and other expense | 4,325 | 4,096 |
| Earnings before income taxes | 2,107 | 3,041 |
| Federal income taxes | | |
| Current | 451 | 1,470 |
| Deferred | (17) | (584) |
| Total federal income taxes | 434 | 886 |
| **NET EARNINGS** | **$ 1,673** | **$2,155** |
| **EARNINGS PER SHARE** | | |
| Basic | **$1.05** | **$1.27** |
| Diluted | **$1.05** | **$1.27** |

The accompanying notes are an integral part of these statements.

## ASB FINANCIAL CORP.

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

**For the years ended June 30, 2006 and 2005**
(In thousands)

| | 2006 | 2005 |
|---|---|---|
| Net earnings | $1,673 | $2,155 |
| Other comprehensive income, net of tax: | | |
| Unrealized holding gains (losses) on securities during the year, net of taxes (benefits) of $(187) and $85 in 2006 and 2005, respectively | (363) | 165 |
| Comprehensive income | **$1,310** | **$2,320** |
| Accumulated comprehensive income | **$ 179** | **$ 542** |

The accompanying notes are an integral part of these statements.

## ASB FINANCIAL CORP.

## CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

**For the years ended June 30, 2006 and 2005**
(In thousands, except share data)

| | Common stock | Additional paid-in capital | Retained earnings | Shares acquired by stock benefit plans | Unrealized gains (losses) on securities designated as available for sale | Treasury stock | Total |
|---|---|---|---|---|---|---|---|
| Balance at July 1, 2004 | $ - | $10,165 | $ 9,848 | $(126) | $377 | $(2,840) | $17,424 |
| Amortization of expense related to stock benefit plan | - | 57 | - | 63 | - | - | 120 |
| Net earnings for the year ended June 30, 2005 | - | - | 2,155 | - | - | - | 2,155 |
| Cash dividends of $.61 per share | - | - | (1,025) | - | - | - | (1,025) |
| Purchase of treasury shares - at cost | - | - | - | - | - | (245) | (245) |
| Issuance of shares under stock option plan | - | 601 | - | - | - | - | 601 |
| Unrealized gains on securities designated as available for sale, net of related tax effects | - | - | - | - | 165 | - | 165 |
| Balance at June 30, 2005 | - | 10,823 | 10,978 | (63) | 542 | (3,085) | 19,195 |
| Amortization of expense related to stock benefit plan | - | 51 | - | 63 | - | - | 114 |
| Net earnings for the year ended June 30, 2006 | - | - | 1,673 | - | - | - | 1,673 |
| Cash dividends of $.65 per share | - | - | (1,034) | - | - | - | (1,034) |
| Cash paid for fractional shares in reverse stock split | - | (2,706) | - | - | - | - | (2,706) |
| Issuance of shares under stock option plan | - | 37 | - | - | - | - | 37 |
| Unrealized losses on securities designated as available for sale, net of related tax effects | - | - | - | - | (363) | - | (363) |
| Balance at June 30, 2006 | $ - | $ 8,205 | $11,617 | $ - | $179 | $(3,085) | $16,916 |

The accompanying notes are an integral part of these statements.

**ASB FINANCIAL CORP.**

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

**For the years ended June 30, 2006 and 2005**
(In thousands)

| | **2006** | **2005** |
|---|---|---|
| Cash flows from operating activities: | | |
| Net earnings for the year | $ 1,673 | $ 2,155 |
| Adjustments to reconcile net earnings to net cash from operating activities: | | |
| Amortization of discounts and premiums on loans, investments and mortgage-backed securities - net | (67) | 40 |
| Amortization of deferred loan origination fees | (60) | (57) |
| Amortization of expense related to stock benefit plans | 114 | 120 |
| Depreciation and amortization | 159 | 166 |
| Provision for losses on loans | 269 | 313 |
| Gain on redemption of investment securities | (53) | (590) |
| Federal Home Loan Bank stock dividends | (65) | (50) |
| Loss on sale of real estate acquired through foreclosure | 38 | - |
| Increase (decrease) in cash due to changes in: | | |
| Accrued interest receivable on loans | (125) | (165) |
| Accrued interest receivable on mortgage-backed securities | (7) | 12 |
| Accrued interest receivable on investments and interest-bearing deposits | (21) | 61 |
| Prepaid expenses and other assets | (32) | (13) |
| Accrued interest payable | 74 | 29 |
| Other liabilities | 28 | 146 |
| Tax benefit from exercise of stock options | 3 | 150 |
| Federal income taxes | | |
| Current | (754) | 763 |
| Deferred | (17) | (584) |
| Net cash provided by operating activities | 1,157 | 2,496 |
| Cash flows from investing activities: | | |
| Proceeds from maturity of investment securities | 1,300 | 5,801 |
| Proceeds from redemption of investment security | 53 | 722 |
| Purchase of investment securities | (4,929) | (2,304) |
| Purchase of mortgage-backed securities | (3,791) | (1,349) |
| Principal repayments on mortgage-backed securities | 3,025 | 3,579 |
| Loan principal repayments | 24,641 | 32,008 |
| Loan disbursements | (41,666) | (48,433) |
| Purchase of office premises and equipment | (645) | (512) |
| (Increase) decrease in certificates of deposit in other financial institutions - net | (128) | 106 |
| Increase in cash surrender value of bank owned life insurance | (122) | (103) |
| Purchase of bank owned life insurance | - | (2,700) |
| Net cash used in investing activities | (22,262) | (13,185) |
| Net cash used in operating and investing activities (subtotal carried forward) | (21,105) | (10,689) |

## ASB FINANCIAL CORP.

## CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)

**For the years ended June 30, 2006 and 2005**
(In thousands)

| | 2006 | 2005 |
|---|---|---|
| Net cash used in operating and investing activities (subtotal brought forward) | $(21,105) | $(10,689) |
| Cash flows from financing activities: | | |
| Net increase in deposit accounts | 9,217 | 6,517 |
| Proceeds from Federal Home Loan Bank advances | 27,650 | 24,973 |
| Repayment of Federal Home Loan Bank advances | (20,438) | (15,588) |
| Advances by borrowers for taxes and insurance | 15 | 13 |
| Proceeds from issuance of shares under stock option plan | 34 | 451 |
| Purchase of treasury stock | - | (245) |
| Cash paid for fractional shares in reverse stock split | (2,706) | - |
| Dividends paid on common stock | (1,034) | (1,025) |
| Net cash provided by financing activities | 12,738 | 15,096 |
| Net increase (decrease) in cash and cash equivalents | (8,367) | 4,407 |
| Cash and cash equivalents at beginning of year | 11,792 | 7,385 |
| Cash and cash equivalents at end of year | $ 3,425 | $ 11,792 |
| Supplemental disclosure of cash flow information: | | |
| Cash paid during the year for: | | |
| Federal income taxes | $ 1,187 | $ 603 |
| Interest on deposits and borrowings | $ 5,268 | $ 3,468 |
| Supplemental disclosure of noncash investing activities: | | |
| Unrealized gains (losses) on securities designated as available for sale, net of related tax effects | $ (363) | $ 165 |
| Transfers from loans to real estate acquired through foreclosure | $ 68 | $ - |
| Loans disbursed upon sale of real estate acquired through foreclosure | $ 30 | $ - |
| Dividends payable | $ 271 | $ 254 |

The accompanying notes are an integral part of these statements.

## NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

ASB Financial Corp. (the "Corporation") is a savings and loan holding company whose primary activity is holding the stock of its wholly-owned subsidiary, American Savings Bank, fsb (the "Savings Bank"). The Savings Bank conducts a general banking business in southeastern Ohio which consists of attracting deposits from the general public and primarily applying those funds to the origination of loans for residential, consumer and nonresidential purposes. The Savings Bank's profitability is significantly dependent on net interest income, which is the difference between interest income generated from interest-earning assets (i.e. loans and investments) and the interest expense paid on interest-bearing liabilities (i.e. customer deposits and borrowed funds). Net interest income is affected by the relative amounts of interest-earning assets and interest-bearing liabilities and the interest received or paid on these balances. The level of interest rates paid or received by the Savings Bank can be significantly influenced by a number of factors that are outside of management's control, such as governmental monetary policy.

The consolidated financial information presented herein has been prepared in accordance with accounting principles generally accepted in the United States of America ("U. S. GAAP") and general accounting practices within the financial services industry. In preparing consolidated financial statements in accordance with U. S. GAAP, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and revenues and expenses during the reporting period. Actual results could differ from such estimates.

The following is a summary of the Corporation's significant accounting policies which have been consistently applied in the preparation of the accompanying consolidated financial statements.

### Principles of Consolidation

The consolidated financial statements include the accounts of the Corporation, the Savings Bank, ASB Community Development Corporation and A.S.L. Services, Inc., the Savings Bank's wholly-owned subsidiaries. ASB Community Development Corporation was formed in fiscal 2003 for the purpose of participating in a federal program designed to promote lending in new markets, which in turn provides federal income tax credits to the Savings Bank. All significant intercompany balances and transactions have been eliminated.

### Investment Securities and Mortgage-Backed Securities

The Corporation accounts for investment and mortgage-backed securities in accordance with Statement of Financial Accounting Standards ("SFAS") No. 115 "Accounting for Certain Investments in Debt and Equity Securities." SFAS No. 115 requires that investments in debt and equity securities be categorized as held-to-maturity, trading, or available for sale. Securities classified as held-to-maturity are carried at cost only if the Corporation has the positive intent and ability to hold these securities to maturity. Trading securities and securities designated as available for sale are carried at fair value with resulting unrealized gains or losses recorded to operations or shareholders' equity, respectively.

## NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### Investment Securities and Mortgage-Backed Securities (continued)

At June 30, 2006 and 2005, the Corporation had designated all investment and mortgage-backed securities as available for sale.

Realized gains and losses on sales of securities are recognized using the specific identification method.

### Loans Receivable

Loans receivable are stated at the principal amount outstanding, adjusted for deferred loan origination fees and the allowance for loan losses. Interest is accrued as earned unless the collectibility of the loan is in doubt. Interest on loans that are contractually past due is charged off, or an allowance is established based on management's periodic evaluation. The allowance is established by a charge to interest income equal to all interest previously accrued, and income is subsequently recognized only to the extent that cash payments are received until, in management's judgment, the borrower's ability to make periodic interest and principal payments has returned to normal, in which case the loan is returned to accrual status. If the ultimate collectibility of the loan is in doubt, in whole or in part, all payments received on nonaccrual loans are applied to reduce principal until such doubt is eliminated.

### Loan Origination Fees

The Savings Bank accounts for loan origination fees in accordance with SFAS No. 91 "Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Cost of Leases." Pursuant to the provisions of SFAS No. 91, origination fees received from loans, net of direct origination costs, are deferred and amortized to interest income using the level-yield method, giving effect to actual loan prepayments. Additionally, SFAS No. 91 generally limits the definition of loan origination costs to the direct costs of originating a loan, i.e., principally actual personnel costs. Fees received for loan commitments that are expected to be drawn upon, based on the Savings Bank's experience with similar commitments, are deferred and amortized over the life of the loan using the level-yield method. Fees for other loan commitments are deferred and amortized over the loan commitment period on a straight-line basis.

### Allowance for Loan Losses

It is the Savings Bank's policy to provide valuation allowances for estimated losses on loans based on past loss experience, trends in the level of delinquent and problem loans, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral and current and anticipated economic conditions in the Savings Bank's primary lending area. When the collection of a loan becomes doubtful or otherwise troubled, the Savings Bank records a loan charge-off equal to the difference between the fair value of the property securing the loan and the loan's carrying value. Major loans (including development projects) and major lending areas are reviewed periodically to determine potential problems at an early date. The allowance for loan losses is increased by charges to earnings and decreased by charge-offs (net of recoveries).