GERMAN AMERICAN BANCORP, INC.
Form 10-K
March 09, 2007

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended: December 31, 2006

OR

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from __________ to __________

Commission File Number 0-11244

GERMAN AMERICAN BANCORP, INC.
(Exact name of registrant as specified in its charter)

INDIANA	35-1547518
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
711 Main Street, Box 810, Jasper, Indiana	47546
(Address of Principal Executive Offices)	(Zip Code)

Registrant's telephone number, including area code: (812) 482-1314

Securities registered pursuant to Section 12 (b) of the Act: None
Securities registered pursuant to Section 12 (g) of the Act:
Common Shares, No Par Value Preferred Stock Purchase Rights
(Titles of Classes)

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 if disclosure of delinquent filers pursuant to Item 405 Regulation S-K 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 or a non-accelerated filer:

Large accelerated filer o Accelerated filer x Non-accelerated filer o

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

The aggregate market value of the registrant's common shares held by non-affiliates of the registrant, computed by reference to the price at which the common shares were last sold, as of June 30, 2006 (the last business day of the registrant's most recently completed second fiscal quarter) was approximately $132,632,000. This calculation does not reflect a determination that persons are affiliates for any other purposes.

As of March 1, 2007, there were outstanding 11,029,612 common shares, no par value, of the registrant.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement of German American Bancorp, Inc., for the Annual Meeting of its Shareholders to be held April 26, 2007, to the extent stated herein, are incorporated by reference into Part III.

GERMAN AMERICAN BANCORP, INC.
ANNUAL REPORT ON FORM 10-K
For Fiscal Year Ended December 31, 2006

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Information included in or incorporated by reference in this Annual Report on Form 10-K, our other filings with the Securities and Exchange Commission and our press releases or other public statements, contain or may contain "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Please refer to a discussion of our forward- looking statements and associated risks in Item 1, "Business - Forward-Looking Statements and Associated Risks" and our discussion of risk factors in Item 1A, "Risk Factors" in this Annual Report on Form 10-K.

PART I

Item 1. Business.

General.

German American Bancorp, Inc. is a financial services holding company based in Jasper, Indiana. The Company's Common Stock is traded on NASDAQ's Global Select Market. under the symbol GABC. The principal subsidiary of German American Bancorp, Inc., is its banking subsidiary, German American Bancorp which operates through six community banking affiliates with 30 retail banking offices in the ten contiguous Southern Indiana counties of Daviess, Dubois, Gibson, Knox, Lawrence, Martin, Monroe, Perry, Pike, and Spencer. German American Bancorp, Inc., also owns a trust, brokerage, and financial planning subsidiary, which operates from the banking offices of the bank subsidiary and two insurance agencies with six insurance agency offices throughout its market area.

Throughout this report, when we use the term "Company", we will usually be referring to the business and affairs (financial and otherwise) of the Company and its subsidiaries and affiliates as a whole. Occasionally, we will refer to the term "parent company" or "holding company" when we mean to refer to only German American Bancorp, Inc.

The Company's lines of business include retail and commercial banking, mortgage banking, comprehensive financial planning, full service brokerage and trust administration, title insurance, and a full range of personal and corporate insurance products. Financial and other information by segment is included in Note 16 - Segment Information of the Notes to the Consolidated Financial Statements included in Item 8 of this Report and is incorporated into this Item 1 by reference. Substantially all of the Company's revenues are derived from customers located in, and substantially all of its assets are located in, the United States.

Developments in the Company's Business

Since January 1, 2006, the Company's business has grown through both organic internal growth and acquisitions. Effective January 1, 2006, the Company completed its acquisition of Stone City Bancshares, Inc. and its subsidiary Stone City Bank of Bedford, Indiana, and effective October 1, 2006, the Company completed the acquisition of the insurance agency business of Keach and Grove Insurance, Inc. also of Bedford, Indiana. For a description of these acquisitions, see Note 18 to the consolidated financial statements included in Item 8 of this Report, which description is incorporated into this Item 1 by reference. During the first quarter of 2007, the Company established its first branch in Bloomington, Indiana, which is located in Monroe County, Indiana (immediately north of Lawrence County, in which Bedford is located). As a result of this acquisition and branching activity, the Company now operates in both the Bloomington (Monroe County) and Bedford (Lawrence County) banking markets.

In addition, during the second quarter of 2006, the Company purchased a non-controlling investment in the common stock of a small banking company based in Dana, Indiana (near Terre Haute, Indiana) that has since branched into Lafayette, Indiana. As a result of making this investment, the Company has the opportunity to bid to purchase participations in loans that may be originated by this other banking company from time to time, if and to the extent that the banking company desires to sell participations in such loans to third parties. During the fourth quarter of 2006, the Company expanded its agricultural lending business by acquiring the Southern Indiana based agricultural loan

portfolio of a regional banking company.

Subsidiaries

The Company's principal operating subsidiaries are described in the following table:

1) Name	2) Type of Business	3) Principal Office Location
German American Bancorp	Commercial Bank	Jasper, IN
First Title Insurance Company	Title Insurance Agency	Vincennes, IN
German American Insurance, Inc.	Multi-Line Insurance Agency	Petersburg, IN
German American Financial Advisors & Trust Company	Trust, Brokerage, Financial Planning	Jasper, IN

Two of these subsidiaries (German American Bancorp and German American Insurance, Inc.) do business in the various communities served by the Company under distinctive trade names that relate to the names under which the Company (or a predecessor) has done banking and insurance business with the public in those communities in prior years.

Competition.

The industries in which the Company operates are highly competitive. The Company's subsidiary bank competes for commercial and retail banking business within its core banking segment not only with financial institutions that have offices in the same counties but also with financial institutions that compete from other locations in Southern Indiana and elsewhere. The Company's subsidiaries compete with commercial banks, savings and loan associations, savings banks, credit unions, production credit associations, federal land banks, finance companies, credit card companies, personal loan companies, investment brokerage firms, insurance agencies, insurance companies, lease finance companies, money market funds, mortgage companies, and other non-depository financial intermediaries. Many of these banks and other organizations have substantially greater resources than the Company.

Employees.

At March 1, 2007 the Company and its subsidiaries employed approximately 395 full-time equivalent employees. There are no collective bargaining agreements, and employee relations are considered to be good.

Regulation and Supervision.

The Company is subject to regulation and supervision by the Board of Governors of the Federal Reserve System ("FRB") under the Bank Holding Company Act of 1956, as amended ("BHC Act"), and is required to file with the FRB annual reports and such additional information as the FRB may require. The FRB may also make examinations or inspections of the Company. Under FRB policy, the Company is expected to act as a source of financial strength to its bank subsidiary and to commit resources to support that subsidiary even in circumstances where the Company might not do so absent such an FRB policy.

The Company's subsidiary bank is under the supervision of and subject to examination by the Indiana Department of Financial Institutions ("DFI"), and the Federal Deposit Insurance Corporation ("FDIC"). Regulation and examination by banking regulatory agencies are primarily for the benefit of depositors rather than shareholders.

With certain exceptions, the BHC Act prohibits a bank holding company from engaging in (or acquiring direct or indirect control of more than 5 percent of the voting shares of any company engaged in) nonbanking activities. One of the principal exceptions to this prohibition is for activities deemed by the FRB to be "closely related to banking." Under current regulations, bank holding companies and their subsidiaries are permitted to engage in such banking-related business ventures as consumer finance; equipment leasing; credit life insurance; computer service bureau and software operations; mortgage banking; and securities brokerage.

Under the BHC Act, certain well-managed and well-capitalized bank holding companies may elect to be treated as a "financial holding company" and, as a result, be permitted to engage in a broader range of activities that are "financial in nature" and in activities that are determined to be incidental or complementary to activities that are financial in nature. These activities include underwriting, dealing in and making a market in securities; insurance underwriting and agency activities; and merchant banking. Banks may also engage through financial subsidiaries in certain of the activities permitted for financial holding companies, subject to certain conditions. The Company has not elected to become a financial holding company and its subsidiary bank has not elected to form financial subsidiaries.

The Company's bank subsidiary and that bank's subsidiaries may generally engage in activities that are permissible activities for state chartered banks under Indiana banking law, without regard to the limitations that might apply to such activities under the BHC Act if the Company were to engage directly in such activities at the parent company level or through parent company subsidiaries that were not also bank subsidiaries.

Indiana law and the BHC Act restrict certain types of expansion by the Company and its bank subsidiary. The Company and its subsidiaries may be required to apply for prior approval from (or give prior notice and an opportunity for review to) the FRB, the DFI, and/or other bank regulatory or other regulatory agencies, as a condition to the acquisition or establishment of new offices, or the acquisition (by merger or consolidation, purchase or otherwise) of the stock, business or properties of other banks or other companies.

The earnings of commercial banks and their holding companies are affected not only by general economic conditions but also by the policies of various governmental regulatory authorities. In particular, the FRB regulates money and credit conditions and interest rates in order to influence general economic conditions, primarily through open-market operations in U.S. Government securities, varying the discount rate on bank borrowings, and setting reserve requirements against bank deposits. These policies have a significant influence on overall growth and distribution of bank loans, investments and deposits, and affect interest rates charged on loans and earned on investments or paid for time and savings deposits. FRB monetary policies have had a significant effect on the operating results of commercial banks in the past and this is expected to continue in the future. The general effect, if any, of such policies upon the future business and earnings of the Company cannot accurately be predicted.

The Company and its bank subsidiary are required by law to maintain minimum levels of capital. These required capital levels are expressed in terms of capital ratios, known as the leverage ratio and the capital to risk-based assets ratios. The Company and its bank subsidiary each significantly exceeded the minimum required capital levels for each measure of capital adequacy as of December 31, 2006. See Note 9 to the Company's consolidated financial statements that are presented in Item 8 of this Report, which Note 9 is incorporated herein by reference.

Also, federal regulations define five categories of financial institutions for purposes of implementing prompt corrective action and supervisory enforcement requirements of the Federal Deposit Insurance Corporation Improvements Act of 1991. The category to which the most highly capitalized institutions are assigned is termed "well-capitalized." Institutions falling into this category must have a total risk-based capital ratio (the ratio of total capital to risk-weighted assets) of at least 10%, a Tier 1 risk-based capital ratio (the ratio of Tier 1, or "core", capital to risk-weighted assets) of at least 6%, a leverage ratio (the ratio of Tier 1 capital to total assets) of at least 5%, and must not be subject to any written agreement, order or directive from its regulator relative to meeting and maintaining a specific capital level. On December 31, 2006, the Company had a total risk-based capital ratio of 10.66%, a Tier 1 risk-based capital ratio of 8.69% (based on Tier 1 capital of $77,926,000 and total risk-weighted assets of $896,450,000), and a leverage ratio of 7.41%. The Company's affiliate bank met all of the requirements of the "well-capitalized" category. In addition the Company meets the requirements of the FRB to be considered a "well-capitalized" bank holding company. Accordingly, the Company does not expect these regulations to significantly impact operations.

The Company is a corporation separate and distinct from its bank and other subsidiaries. Most of the Company's revenues will be received by it in the form of dividends, fees, and interest paid by its bank subsidiary. This subsidiary is subject to statutory restrictions on its ability to pay dividends. The FRB possesses enforcement powers over bank holding companies and their non-bank subsidiaries that enable it to prevent or remedy actions that in its view may represent unsafe or unsound practices or violations of applicable statutes and regulations. Among these powers is the ability in appropriate cases to proscribe the payment of dividends by banks and bank holding companies. The FDIC and DFI possess similar enforcement powers over the bank subsidiary of the Company for which they have supervision. The "prompt corrective action" provisions of federal banking law impose further restrictions on the payment of dividends by insured banks which fail to meet specified capital levels and, in some cases, their parent bank holding companies.

Internet Address; Internet Availability of SEC Reports.

The Company's Internet address is www.germanamericanbancorp.com.

The Company makes available, free of charge through the Investors section of its Internet website, a link to the Internet website of the Securities and Exchange Commission (SEC) by which the public may view the Company's annual report on Form 10-K, its quarterly reports on Form 10-Q, its current reports on Form 8-K and any amendments to those reports filed or furnished pursuant to Section 13(a) of the Securities Exchange Act of 1934, as amended, as soon as reasonably practicable after those reports are filed with or furnished to the SEC.

Forward-Looking Statements and Associated Risks.

The Company from time to time in its oral and written communications makes statements relating to its expectations regarding the future. These types of statements are considered "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements can include statements about the Company's net interest income or net interest margin; adequacy of allowance for loan losses, and the quality of the Company's loans, investment securities and other assets; simulations of changes in interest rates; litigation results; dividend policy; estimated cost savings, plans and objectives for future operations; and expectations about the Company's financial and business performance and other business matters as well as economic and market conditions

and trends. They often can be identified by the use of words like "expect," "may," "will," "would," "could," "should," "i
"project," "estimate," "believe" or "anticipate," or similar expressions.

The Company may include forward-looking statements in filings with the SEC, such as this Form 10-K, in other written materials, and in oral statements made by senior management to analysts, investors, representatives of the media, and others. It is intended that these forward-looking statements speak only as of the date they are made, and the Company undertakes no obligation to update any forward-looking statement to reflect events or circumstances after the date on which the forward-looking statement is made.

Readers are cautioned that, by their nature, forward-looking statements are based on assumptions and are subject to risks, uncertainties, and other factors. Actual results may differ materially from the expectations of the Company that are expressed or implied by any forward-looking statement. The discussions in Item 1A, "Risk Factors," and in Item 7 of this Form 10-K, "Management's Discussion and Analysis of Financial Condition and Results of Operations," list some of the factors that could cause the Company's actual results to vary materially from those expressed or implied by any forward-looking statements. Other risks, uncertainties, and factors that could cause the Company's actual results to vary materially from those expressed or implied by any forward-looking statement include the unknown future direction of interest rates and the timing and magnitude of any changes in interest rates; the effects of changes in competitive conditions; acquisitions of other businesses or intangible customer relationships of other companies by the Company and costs of integrations of such acquired businesses and intangible customer relationships; the introduction, withdrawal, success, and timing of business initiatives and strategies; changes in customer borrowing, repayment, investment, and deposit practices; changes in fiscal, monetary, and tax policies; changes in financial and capital markets; changes in general economic conditions, either nationally or regionally, resulting in, among other things, credit quality deterioration; the impact, extent and timing of technological changes; capital management activities; actions of the Federal Reserve Board and legislative and regulatory actions and reforms; changes in accounting principles and interpretations; the inherent uncertainties involved in litigation and regulatory proceedings which could result in the Company's incurring loss or damage regardless of the merits of the Company's claims or defenses; and the continued availability of earnings and excess capital sufficient for the lawful and prudent declaration and payment of cash dividends. Investors should consider these risks, uncertainties, and other factors in addition to those mentioned by the Company in its other SEC filings from time to time when considering any forward-looking statement.

Item 1A. Risk Factors.

While we a have a history of profitability and operate in mature industries with capital that substantially exceeds the requirements of bank regulatory agencies, an investment in our common stock (like an investment in the equity securities of any business enterprise) is subject to investment risks and uncertainties. The following describes some of the principal risks and uncertainties to which we and our assets and businesses are subject; other risks are briefly identified in our cautionary statement that is included "Forward-Looking Statements and Associated Risks" in Part I, Item 1, "Business." Although we seek ways to manage these risks and uncertainties and to develop programs to control those that we can, we ultimately cannot predict the future. Future results may differ materially from past results, and from our expectations and plans.

If our actual loan losses exceed our estimates, our earnings and financial condition will be impacted.

A significant source of risk for any bank or other enterprise that lends money arises from the possibility that losses will be sustained because borrowers, guarantors and related parties may fail (because of financial difficulties or other reasons) to perform in accordance with the terms of their loan agreements. In our case, we originate many loans that are secured, but some loans are unsecured depending on the nature of the loan. With respect to secured loans, the collateral securing the repayment of these loans includes a wide variety of real and personal property that may be insufficient to cover the obligations owed under such loans. Collateral values may be adversely affected by changes in prevailing economic, environmental and other conditions, including declines in the value of real estate, changes in interest rates, changes in monetary and fiscal policies of the federal government, wide-spread disease, terrorist activity, environmental contamination, natural disasters, and other external events. We have adopted underwriting and credit monitoring procedures and policies, including the establishment and review of the allowance for loan losses and regular review of appraisals and borrower financial statements, that we believe are appropriate to mitigate the risk of loss by assessing the likelihood of nonperformance and the value of available collateral, monitoring loan performance and diversifying our credit portfolio. Such policies and procedures, however, may not prevent unexpected losses that could have a material adverse effect on our business, financial condition, results of operations or liquidity. For additional information regarding our asset quality, see Part II, Item 7 ("Management's Discussion and Analysis of Financial Condition and Results of Operations.")

We could be adversely affected by changes in interest rates.

Our earnings depend largely on the relationship between the yield on earning assets, primarily loans and investments, and the cost of funds, primarily deposits and borrowings. This relationship, known as the interest rate spread, is subject to fluctuation and is affected by economic and competitive factors which influence interest rates, the volume and mix of interest-earning assets and interest-bearing liabilities and the level of non-performing assets. Fluctuations in interest rates affect the demand of customers for our products and services. We are subject to interest rate risk to the degree that our interest-bearing liabilities reprice or mature more slowly or more rapidly or on a different basis than its interest-earning assets. Significant fluctuations in interest rates could have a material adverse effect on our business, financial condition, results of operations or liquidity. For additional information regarding interest rate risk, see Part II, Item 7A, ("Quantitative and Qualitative Disclosures About Market Risk.")

Our success is tied to the economic vitality of our Southern Indiana markets.

We conduct business from offices that are exclusively located in ten contiguous counties of Southern Indiana, from which substantially all of our customer base is drawn. Because of the geographic concentration of our operations and customer base, our results depend largely upon economic conditions in this area. Deterioration in economic conditions in this area could adversely affect the quality of our loan portfolio and the demand for our products and services, and accordingly, could have a material adverse effect on our business, financial condition, results of operations or liquidity. See also Part I, Item 1, "Business --- Competition."

We face substantial competition.

The banking and financial services business in our markets is highly competitive. We compete with much larger regional, national, and international competitors. In addition, new banks could be organized in our market area which might bid aggressively for new business to capture market share in these markets. Developments increasing the nature or level of our competition, or decreasing the effectiveness by which we compete, could have a material adverse effect on our business, financial condition, results of operations or liquidity. See also “Competition,” and “Regulation and Supervision.”

Our business expansion and capital management strategies may be less successful than planned.

We from time to time consider opportunities to expand our business including strategies for launching new internal business initiatives and buying or investing in other businesses or business assets. Our earnings and financial condition could be adversely affected to the extent that the acquisitions or other business initiatives and strategies are not successful (or take longer than expected to achieve expected results) and such initiative or strategies could even result in losses. We also from time to time engage in activities (such as repurchasing and issuing our capital stock or other securities, and utilizing the borrowing capacity of our parent company to borrow funds from third party lenders on short and long term bases) in order to manage our capital structure and to finance acquisitions in a manner that we believe is most advantageous. These capital management activities and financing activities, however, also carry risks in the event that our business does not develop as expected or there are changes in the market for our common stock or in the capital and financial markets generally.

We operate in a highly regulated environment and changes in laws and regulations to which we are subject may adversely affect our results of operations.

The banking industry in which we operate is subject to extensive regulation and supervision under federal and state laws and regulations. The restrictions imposed by such laws and regulations limit the manner in which we conduct our business, undertake new investments and activities and obtain financing. These regulations are designed primarily for the protection of the deposit insurance funds and consumers and not to benefit our shareholders. Financial institution regulation has been the subject of significant legislation in recent years and may be the subject of further significant legislation, none of which is in our control. Significant new laws or changes in, or repeals of, existing laws (including changes in federal or state laws affecting corporate taxpayers generally or financial institutions specifically) could have a material adverse effect on our business, financial condition, results of operations or liquidity. Further, federal monetary policy, particularly as implemented through the Federal Reserve System, significantly affects credit conditions, and any unfavorable change in these conditions could have a material adverse effect on our business, financial condition, results of operations or liquidity. See also Part I, Item 1, “Business -- Supervision and Regulation of Banking Activities.”

The manner in which we report our financial condition and results of operations may be affected by accounting changes.

Our financial condition and results of operations that are presented in the Consolidated Financial Statements, accompanying Notes to the Consolidated Financial Statements, and selected financial data appearing elsewhere within this report, are, to a large degree, dependent upon our accounting policies. The selection of and application of these policies involve estimates, judgments and uncertainties that are subject to change, and the effect of any change in estimates or judgments that might be caused by future developments or resolution of uncertainties could be materially adverse to our reported financial condition and results of operations. See the discussion of critical accounting policies and estimates that we have determined to be the most susceptible to change in the near term that is included in the section captioned “Critical Accounting Policies and Estimates” in Part II, Item 7 (“Management’s Discussion and Analysis of Financial Condition and Results of Operations”) for a complete discussion. In addition, authorities that

prescribe accounting principles and standards for public companies from time to time change those principles or standards or adopt formal or informal interpretations of existing principles or standards, which changes or interpretations (to the extent applicable to us) could result in changes that would be materially adverse to our reported financial condition and results of operations.

Item 1B. Unresolved Staff Comments.

None.

Item 2. Properties.

The Company's executive offices are located in the main office building of its bank subsidiary, German American Bancorp, at 711 Main Street, Jasper, Indiana. The main office building contains approximately 23,600 square feet of office space. The Company's subsidiaries conduct their operations from 36 other locations in Southern Indiana.

Item 3. Legal Proceedings.

There are no material pending legal proceedings, other than routine litigation incidental to the business of the Company's subsidiaries, to which the Company or any of its subsidiaries is a party or of which any of their property is the subject.

Item 4. Submission of Matters to a Vote of Security Holders.

There were no matters submitted during the fourth quarter of 2006 to a vote of security holders, by solicitation of proxies or otherwise.

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

Market and Dividend Information

German American Bancorp, Inc.'s stock is traded on NASDAQ's Global Select Market under the symbol GABC. The quarterly high and low closing prices for the Company's common stock as reported by NASDAQ and quarterly cash dividends declared and paid are set forth in the table below.

	2006			2005		
	High	Low	Cash Dividend	High	Low	Cash Dividend
Fourth Quarter	**$ 14.41**	**$ 13.59**	**$ 0.140**	$ 13.64	$ 12.71	$ 0.140
Third Quarter	**$ 14.39**	**$ 12.89**	**$ 0.140**	$ 14.74	$ 13.30	$ 0.140
Second Quarter	**$ 13.65**	**$ 12.90**	**$ 0.140**	$ 15.21	$ 12.53	$ 0.140
First Quarter	**$ 13.70**	**$ 12.83**	**$ 0.140**	$ 15.98	$ 15.18	$ 0.140
			$ 0.560			$ 0.560

The Common Stock was held of record by approximately 3,425 shareholders at March 1, 2007.

Cash dividends paid to the Company's shareholders are primarily funded from dividends received by the Company from its bank subsidiary. The declaration and payment of future dividends will depend upon the earnings and financial condition of the Company and its subsidiaries, general economic conditions, compliance with regulatory requirements affecting the ability of the bank subsidiary to declare dividends, and other factors.

Transfer Agent:	UMB Bank, N.A. Securities Transfer Division P.O. Box 410064	**Shareholder Information and Corporate Office:**	Terri A. Eckerle German American Bancorp, Inc P. O. Box 810 Jasper, Indiana 47547-0810

Kansas City, MO	(800) 482-1314
64141-0064	(812) 482-1314
Contact: Shareholder Relations	
(800) 884-4225	

Stock Performance Graph

The following graph compares the Corporation's five-year cumulative total returns with those of the Russell 2000 Stock Index and the Indiana Bank Peer Group. The Indiana Bank Peer Group (which is a custom peer group identified by Company management) includes all Indiana-based commercial bank holding companies (excluding companies owning thrift institutions that are not regulated as bank holding companies) that have been in existence as commercial bank holding companies throughout the five-year period ended December 2006, the stocks of which have been traded on an established securities market (NYSE, AMEX, NASDAQ) throughout that five-year period. The returns of each company in the Indiana Bank Peer Group have been weighted to reflect the company's market capitalization. The Russell 2000 Stock Index is an index consisting of the 1,001st through 3,000th largest United States traded stocks, based on market capitalization, which is annually reconstituted at the end of each June. The Company's stock was included in the Russell 2000 Index as it was constituted from July 2001 through June 2005.

Stock Repurchase Program Information

The following table sets forth information regarding the Company's purchases of its common shares during each of the three months ended December 31, 2006.

Period	Total Number Of Shares (or Units) Purchased	Average Price Paid Per Share (or Unit)	Total Number of Shares (or Units) Purchases as Part of Publicly Announced Plans or Programs	Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs [1]
October 2006	—	—	—	272,789
November 2006	—	—	—	272,789
December 2006	—	—	—	272,789

[1] On April 26, 2001, the Company announced that its Board of Directors had approved a stock repurchase program for up to 607,754 of its outstanding common shares, of which the Company had purchased 334,965 common shares through December 31, 2006 (both such numbers adjusted for subsequent stock dividends). The Board of Directors established no expiration date for this program. The Company purchased no shares under this program during the quarter ended December 31, 2006.

Item 6. Selected Financial Data.

The following selected data should be read in conjunction with the consolidated financial statements and related notes that are included in Item 8 of this Report, and "Management's Discussion and Analysis of Financial Condition and Results of Operations," which is included in Item 7 of this Report (dollars in thousands, except per share data).

	2006	2005	2004	2003	2002
Summary of Operations:					
Interest Income	**$ 63,594**	$ 50,197	$ 47,710	$ 50,619	$ 60,494
Interest Expense	**27,398**	17,984	16,471	21,084	28,492
Net Interest Income	**36,196**	32,213	31,239	29,535	32,002
Provision for Loan Losses	**925**	1,903	2,015	811	1,115
Net Interest Income after Provision For Loan Losses	**35,271**	30,310	29,224	28,724	30,887
Non-interest Income	**15,390**	14,194	9,620[1]	12,934	9,509
Non-interest Expense	**36,456**	31,448	30,609	32,219[2]	28,967
Income before Income Taxes	**14,205**	13,056	8,235	9,439	11,429
Income Tax Expense	**3,984**	3,335	996	1,271	1,987
Net Income	**$ 10,221**	$ 9,721	$ 7,239	$ 8,168	$ 9,442
Year-end Balances:					
Total Assets	**$ 1,093,424**	$ 946,467	$ 942,094	$ 925,946	$ 957,005
Total Loans, Net of Unearned Income	**796,259**	651,956	629,793	611,866	610,741
Total Deposits	**867,618**	746,821	750,383	717,133	707,194
Total Long-term Debt	**68,333**	66,606	69,941	76,880[2]	121,687
Total Shareholders' Equity	**92,391**	82,255	83,669	83,126[3]	104,519
Average Balances:					
Total Assets	**$ 1,029,838**	$ 925,851	$ 927,528	$ 938,992	$ 1,000,167
Total Loans, Net of Unearned Income	**715,260**	634,526	622,240	618,340	644,990
Total Deposits	**814,440**	730,220	731,467	711,310	718,763
Total Shareholders' Equity	**88,451**	84,479	82,558	87,703[3]	103,301
Per Share Data [4]:					
Net Income	**$ 0.93**	$ 0.89	$ 0.66	$ 0.73[3]	$ 0.79
Cash Dividends	**0.56**	0.56	0.56	0.53	0.51
Book Value at Year-end	**8.39**	7.73	7.68	7.60[3]	8.72
Other Data at Year-end:					
	3,438	3,494	3,219	3,198	3,299

Number of Shareholders					
Number of Employees	**397**	367	372	383	390
Weighted Average Number of Shares [4]	**10,994,739**	10,890,987	10,914,622	11,176,766 [3]	12,007,009
Selected Performance Ratios:					
Return on Assets	**0.99%**	1.05%	0.78%	0.87%	0.94%
Return on Equity	**11.56%**	11.51%	8.77%	9.31%[3]	9.14%
Equity to Assets	**8.45%**	8.69%	8.88%	8.98%[3]	10.92%
Dividend Payout	**60.30%**	62.83%	84.46%	73.26%	64.99%
Net Charge-offs to Average Loans	**0.50%**	0.26%	0.24%	0.14%	0.19%
Allowance for Loan Losses to Loans	**0.90%**	1.42%	1.40%	1.35%	1.36%
Net Interest Margin	**3.96%**	3.92%	3.86%	3.61%	3.67%

(1) In 2004, the Company recognized a $3.7 million non-cash pre-tax charge (which reduced Non-interest Income) for the other-than-temporary decline in value of its FHLMC and FNMA preferred stock portfolio. In 2006, the Company sold these same FHLMC and FNMA preferred stocks and recognized a pre-tax gain of $951.

(2) In 2003, the Company prepaid $40.0 million of FHLB borrowings within its mortgage banking segment. The prepayment fees associated with the extinguishment of these borrowings totaled $1.9 million.

(3) In March 2003, the Company purchased 1,110,444 (approximately 9% of the number of shares that were then outstanding) of its common shares at $19.05 per share pursuant to a self tender offer at a total cost, including fees and expenses incurred in connection with the offer, of approximately $21.4 million.

(4) Share and Per Share Data has been retroactively adjusted to give effect for stock dividends and excludes the dilutive effect of stock options.

Year to year financial information comparability is affected by the purchase accounting treatment for mergers and acquisitions. See Note 18 to the Company's consolidated financial statements included in Item 8 of this Report.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

INTRODUCTION

German American Bancorp, Inc. is a financial services holding company based in Jasper, Indiana. The Company's Common Stock is traded on NASDAQ's Global Select Market, under the symbol GABC. The principal subsidiary of German American Bancorp, Inc., is its banking subsidiary, German American Bancorp, which operates through six community banking affiliates with 30 retail banking offices in the ten contiguous Southern Indiana counties of Daviess, Dubois, Gibson, Knox, Lawrence, Martin, Monroe, Perry, Pike, and Spencer. German American Bancorp, Inc., also owns a trust, brokerage, and financial planning subsidiary, which operates from the banking offices of the bank subsidiary, and two insurance agencies with six insurance agency offices throughout its market area.

Throughout this Management's Discussion and Analysis, as elsewhere in this report, when we use the term "Company", we will usually be referring to the business and affairs (financial and otherwise) of the Company and its subsidiaries and affiliates as a whole. Occasionally, we will refer to the term "parent company" or "holding company" when we mean to refer to only German American Bancorp, Inc.

The information in this Management's Discussion and Analysis is presented as an analysis of the major components of the Company's operations for the years 2004 through 2006 and its financial condition as of December 31, 2006 and 2005. This information should be read in conjunction with the accompanying consolidated financial statements and footnotes contained elsewhere in this report and with the description of business included in Item 1 of this Report (including the cautionary disclosure regarding "Forward Looking Statements and Associated Risks"). Financial and other information by segment is included in Note 16 to the Company's consolidated financial statements included in Item 8 of this Report and is incorporated into this Item 7 by reference.

The statements of management's expectations and goals concerning the Company's future operations and performance that are set forth in the following Management Overview and in other sections of this Item 7 are forward-looking statements, and readers are cautioned that these forward-looking statements are based on assumptions and are subject to risks, uncertainties, and other factors. Actual results may differ materially from the expectations of the Company that is expressed or implied by any forward-looking statement. This Item 7, as well as the discussions in Item 1 ("Business") entitled "Forward-Looking Statements and Associated Risks" and in Item 1A ("Risk Factors") (which discussions are incorporated in this Item 7 by reference) list some of the factors that could cause the Company's actual results to vary materially from those expressed or implied by any such forward-looking statements.

MANAGEMENT OVERVIEW

The Company's net income increased 5% in 2006 compared with 2005. The Company's 2006 net income totaled $10,221,000, or $0.93 per share, compared with $9,721,000, or $0.89 per share, for 2005. Current year earnings were positively affected by increases within the Company's net interest income and non-interest income as well as a reduced level of provision for loan losses. The improvement in the level of net interest income was largely attributable to strong loan growth. Loans outstanding grew by $145.1 million or 22% during 2006. The increase in non-interest income was primarily credited to the gain derived from the sale of the Company's portfolio of agency-issued preferred stock during the third quarter of 2006 and an increased level of insurance revenues. An offsetting factor to these positive earnings contributors was an increased level of non-interest related operating expenses due in large part to the inclusion of the recent banking and insurance acquisitions.

Effective January 1, 2006, the Company completed the acquisition of Stone City Bancshares, Inc. which was in an adjacent market to its primary market area and effective October 1, 2005, the Company completed the in-market acquisition of PCB Holding Company. In addition to these acquisitions, during the three-year period ended December

31, 2006, the Company invested in non-controlling interests in the common stocks of four separate banking companies that operate in the Indianapolis, Evansville, Louisville, and Terre Haute/Lafayette (Indiana) banking markets. As a result of making these four non-controlling investments, the Company has the opportunity to bid to purchase participations in loans that may be originated by these other banking companies from time to time, if and to the extent that the banking company desires to sell participations in such loans to third parties. During the fourth quarter of 2006, the Company expanded its agricultural lending business by acquiring the Southern Indiana-based agricultural loan portfolio of a regional banking company. Finally, effective October 1, 2006, the Company completed the acquisition of the insurance agency business of Keach and Grove Insurance, Inc. of Bedford, Indiana which was in the market of the Company's recent banking acquisition of Stone City Bancshares, Inc. These acquisitions, purchases and investments have been undertaken to supplement organic growth within the Company's primary markets. Management expects to continue to pursue similar strategic acquisition and investing opportunities should opportunities become available.

Effective September 30, 2006, the Company combined the charters of its six subsidiary banks into a single bank charter in order to simplify its corporate structure and better serve its customers, while retaining local direction of affiliate bank operations under the existing distinctive bank trade names in each of the markets served by the Company.

MERGERS AND ACQUISITIONS

On October 1, 2005 PCB Holding Company ("PCB") merged with and into the Company. PCB's sole banking subsidiary, Peoples Community Bank, operated two banking offices in Tell City, Indiana. PCB's assets and equity (unaudited) as of September 30, 2005 totaled $34.6 million and $4.8 million, respectively. Under the terms of the merger, the shareholders of PCB received an aggregate of 257,029 shares of common stock of the Company valued at approximately $3.5 million and approximately $3.2 million of cash, representing a total transaction value of $6.7 million. This merger was accounted for under the purchase method of accounting.

On January 1, 2006, Stone City Bancshares, Inc. ("Stone City") merged with and into the Company, and as a result acquired all of the stock of Stone City's sole banking subsidiary, Stone City Bank of Bedford, Indiana, which operated two banking offices in Bedford, Indiana. Stone City's assets and equity as of December 31, 2005 totaled $61.2 million and $5.4 million, respectively. Under the terms of the merger, the shareholders of Stone City received aggregate cash payments of approximately $6.4 million and 349,468 common shares of the Company valued during a pre-closing valuation period of approximately $4.6 million, representing a total transaction value of approximately $11.0 million. This merger was accounted for under the purchase method of accounting.

On October 1, 2006 the Company acquired substantially all of the assets, net of certain assumed liabilities of Keach and Grove Insurance, Inc. of Bedford, Indiana. The agency operations became a part of German American Insurance, Inc., the Company's property and casualty insurance entity. The purchase price for this transaction was $2.26 million in cash. This merger was accounted for under the purchase method of accounting.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The financial condition and results of operations for German American Bancorp, Inc. presented in the Consolidated Financial Statements, accompanying Notes to the Consolidated Financial Statements, and selected financial data appearing elsewhere within this report, are, to a large degree, dependent upon the Company's accounting policies. The selection of and application of these policies involve estimates, judgments and uncertainties that are subject to change. The critical accounting policies and estimates that the Company has determined to be the most susceptible to change in the near term relate to the determination of the allowance for loan losses, the valuation of securities available for sale, and the valuation allowance on deferred tax assets and loss contingencies related to exposure from tax examinations.

Allowance for Loan Losses

The Company maintains an allowance for loan losses to cover probable incurred credit losses at the balance sheet date. 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. Allocations of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management's judgment, should be charged-off. A provision for loan losses is charged to operations based on management's periodic evaluation of the necessary allowance balance. Evaluations are conducted at least quarterly and more often if deemed necessary. The ultimate recovery of all loans is susceptible to future market factors beyond the Company's control.

The Company has an established process to determine the adequacy of the allowance for loan losses. The determination of the allowance is inherently subjective, as it requires significant estimates, including the amounts and timing of expected future cash flows on impaired loans, estimated losses on other classified loans and pools of homogeneous loans, and consideration of past loan loss experience, the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values, economic conditions, and other factors, all of which may be susceptible to significant change. The allowance consists of two components of allocations, specific and general. These two components represent the total allowance for loan losses deemed adequate to cover losses inherent in the loan portfolio.

Commercial and agricultural loans are subject to a standardized grading process administered by an internal loan review function. The need for specific reserves is considered for credits when graded substandard or special mention, or when: (a) the customer's cash flow or net worth appears insufficient to repay the loan; (b) the loan has been criticized in a regulatory examination; (c) the loan is on non-accrual; or, (d) other reasons where the ultimate collectibility of the loan is in question, or the loan characteristics require special monitoring. Specific allowances are established in cases where management has identified significant conditions or circumstances related to an individual credit that we believe indicates the loan is impaired. Specific allocations on impaired loans are determined by comparing the loan balance to the present value of expected cash flows or expected collateral proceeds. Allocations are also applied to categories of loans not considered individually impaired but for which the rate of loss is expected to be greater than historical averages, including those graded substandard or special mention and non-performing consumer or residential real estate loans. Such allocations are based on past loss experience and information about specific borrower situations and estimated collateral values.

General allocations are made for other pools of loans, including non-classified loans, homogeneous portfolios of consumer and residential real estate loans, and loans within certain industry categories believed to present unique risk of loss. General allocations of the allowance are primarily made based on a five-year historical average for loan losses for these portfolios, judgmentally adjusted for economic factors and portfolio trends.

Due to the imprecise nature of estimating the allowance for loan losses, the Company’s allowance for loan losses includes a minor unallocated component. The unallocated component of the allowance for loan losses incorporates the Company’s judgmental determination of inherent losses that may not be fully reflected in other allocations, including factors such as economic uncertainties, lending staff quality, industry trends impacting specific portfolio segments, and broad portfolio quality trends. Therefore, the ratio of allocated to unallocated components within the total allowance may fluctuate from period to period.

Mortgage Servicing Rights Valuation

Mortgage servicing rights (MSRs) were recognized and included with other assets for the allocated value of retained servicing rights on loans sold. Servicing rights were expensed in proportion to, and over the period of, estimated net servicing revenues. Impairment was evaluated based on the fair value of the rights, using groupings of the underlying loans as to type and age. Fair value was determined based upon discounted cash flows using market-based assumptions.

To determine the fair value of MSRs, the Company used a valuation model that calculated the present value of estimated future net servicing income. In using this valuation method, the Company incorporated assumptions that market participants would use in estimating future net servicing income, which included estimates of prepayment speeds, discount rate, cost to service, escrow account earnings, contractual servicing fee income, ancillary income, late fees, and float income.

The Company sold its mortgage servicing rights portfolio during the second quarter of 2006. Currently, all residential loans that are sold in the secondary market are sold on a servicing released basis.

Securities Valuation

Securities available-for-sale are carried at fair value, with unrealized holding gains and losses reported separately in accumulated other comprehensive income (loss), net of tax. The Company obtains market values from a third party on a monthly basis in order to adjust the securities to fair value. Additionally, all securities are required to be written down to fair value when a decline in fair value is other than temporary; therefore, future changes in the fair value of securities could have a significant impact on the Company’s operating results. In determining whether a market value decline is other than temporary, management considers the reason for the decline, the extent of the decline and the duration of the decline. See Note 2 in the accompanying Consolidated Financial Statements for information regarding unrealized losses on the securities.

Income Tax Expense

Income tax expense involves estimates related to the valuation allowance on deferred tax assets and loss contingencies related to exposure from tax examinations.

A valuation allowance reduces deferred tax assets to the amount management believes is more likely than not to be realized. In evaluating the realization of deferred tax assets, management considers the likelihood that sufficient taxable income of appropriate character will be generated within carryback and carryforward periods, including consideration of available tax planning strategies. As of December 31, 2006, the Company had a deferred tax asset of $1.9 million representing various tax credit carryforwards. Based on the long carryforward periods available,

management has assessed it more likely than not that these credits will be realized and no valuation allowance has been established on this asset.

Loss contingencies, including assessments arising from tax examinations and tax strategies, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated. In considering the likelihood of loss, management considers the nature of the contingency, the progress of any examination or related protest or appeal, the views of legal counsel and other advisors, experience of the Company or other enterprises in similar matters, if any, and management's intended response to any assessment.

During the first quarter of 2005, the Company received notices of proposed assessments of unpaid financial institutions tax for the years 2001 and 2002 of approximately $691,000 ($456,000 net of federal tax), including interest and penalties of approximately $100,000. The Company filed a protest with the Indiana Department of Revenue contesting the proposed assessments and vigorously defended its position that the income of the Nevada subsidiaries was not subject to the Indiana financial institutions tax. Therefore, no tax provision was recognized for the potential assessment of additional financial institutions tax for 2001 and 2002 or for financial institutions tax with respect to any of the Nevada subsidiaries in any period subsequent to 2002, including the year ended December 31, 2006.

During the first quarter of 2007, the Company and the Indiana Department of Revenue entered into an agreement regarding the proposed assessment for tax years 2001 and 2002. As a result of this agreement the Company was not required to pay any tax liability as assessed by the Indiana Department of Revenue for tax years 2001 and 2002. In addition, tax years 2001 and 2002 are closed to further examination.

RESULTS OF OPERATIONS

NET INCOME

Net income increased $500,000 or 5% to $10,221,000 or $0.93 per share in 2006 compared to $9,721,000 or $0.89 per share during 2005. The increase in net income during 2006 compared with 2005 was attributable principally to an increase in net interest income of $3,983,000, a reduction in provision for loan losses of $978,000, and a gain on the sale of the Company’s portfolio of agency preferred stock of $951,000, which were partially mitigated by an increase of $5,008,000 in non-interest expense. The increases in net interest income and non-interest expenses were largely attributable to acquisitions of PCB Holding Company and Stone City Bancshares, Inc., which are discussed in Note 18 to the consolidated financial statements included in Item 8 of this Report.

Net income increased $2,482,000 or 34% to $9,721,000 or $0.89 per share in 2005 compared to $7,239,000 or $0.66 per share during 2004. The earnings increase was largely attributable to the inclusion in 2004’s results of an after-tax charge of $2,430,000 or $0.23 per share, related to other-than-temporary impairment of the Company’s portfolio of Federal Home Loan Mortgage Corporation (“FHLMC”) and Federal National Mortgage Association (“FNMA”) preferred stocks. In addition to the effect of the securities impairment charge, the earnings comparison of 2005 to 2004 was positively impacted by improvements in net interest income of $974,000, as well as increases in the level of other non-interest income. Non-interest income, excluding the impairment charge on equity securities in 2004, increased by approximately $891,000 in 2005 compared to 2004. Those increases were partially mitigated by increased non-interest expense of $839,000, a significant portion of which related to increased employee health insurance costs, and increased income tax expense of $2,339,000 ($1,087,000 excluding the tax effect of the impairment charge in 2004).

NET INTEREST INCOME

Net interest income is the Company’s single largest source of earnings, and represents the difference between interest and fees realized on earning assets, less interest paid on deposits and borrowed funds. Several factors contribute to the determination of net interest income and net interest margin, including the volume and mix of earning assets, interest rates, and income taxes. Many factors affecting net interest income are subject to control by management policies and actions. Factors beyond the control of management include the general level of credit and deposit demand, Federal Reserve Board monetary policy, and changes in tax laws.

Net interest income increased $3,983,000 or 12% (an increase of $3,809,000 or 11% on a tax-equivalent basis) for the year ended 2006 compared with 2005. The increase in net interest income was primarily attributable to an increased level of average earning assets and an increased net interest margin for the year ended 2006 compared with 2005. The

higher level of earning assets was primarily attributable to an increase in the average level of loans outstanding that resulted from new loan activity and from the previously discussed banking acquisitions completed effective October 1, 2005 and effective January 1, 2006. Average earning assets totaled $941.6 million during 2006 compared with $853.3 million during 2005.

For 2006, the net interest margin increased to 3.96% compared to 3.92% during 2005. Net interest margin is tax equivalent net interest income expressed as a percentage of average earning assets. The Company’s yield on earning assets totaled 6.87% compared with a cost of funds (expressed as a percentage of average earning assets) of 2.91% producing the net interest margin of 3.96% for the year ended December 31, 2006. The Company’s yield on earning assets was 6.03% compared with a cost of funds of 2.11% netting to a net interest margin of 3.92% for the year ended December 31, 2005.

Net interest income increased $974,000 or 3% ($576,000 or 2% on a tax-equivalent basis) in 2005 compared with 2004. For 2005, the net interest margin increased to 3.92% compared with 3.86% in 2004. The Company's increase in net interest income during 2005 compared with 2004 was largely attributable to the increase in the net interest margin. The Company's yield on earning assets increased to 6.03% during 2005 compared with 5.79% for 2004. The increased yield on earning assets was primarily attributable to higher short-term interest rates and an increased level of loans outstanding during 2005 compared with 2004. The Company's cost of funds (expressed as a percentage of average earning assets) during 2005 was 2.11% compared with 1.93% for 2004. The increase in the cost of funds was due to a rise in short-term market interest rates tempered by an increased level of non-maturity deposits including non-interest bearing demand accounts, less reliance on time deposits and borrowings and a decline in interest rates on outstanding borrowings from the Federal Home Loan Bank due to repayments of higher-cost advances that were outstanding in 2004.

The following table summarizes net interest income (on a tax-equivalent basis) for each of the past three years. For tax-equivalent adjustments, an effective tax rate of 34% was used for all years presented [(1)].

Average Balance Sheet
(Tax-equivalent basis / dollars in thousands)

	Twelve Months Ended December 31, 2006			Twelve Months Ended December 31, 2005			Twelve Months Ended December 31, 2004		
	Principal Balance	Income/ Expense	Yield / Rate	Principal Balance	Income/ Expense	Yield / Rate	Principal Balance	Income/ Expense	Yield / Rate
ASSETS									
Federal Funds Sold and Other Short-term Investments	**$ 10,971**	**$ 545**	**4.97%**	$ 10,632	$ 316	2.97%	$ 10,635	$ 129	1.21%
Securities:									
Taxable	**174,007**	**7,763**	**4.46%**	161,499	5,954	3.69%	161,601	5,455	3.38%
Non-taxable	**41,312**	**2,721**	**6.59%**	46,666	3,297	7.07%	57,729	4,347	7.53%
Total Loans and Leases [(2)]	**715,260**	**53,621**	**7.50%**	634,526	41,860	6.60%	622,240	39,407	6.33%
TOTAL INTEREST EARNING ASSETS	**941,550**	**64,650**	**6.87%**	853,323	51,427	6.03%	852,205	49,338	5.79%
Other Assets	**97,570**			81,771			83,960		
Less: Allowance for Loan Losses	**(9,282)**			(9,243)			(8,637)		
TOTAL ASSETS	**$ 1,029,838**			$ 925,851			$ 927,528		
LIABILITIES AND SHAREHOLDERS' EQUITY									
Interest-Bearing Demand Deposits	**$ 140,786**	**$ 2,625**	**1.86%**	$ 137,318	$ 1,436	1.05%	$ 121,173	$ 557	0.46%
Savings Deposits	**174,095**	**4,263**	**2.45%**	156,820	2,212	1.41%	163,272	1,188	0.73%
Time Deposits	**369,800**	**14,441**	**3.91%**	314,420	9,741	3.10%	330,898	10,002	3.02%
FHLB Advances and Other Borrowings	**113,559**	**6,069**	**5.34%**	98,932	4,595	4.64%	101,067	4,724	4.67%
TOTAL INTEREST-BEARING LIABILITIES	**798,240**	**27,398**	**3.43%**	707,490	17,984	2.54%	716,410	16,471	2.30%
Demand Deposit Accounts	**129,759**			121,662			116,124		
Other Liabilities	**13,388**			12,220			12,436		

TOTAL LIABILITIES	**941,387**	841,372	844,970
Shareholders' Equity	**88,451**	84,479	82,558
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	**$ 1,029,838**	$ 925,851	$ 927,528
NET INTEREST INCOME	**$ 37,252**	$ 33,443	$ 32,867
NET INTEREST MARGIN	**3.96%**	3.92%	3.86%

[1] Effective tax rates were determined as though interest earned on the Company's investments in municipal bonds and loans was fully taxable.

[2] Loans held-for-sale and non-accruing loans have been included in average loans. Interest income on loans includes loan fees of $1,727, $1,326, and $1,442 for 2006, 2005, and 2004, respectively.

The following table sets forth for the periods indicated a summary of the changes in interest income and interest expense resulting from changes in volume and changes in rates:

Net Interest Income - Rate/Volume Analysis:
(Tax-Equivalent basis, dollars in thousands)

	2006 compared to 2005 Increase / (Decrease) Due to [1]			2005 compared to 2004 Increase / (Decrease) Due to [1]		
	Volume	**Rate**	**Net**	**Volume**	**Rate**	**Net**
Interest Income:						
Federal Funds Sold and Other Short-term Investments	**$ 10**	**$ 219**	**$ 229**	$ —	$ 187	$ 187
Taxable Securities	**487**	**1,322**	**1,809**	(3)	502	499
Non-taxable Securities	**(362)**	**(214)**	**(576)**	(794)	(256)	(1,050)
Loans and Leases	**5,677**	**6,084**	**11,761**	788	1,665	2,453
Total Interest Income	**5,812**	**7,411**	**13,223**	(9)	2,098	2,089
Interest Expense:						
Savings and Interest-bearing Demand	**274**	**2,966**	**3,240**	61	1,842	1,903
Time Deposits	**1,896**	**2,804**	**4,700**	(506)	245	(261)
FHLB Advances and Other Borrowings	**730**	**744**	**1,474**	(99)	(30)	(129)
Total Interest Expense	**2,900**	**6,514**	**9,414**	(544)	2,057	1,513
Net Interest Income	**$ 2,912**	**$ 897**	**$ 3,809**	$ 535	$ 41	$ 576

[1] The change in interest due to both rate and volume has been allocated to volume and rate changes in proportion to the relationship of the absolute dollar amounts of the change in each.

See the Company's Average Balance Sheet and the discussions headed USES OF FUNDS, SOURCES OF FUNDS, and "RISK MANAGEMENT - Liquidity and Interest Rate Risk Management" for further information on the Company's net interest income, net interest margin, and interest rate sensitivity position.

PROVISION FOR LOAN LOSSES

The Company provides for loan losses through regular provisions to the allowance for loan losses. The provision is affected by net charge-offs on loans and changes in specific and general allocations required on the allowance for loan losses. Provisions for loan losses totaled $925,000, $1,903,000, and $2,015,000, in 2006, 2005 and 2004, respectively.

The Company's provision for loan losses declined during 2006 in conjunction with a decline in the Company's level of non-performing loans. The largest factor in the Company's ability to recognize the reduced level of provision for loan losses was the finalization of settlement of a previously identified large nonperforming credit in the second quarter of 2006. The Company recognized a charge-off of approximately $393,000 on this individual credit facility. The specific allocation as of year end 2005 was for considerably more than the level of charge-off allowing the Company to recover the balance of the specific allocation assigned to this credit. For further discussion of non-performing loans refer to "Risk Management - Lending and Loan Administration."

Loan loss provision remained relatively stable during 2005 compared with 2004. While net charge-offs increased in 2005, a portion of the increase in charge-offs was provided for prior to 2005.

These provisions were made at a level deemed necessary by management to absorb estimated, probable incurred losses in the loan portfolio. A detailed evaluation of the adequacy of the allowance for loan losses is completed quarterly by management, the results of which are used to determine provisions for loan losses. Management estimates the allowance balance required using past loan loss experience, the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values, economic conditions, and other factors. Refer also to the sections entitled CRITICAL ACCOUNTING POLICIES AND ESTIMATES and “RISK MANAGEMENT - Lending and Loan Administration” for further discussion of the provision and allowance for loan losses.

NON-INTEREST INCOME

During 2006, Non-interest Income totaled $15,390,000, an increase of 8% compared with 2005. The increase during 2006 was largely attributable to the gain on the sale of the Company's FHLMC and FNMA preferred stock portfolio and an increase in revenues generated by the Company's insurance operations. During 2005, all categories of Non-interest Income increased. Non-interest Income for 2005 was $14,194,000, an increase of $4,574,000 or 48%, as compared to $9,620,000 in 2004. The increase in 2005 was predominantly attributable to an other-than-temporary impairment charge on the Company's FHLMC and FNMA preferred stock portfolio recognized in the fourth quarter of 2004.

Non-interest Income (dollars in thousands)	Years Ended December 31,			% Change From Prior Year	
	2006	**2005**	**2004**	**2006**	**2005**
Trust and Investment Product Fees	**$ 2,210**	$ 2,081	$ 2,046	**6%**	2%
Service Charges on Deposit Accounts	**3,901**	3,723	3,537	**5**	5
Insurance Revenues	**5,094**	4,703	4,666	**8**	1
Other Operating Income	**2,384**	2,687	2,074	**(11)**	30
Subtotal	**13,589**	13,194	12,323	**3**	7
Net Gains on Sales of Loans and Related Assets	**850**	1,000	975	**(15)**	3
Net Gain / (Loss) on Securities	**951**	—	(3,678)	**n/m(1)**	n/m(1)
TOTAL NON-INTEREST INCOME	**$ 15,390**	$ 14,194	$ 9,620	**8**	48

(1) n/m = not meaningful

Insurance Revenues increased 8% for 2006 as compared 2005. The increased Insurance Revenues were primarily the result of a higher level of contingency revenues during 2006 compared with 2005 and the revenues generated from the insurance agency acquisition completed in the fourth quarter of 2006. For more information on the business combination, see Note 18 to the Company's consolidated financial statements included in Item 8 of this Report. Insurance Revenues remained relatively stable for the year ended December 31, 2005 compared with 2004.

For the year ended 2006, Other Operating Income declined 11% compared with 2005. The decline for the year ended December 31, 2006 was predominately due to a gain on the sale of a former branch facility of approximately $313,000 that was recorded during the second quarter of 2005 and a higher level of recovery of mortgage servicing rights impairment charges during 2005 than during 2006. For the year ended 2005, Other Operating Income increased 30% as compared to the prior year. The increase during 2005 compared with 2004 was primarily due to the aforementioned gain from the sale of a former branch facility and a higher level of impairment recovery for mortgage servicing rights.

Net Gains on Sales of Loans and Related Assets declined 15% during 2006 following an increase of 3% in 2005. Loan sales for 2006, 2005, and 2004 were $55.6 million, $64.1 million, and $61.4 million, respectively. The decline during 2006 compared with the 2005 was largely due to a reduced level of sales of residential mortgage loans and a lower margin on those loans sold in the secondary market. The decline in gains from the sales of loans was somewhat offset by the sale of the Company's mortgage servicing rights portfolio during the second quarter of 2006. The Company sold its mortgage servicing rights relating to approximately $344.5 million of mortgage loans serviced for others for a total sales price of $3.6 million resulting in a net gain of $198,000.

The Company recognized a gain on the sale of its portfolio of FHLMC and FNMA preferred stock during the third quarter of 2006. The gain from the sale of this agency preferred stock portfolio totaled $951,000. The portfolio had a

book value at the time of the sale of approximately $12.1 million. The Company had previously recorded a non-cash other-than-temporary impairment charge of $3.7 million on this portfolio during 2004.

NON-INTEREST EXPENSE

For the year ended 2006, Non-interest Expense increased 16%. These increases in non-interest expense were largely attributable to the acquisitions of PCB Holding Company as of October 1, 2005 and Stone City Bancshares, Inc. as of January 1, 2006. For the year ended 2005, Non-interest Expense increased 3%.

Non-interest Expense (dollars in thousands)	Years Ended December 31,			% Change From Prior Year	
	2006	**2005**	**2004**	**2006**	**2005**
Salaries and Employee Benefits	**$ 21,491**	$ 18,511	$ 17,814	**16%**	4%
Occupancy, Furniture and Equipment Expense	**4,988**	4,404	4,292	**13**	3
FDIC Premiums	**108**	101	106	**7**	(5)
Data Processing Fees	**1,646**	1,322	1,186	**25**	11
Professional Fees	**1,786**	1,703	1,690	**5**	1
Advertising and Promotion	**940**	784	888	**20**	(12)
Supplies	**619**	544	527	**14**	3
Other Operating Expenses	**4,878**	4,079	4,106	**20**	(1)
TOTAL NON-INTEREST EXPENSE	**$ 36,456**	$ 31,448	$ 30,609	**16**	3

Salaries and Employee Benefits increased 16% during 2006. The increase in Salaries and Employee Benefits Expense was primarily due to an increase in full-time equivalent employees attributable to the banking acquisitions completed effective October 1, 2005 and January 1, 2006 and to a lesser degree the insurance agency acquisition completed effective October 1, 2006. Also contributing to the increase in Salaries and Employee Benefits Expense to a lesser degree was the adoption of FAS 123R, "Share Based Payments," as of January 1, 2006. In 2005, Salaries and Employee Benefits Expense increased 4%. The increase was primarily attributable to increased employee health insurance costs of $528,000.

Occupancy, Furniture and Equipment Expense increased 13% during 2006 compared with 2005. The increase was primarily attributable to the acquisition activity during 2005 and 2006. Occupancy, Furniture and Equipment Expense increased 3% in 2005. The increase was primarily attributable to a lowered amount of real estate and personal property tax expense recognized in 2004.

Data Processing Fees increased 25% during 2006 following an increase of 11% during 2005. These increases were largely attributable to the banking acquisition activity completed during 2005 and 2006. Advertising and Promotion expense increased 20% following a decline of 12% in 2005. The increase in 2006 compared with 2005 was largely attributable to the acquisition activity during 2006. The decline during 2005 was the result of more directed marketing campaigns during the year.

Other Operating Expenses increased 20% during 2006 following a modest decline of 1% during 2005. The increase was primarily attributable to a higher level of intangible amortization of $265,000 which resulted from the Company's banking and insurance acquisitions during 2005 and 2006 and increased amortization and impairment charges during 2006 associated with one of the Company's affordable housing limited partnership investments of $313,000. For further discussion of intangible amortization, see Note 18 to the Company's consolidated financial statements included in Item 8 of this Report.

PROVISION FOR INCOME TAXES

The Company records a provision for current income taxes payable, along with a provision for deferred taxes payable in the future. Deferred taxes arise from temporary differences, which are items recorded for financial statement purposes in a different period than for income tax returns. The Company's effective tax rate was 28.0%, 25.5%, and 12.1%, respectively, in 2006, 2005, and 2004. The higher effective tax rate in 2006 compared with both 2005 and 2004 was the result of higher levels of before tax net income combined with a lower level of tax-exempt investment income and a lower level of tax credits generated by investments in affordable housing projects. The effective tax rate in all periods is lower than the blended statutory rate of 39.6%. The lower effective rate in all periods primarily resulted from the Company's tax-exempt investment income on securities and loans, income tax credits generated by investments in affordable housing projects, and income generated by subsidiaries domiciled in a state with no state or local income tax. See Note 11 to the Company's consolidated financial statements included in Item 8 of this Report for additional details relative to the Company's income tax provision.

Since December 31, 2001, the Company's effective tax rate has been favorably impacted by Indiana financial institution tax savings resulting from the Company's formation of investment subsidiaries in the state of Nevada by four of the Company's banking subsidiaries. The state of Nevada has no state or local income tax. During the first quarter of 2005, the Company received notices of proposed assessments of unpaid Indiana financial institutions tax for the years 2001 and 2002 of approximately $691,000 ($456,000 net of federal tax), including interest and penalties of approximately $100,000. The Company filed a protest with the Indiana Department of Revenue contesting the proposed assessments and vigorously defended its position that the income of the Nevada subsidiaries was not subject to the Indiana financial institutions tax. Therefore, no tax provision was recognized for the potential assessment of additional financial institutions tax for 2001 and 2002 or for financial institutions tax with respect to any of the Nevada subsidiaries in any period subsequent to 2002, including the year ended December 31, 2006.

During the first quarter of 2007, the Company and the Indiana Department of Revenue entered into an agreement regarding the proposed assessment for tax years 2001 and 2002. As a result of this agreement the Company was not required to pay any tax liability as assessed by the Indiana Department of Revenue for tax years 2001 and 2002. In addition, tax years 2001 and 2002 are closed to further examination.

CAPITAL RESOURCES

The Company and its affiliate bank are subject to regulatory capital requirements administered by federal banking agencies. Capital adequacy guidelines and prompt corrective action regulations involve quantitative measures of assets, liabilities, and certain off-balance sheet items calculated under regulatory accounting practices. The prompt corrective action regulations provide five classifications, including well-capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized, although these terms are not used to represent overall financial condition. The Company and its affiliate bank at year-end 2006 were categorized as well-capitalized as that term is defined by applicable regulations. The Company has agreed with its parent-company correspondent bank lender, JPMorgan Chase Bank, N.A., as a term of its credit facilities with that lender (see "SOURCES OF FUNDS - Parent Company Funding sources", below) that it will maintain the capital ratios of the Company and its affiliate bank at levels that would qualify it as well-capitalized as that term is defined by the prompt corrective action regulations. See Note 9 to the Company's consolidated financial statements included in Item 8 of this Report for actual and required capital ratios and for additional information regarding capital adequacy.

The Company continues to maintain a strong capital position. Shareholders' equity totaled $92.4 million and $82.3 million at December 31, 2006 and 2005, respectively. Total equity represented 8.5% and 8.7%, respectively, of year-end total assets. The Company paid cash dividends of $6.2 million and $6.1 million or $0.56 per share in 2006 and 2005. The increase in shareholders' equity during 2006 compared with 2005 was primarily the result of retained earnings, shares issued in conjunction with the Stone City Bancshares, Inc. acquisition, and a reduction in the unrealized loss on available for sale securities.

USES OF FUNDS

LOANS

Total loans at year-end 2006 increased $145.1 million or 22% compared with year-end 2005 including increases in each category of loans. The Company's commercial and industrial loans increased $82.6 million or 26% and agricultural based loans increased $47.5 million or 47% during 2006. Consumer loans increased $3.2 million or 2% and residential mortgage loans increased $11.8 million or 11% during 2006. The growth during 2006 was generated from a variety of sources, including approximately $55.0 million of internally generated growth, $48.0 million related to the acquisition of Stone City Bancshares, Inc., and $42.1 million from the purchase of a Southern Indiana-based agricultural loan portfolio of a regional banking company in December 2006.

Total loans at year-end 2005 increased $22.5 million or 4% compared with year-end 2004 including increases in each category of loans. The Company's commercial and industrial loans increased $5.9 million or 2% and agricultural based loans increased $1.8 million or 2% during 2005. Consumer loans increased $6.7 million or 6% during 2005. Residential mortgage loans increased $8.1 million or 9% during 2005. This increase reversed a trend over the past several years and was due in large part to the acquisition of Peoples Community Bank during the fourth quarter of 2005.

The Company's loan portfolio is diversified, with the heaviest concentration in commercial and industrial loans. The composition of the loan portfolio remained relatively stable at year-end 2006 compared with year-end 2005. The acquisition of the agricultural loan portfolio in December 2006 increased the concentration of agricultural based loans

to approximately 19% of the total loan portfolio. The largest concentration of loans continued to be in commercial and industrial loans, which comprised 50% of the total loan portfolio at year-end 2006, compared with 49% in 2005. The Company's commercial lending is extended to various industries, including hotel, agribusiness and manufacturing, as well as health care, wholesale, and retail services.

Loan Portfolio dollars in thousands	December 31, 2006	2005	2004	2003	2002
Residential Mortgage Loans	**$ 114,687**	$ 102,891	$ 94,800	$ 110,325	$ 156,180
Agricultural Loans	**148,872**	101,355	99,557	92,095	84,984
Commercial and Industrial Loans	**402,285**	319,681	314,354	296,661	254,776
Consumer Loans	**132,791**	129,587	122,888	114,816	116,987
Total Loans	**798,635**	653,514	631,599	613,897	612,927
Less: Unearned Income	**(2,376)**	(1,558)	(1,806)	(2,031)	(2,186)
Subtotal	**796,259**	651,956	629,793	611,866	610,741
Less: Allowance for Loan Losses	**(7,129)**	(9,265)	(8,801)	(8,265)	(8,301)
Loans, Net	**$ 789,130**	$ 642,691	$ 620,992	$ 603,601	$ 602,440
Ratio of Loans to Total Loans:					
Residential Mortgage Loans	**14%**	16%	15%	18%	26%
Agricultural Loans	**19%**	15%	16%	15%	14%
Commercial and Industrial Loans	**50%**	49%	50%	48%	41%
Consumer Loans	**17%**	20%	19%	19%	19%
Totals	**100%**	100%	100%	100%	100%

The Company's policy is generally to extend credit to consumer and commercial borrowers in its primary geographic market area in Southern Indiana. Commercial extensions of credit outside this market area are generally concentrated in real estate loans within a 120 mile radius of the Company's primary market and are granted on a selective basis. These out-of-market credits include participations that the Company may purchase from time to time in loans that are originated by the four banks in which the Company owns non-controlling common stock investments. These banks operate from headquarters in Indianapolis, Evansville, and Dana, Indiana (near Terre Haute) and Louisville, Kentucky; the bank in Dana, Indiana has branched into Lafayette, Indiana.

The following table indicates the amounts of loans (excluding residential mortgages on 1-4 family residences and consumer loans) outstanding as of December 31, 2006, which, based on remaining scheduled repayments of principal, are due in the periods indicated (dollars in thousands).

	Within One Year	One to Five Years	After Five Years	Total
Commercial and Agricultural	**$ 211,032**	**$ 229,485**	**$ 110,640**	**$ 551,157**

	Interest Sensitivity	
	Fixed Rate	Variable Rate
Loans maturing after one year	**$ 96,265**	**$ 243,860**

INVESTMENTS

The investment portfolio is a principal source for funding the Company's loan growth and other liquidity needs of its subsidiaries. The Company's securities portfolio consists of money market securities, uncollateralized U.S. Treasury and federal agency securities, municipal obligations of state and political subdivisions, asset- / mortgage-backed

securities issued by U.S. government agencies and other intermediaries, and corporate investments. Money market securities include federal funds sold, interest-bearing balances with banks, and other short-term investments. The composition of the year-end balances in the investment portfolio is presented in Note 2 to the Company's consolidated financial statements included in Item 8 of this Report and in the table below:

Investment Portfolio, at Amortized Cost dollars in thousands	**December 31, 2006**	**%**	**2005**	**%**	**2004**	**%**
Federal Funds Sold and Short-term Investments	**$ 5,935**	**3%**	$ 5,287	3%	$ 24,354	11%
U.S. Treasury and Agency Securities	**28,083**	**15**	13,631	7	4,060	2
Obligations of State and Political Subdivisions	**25,788**	**13**	31,759	16	43,125	20
Asset- / Mortgage-backed Securities	**125,340**	**66**	128,602	65	131,614	60
Corporate Securities	—	—	500	n/m[1]	503	n/m[1]
Equity Securities	**6,236**	**3**	17,350	9	15,149	7
Total Securities Portfolio	**$ 191,382**	**100%**	$ 197,129	100%	$ 218,805	100%

[1] n/m = not meaningful

The amortized cost of investment securities, including federal funds sold and short-term investments, decreased $5.7 million at year-end 2006 compared with year-end 2005. The largest concentration in the investment portfolio continues to be in mortgage related securities. The Company's level of obligations of state and political subdivisions declined $6.0 million or 19% during 2006 and $11.4 million or 26% during 2005. The decline in obligations of state and political subdivisions has been primarily the result of the Company's strategy to not invest in these traditionally longer-term securities during periods of relatively low longer-term interest rates. The Company continues to believe that at the proper time, investment in tax-advantaged obligations of state and political subdivisions is prudent. However, in the relatively low longer-term interest rate environment, investments in these types of securities have not been undertaken.

The Company's equity securities portfolio at year-end 2006 consisted of non-controlling common stock investments in five unaffiliated banking companies. In prior years the equity securities also included the Company's portfolio of floating rate preferred stock issued by FHLMC and FNMA. The Company sold its portfolio of FHLMC and FNMA preferred stock during the third quarter of 2006. The gain from the sale of this agency preferred stock portfolio totaled $951,000. The portfolio had a book value at the time of the sale of approximately $12.1 million. The Company had previously recorded a non-cash other-than-temporary impairment charge of $3.7 million on this portfolio during 2004.

Investment Securities, at Carrying Value
dollars in thousands

			December 31,			
Securities Held-to-Maturity:		**2006**		**2005**		**2004**
Obligations of State and Political Subdivisions	**$**	**6,135**	$	8,684	$	13,318
Securities Available-for-Sale:						
U.S. Treasury and Agency Securities	**$**	**28,133**	$	13,492	$	4,034
Obligations of State and Political Subdivisions		**19,928**		23,527		30,621
Asset- / Mortgage-backed Securities		**123,859**		125,844		131,201
Corporate Securities		—		500		503
Equity Securities		**7,302**		17,787		15,317
Subtotal of Securities Available-for-Sale		**179,222**		181,150		181,676
Total Securities	**$**	**185,357**	$	189,834	$	194,994

The Company's $179.2 million available-for-sale portion of the investment portfolio provides an additional funding source for the liquidity needs of the Company's subsidiaries and for asset/liability management requirements. Although management has the ability to sell these securities if the need arises, their designation as available-for-sale should not be interpreted as an indication that management anticipates such sales.

The amortized cost of debt securities at December 31, 2006 are shown in the following table by expected maturity. Asset- / mortgage-backed securities are based on estimated average lives. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations. Equity securities do not have contractual maturities, and are excluded from the table below.

Maturities and Average Yields of Securities at December 31, 2006 (dollars in thousands):

	Within One Year		After One But Within Five Years		After Five But Within Ten Years		After Ten Years	
	Amount	**Yield**	**Amount**	**Yield**	**Amount**	**Yield**	**Amount**	**Yield**

U.S. Treasuries and Agencies	$	3,005	3.14%	$	25,078	5.05%	$	—	N/A	$	—	N/A
State and Political Subdivisions		2,955	6.89%		7,813	7.27%		10,187	7.42%		4,833	7.49%
Asset- / Mortgage-backed Securities		18,404	3.27%		85,686	4.61%		21,040	5.56%		210	3.52%
Corporate Securities		—	N/A		—	N/A		—	N/A		—	N/A
Totals	$	24,364	3.69%	$	118,577	4.88%	$	31,227	6.17%	$	5,043	7.32%

A tax-equivalent adjustment using a tax rate of 34 percent was used in the above table.

In addition to the other uses of funds discussed previously, the Company had certain long-term contractual obligations as of December 31, 2006. These contractual obligations primarily consisted of long-term borrowings with the FHLB and JPMorgan Chase Bank, N.A., time deposits, and lease commitments for certain office facilities. Scheduled principal payments on long-term borrowings, time deposits, and future minimum lease payments are outlined in the table below.

Contractual Obligations dollars in thousands	Total	Payments Due By Period Less Than 1 Year	1-3 Years	3-5 Years	More than 5 Years
Long-Term Borrowings	$ 68,333	$ 11,277	$ 17,187	$ 23,817	$ 16,052
Time Deposits	400,257	291,532	96,658	9,533	2,534
Lease Commitments	567	201	267	99	—
Total	$ 469,157	$ 303,010	$ 114,112	$ 33,449	$ 18,586

SOURCES OF FUNDS

The Company’s primary source of funding is its base of core customer deposits. Core deposits consist of demand deposits, savings, interest-bearing checking, money market accounts, and certificates of deposit of less than $100,000. Other sources of funds are certificates of deposit of $100,000 or more, brokered deposits, overnight borrowings from other financial institutions and securities sold under agreement to repurchase. The membership of the Company’s affiliate bank in the Federal Home Loan Bank System (FHLB) provides a significant additional source for both long and short-term collateralized borrowings. In addition, the Company, as a separate and distinct corporation from its bank and other subsidiaries, also has the ability to borrow funds from other financial institutions. The following pages contain a discussion of changes in these areas.

The table below illustrates changes between years in the average balances of all funding sources:

Funding Sources - Average Balances dollars in thousands	December 31, 2006	2005	2004	% Change From Prior Year 2006	2005
Demand Deposits					
Non-interest Bearing	**$ 129,759**	$ 121,662	$ 116,124	**7%**	5%
Interest Bearing	**140,786**	137,318	121,173	**3**	13
Savings Deposits	**61,453**	66,091	65,757	**(7)**	1
Money Market Accounts	**112,642**	90,729	97,515	**24**	(7)
Other Time Deposits	**276,815**	242,887	268,842	**14**	(10)
Total Core Deposits	**721,455**	658,687	669,411	**10**	(2)
Certificates of Deposits of $100,000 or more and Brokered Deposits	**92,985**	71,533	62,056	**30**	15
FHLB Advances and Other Borrowings	**113,559**	98,932	101,067	**15**	(2)
Total Funding Sources	**$ 927,999**	$ 829,152	$ 832,534	**12**	n/m[1]

[1] n/m = not meaningful

Maturities of certificates of deposit of $100,000 or more are summarized as follows (dollars in thousands):

	3 Months Or Less	3 thru 6 Months	6 thru 12 Months	Over 12 Months	Total
December 31, 2006	**$ 54,351**	**$ 13,625**	**$ 31,918**	**$ 20,653**	**$ 120,547**

CORE DEPOSITS

The Company's overall level of average core deposits increased approximately 10% during 2006 following a 2% decline during 2005. The Company's ability to attract core deposits continues to be influenced by competition and the interest rate environment, as well as the increased availability of alternative investment products. Management believes that core deposits continue to represent a stable and viable funding source for the Company's operations.

Demand, savings and money market deposits have provided a growing source of funding for the company in each of the periods reported. Average demand, savings and money market deposits totaled $444.6 million or 62% of core deposits in 2006 compared with $415.8 million or 63% in 2005 and $400.6 million or 60% in 2004.

Other time deposits consist of certificates of deposits in denominations of less than $100,000. These deposits increased by 14% during 2006 following a decline of 10% in 2005. Other time deposits comprised 38% of core deposits in 2006 compared with 37% in 2005 and 40% in 2004.

OTHER FUNDING SOURCES

Federal Home Loan Bank advances and other borrowings represent the Company's most significant source of other funding. Average borrowed funds increased $14.6 million or 15% during 2006 following a decline of $2.1 million or 2% in 2005. Borrowings comprised approximately 12% of total funding sources in 2006, 2005, and 2004. The increase in average borrowed funds during 2006 was largely attributable to parent company borrowings that resulted from the banking acquisition activity during late 2005 and early 2006.

Certificates of deposits in denominations of $100,000 or more and brokered deposits are an additional source of other funding for the Company's bank subsidiary. Large denomination certificates and brokered deposits increased $21.5 million or 30% during 2006 following an increase of $9.5 million or 15% in 2005. Large certificates and brokered deposits comprised approximately 10% of total funding sources in 2006, 9% in 2005 and 7% in 2004. This type of funding is used as both long-term and short-term funding sources.

The bank subsidiary of the Company also utilizes short-term funding sources from time to time. These sources consist of overnight federal funds purchased from other financial institutions, secured repurchase agreements that generally mature within one day of the transaction date, and secured overnight variable rate borrowings from the FHLB. These borrowings represent an important source of short-term liquidity for the Company's bank subsidiary. Long-term debt at the Company's bank subsidiary is in the form of FHLB advances, which are secured by the pledge of certain investment securities and residential mortgage loans. See Note 8 to the Company's consolidated financial statements included in Item 8 of this Report for further information regarding borrowed funds.

PARENT COMPANY FUNDING SOURCES

The Company is a corporation separate and distinct from its bank and other subsidiaries. For information regarding the financial condition, result of operations, and cash flows of the Company, presented on a parent-company-only basis, see Note 17 to the Company's consolidated financial statements included in Item 8 of this Report.

The Company uses funds at the parent company level to pay dividends to its shareholders, to acquire or make other investments in other businesses or their securities or assets, to repurchase its stock from time to time, and for other general corporate purposes. The parent company does not have access at the parent-company level to the deposits and certain other sources of funds that are available to its bank subsidiary to support its operations. Instead, the parent company has historically derived most of its revenues from dividends paid to the parent company by its bank subsidiary. The Company's banking subsidiary is subject to statutory restrictions on its ability to pay dividends to the parent company. The parent company has in recent years supplemented the dividends received from its subsidiaries with borrowings, which are discussed in detail below.

On December 29, 2006, the Company and JPMorgan Chase Bank, N.A. (the "Lender") executed and delivered to each other a Second Amended and Restated Loan and Subordinated Debenture Purchase Agreement ("Restated Agreement"), and the Company executed and delivered to the Lender a $10 million Subordinated Debenture, a $10 million Term Note and a $15 million Revolving Note pursuant to the Restated Agreement to evidence its obligations for amounts that may from time to time be borrowed thereunder. The Company's obligations under the Term Note and Revolving Note are secured by a pledge of all of the Company's stock in its sole depository institution subsidiary, German American Bancorp, pursuant to a pledge agreement.

The Restated Agreement established new credit facilities that replace the Company's prior credit facilities with the Lender. Among other changes, the Restated Agreement (a) continued through January 1, 2008 the Company's ability under the Prior Agreement to access a $15 million revolving credit line in order to support parent company liquidity needs from time to time, all of which was available for borrowing as of December 31, 2006; (b) restructured $10 million of the prior $25 million term loan as a new subordinated seven-year loan that is intended to qualify as Tier 2 capital for regulatory capital purposes; and (c) lengthened the maturity schedule for repaying another $10 million of the prior $25 million term loan. The remaining $5 million of the $25 million that was outstanding under the term loan with this lender was prepaid by the Company on December 29, 2006, from parent company working capital.

The new term loan established under the Restated Agreement is evidenced by a new term note in the principal amount of $10 million, which matures on the following schedule: $1.0 million principal amount payable on January 1, 2008 and $1.5 million payable on January 1 of each of the years 2009 through 2014, inclusive. Interest is payable quarterly on the outstanding principal balance.

The new subordinated loan established under the Restated Agreement is evidenced by a subordinated debenture in the principal amount of $10 million, and matures in a single installment of principal on January 1, 2014. Interest is payable quarterly on the outstanding principal balance.

The new revolving loan established under the Restated Agreement is evidenced by a new revolving note in the principal amount of $15 million, and matures on January 1, 2008, at which time all amounts borrowed under the revolving loan will become due and payable. Interest is payable quarterly on the outstanding principal balance.

Pursuant to the Restated Agreement, the Company made certain representations and warranties to the Lender, and agreed to comply with certain affirmative and negative covenants with the Lender, which are substantially the same as the representations, warranties, and covenants that were included in the Prior Agreement. Among the affirmative covenants are provisions requiring that (a) the Company maintain the capital ratios of the Company and of its subsidiary bank(s) at levels that would be considered “well-capitalized” under the prompt corrective action regulations of the federal banking agencies, and (b) the Company maintain a consolidated ratio of (i) the sum of its non-performing loans plus other real estate owned (real estate that is neither used in the ordinary course of the business of the Company or its subsidiaries nor held for future use) (OREO) to (ii) the sum of the Company’s loans plus OREO, of not greater than 3.25%. At December 31, 2006, this ratio was 1.32%.

Among the Company’s negative covenants are provisions that generally prohibit the Company and its subsidiaries, without the consent of the Lender, from (a) becoming liable in respect of any indebtedness for borrowed money, other than in the ordinary course of business of the bank subsidiaries, (b) incurring liens on their assets, other than to secure borrowings in the ordinary course of business of the bank subsidiaries, (c) issuing trust preferred securities, and (d) acquiring other businesses in acquisition transactions that would be significant when measured by certain size restrictions described by the Restated Agreement.

Upon the occurrence of an event of default under the Restated Agreement, the Lender may terminate the availability of future credit under the revolving loan facility and declare all amounts outstanding under the revolving loan and term loan to be due and payable in full. In addition, in certain limited circumstances defined by the Restated Agreement, an event of default may entitle the Lender to declare all amounts outstanding under the subordinated loan to be due and payable in full.

See Note 8 to the Company’s consolidated financial statements included in Item 8 of this Report for further information regarding the parent company borrowed funds.

RISK MANAGEMENT

The Company is exposed to various types of business risk on an on-going basis. These risks include credit risk, liquidity risk and interest rate risk. Various procedures are employed at the Company’s affiliate banks to monitor and mitigate risk in the loan and investment portfolios, as well as risks associated with changes in interest rates. Following is a discussion of the Company’s philosophies and procedures to address these risks.

LENDING AND LOAN ADMINISTRATION

Primary responsibility and accountability for day-to-day lending activities rests with the Company’s subsidiary bank. Loan personnel at the subsidiary bank have the authority to extend credit under guidelines approved by the bank’s board of directors. The executive loan committee serves as a vehicle for communication and for the pooling of knowledge, judgment and experience of its members. The committee provides valuable input to lending personnel, acts as an approval body, and monitors the overall quality of the bank’s loan portfolio. The Corporate Risk Management Committee, comprised of members of the Company’s and its subsidiary bank’s executive officers and

board of directors, strives to ensure a consistent application of the Company's lending policies. The Company also maintains a comprehensive risk-grading and loan review program, which includes quarterly reviews of problem loans, delinquencies and charge-offs. The purpose of this program is to evaluate loan administration, credit quality, loan documentation and the adequacy of the allowance for loan losses.

The Company maintains an allowance for loan losses to cover probable, incurred credit losses identified during its loan review process. Management estimates the required level of allowance for loan losses using past loan loss experience, the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values, economic conditions, and other factors. Allocations of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management's judgement, should be charged-off. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed.

The allowance for loan losses is comprised of: (a) specific reserves on individual credits; (b) general reserves for certain loan categories and industries, and overall historical loss experience; and (c) unallocated reserves based on performance trends in the loan portfolios, current economic conditions, and other factors that influence the level of estimated probable losses. The need for specific reserves are considered for credits when: (a) the customer's cash flow or net worth appears insufficient to repay the loan; (b) the loan has been criticized in a regulatory examination; (c) the loan is on non-accrual; or, (d) other reasons where the ultimate collectibility of the loan is in question, or the loan characteristics require special monitoring.

Allowance for Loan Losses
dollars in thousands

	Years Ended December 31,				
	2006	**2005**	**2004**	**2003**	**2002**
Balance of allowance for possible losses at beginning of period	**$ 9,265**	$ 8,801	$ 8,265	$ 8,301	$ 8,388
Loans charged-off:					
Residential Mortgage Loans	**184**	238	292	360	437
Agricultural Loans	—	3	—	42	89
Commercial and Industrial Loans	**3,059**	1,278	904	571	183
Consumer Loans	**705**	624	654	658	876
Total Loans charged-off	**3,948**	2,143	1,850	1,631	1,585
Recoveries of previously charged-off Loans:					
Residential Mortgage Loans	**35**	58	24	220	66
Agricultural Loans	**30**	53	11	56	2
Commercial and Industrial Loans	**98**	205	118	316	59
Consumer Loans	**240**	149	218	192	256
Total Recoveries	**403**	465	371	784	383
Net Loans recovered / (charged-off)	**(3,545)**	(1,678)	(1,479)	(847)	(1,202)
Additions to allowance charged to expense	**925**	1,903	2,015	811	1,115
Allowance from Acquired Subsidiary	**484**	239	—	—	—
Balance at end of period	**$ 7,129**	$ 9,265	$ 8,801	$ 8,265	$ 8,301
Net Charge-offs to Average Loans Outstanding	**0.50%**	0.26%	0.24%	0.14%	0.19%
Provision for Loan Losses to Average Loans Outstanding	**0.13%**	0.30%	0.32%	0.13%	0.17%
Allowance for Loan Losses to Total Loans at Year-end	**0.90%**	1.42%	1.40%	1.35%	1.36%

The following table indicates the breakdown of the allowance for loan losses for the periods indicated (dollars in thousands):

Residential Mortgage Loans	**$ 341**	$ 710	$ 790	$ 839	$ 1,126

Agricultural Loans	**1,001**	822	982	704	781
Commercial and Industrial Loans	**5,134**	6,486	5,906	5,358	4,687
Consumer Loans	**602**	1,127	1,043	1,158	1,140
Unallocated	**51**	120	80	206	567
Total Loans	**$ 7,129**	$ 9,265	$ 8,801	$ 8,265	$ 8,301

The allowance for loan losses at year-end 2006 declined to $7.1 million or 0.90% of total loans compared to $9.3 million or 1.42% of total loans at year-end 2005 and $8.8 million or 1.40% at year-end 2004. The decline in the allowance for loan losses was largely attributable to a higher level of net charge-offs, primarily related to commercial and industrial loans, during 2006 as compared with previous years. Net charge-offs increased to $3.5 million or 0.50% of average loans outstanding during 2006. This level compares to $1.7 million or 0.26% of average loans outstanding in 2005 and $1.5 million or 0.24% of average loans outstanding during 2004. The increase in the level of net charge-offs during 2006 was primarily attributable to three commercial credit facilities. The increased level of net charge-offs during 2006 and to a lesser degree in 2005 had been provided for during 2004 and 2005. Therefore, the provision for loan loss declined by $978,000 in 2006 compared with 2005 while the loan loss provision remained relatively stable during 2005 compared with 2004.

The charge-off on the three previously mentioned credit facilities totaled approximately $2.5 million or approximately 0.35% of average loans outstanding. As of year-end 2005, the specific allocations on these credits totaled approximately $2.2 million or 0.34% of average loans outstanding while at year-end 2006 there were only nominal allocations for these credits due to the charge-off activity during 2006. These credit facilities are discussed in additional detail in the following section of this report titled NON-PERFORMING ASSETS.

The Company continues to monitor trends and patterns in loan charge-offs by various product types. Through use of migration analysis for commercial loans and continued analysis of charge-off information for homogenous loan pools, data as of and for the relevant time periods ended December 31, 2006, suggested a lower level of allowance was needed to support probable incurred loan losses. This, along with the previously discussed charge-offs, resulted in a lower level of allowance at year-end 2006.

Please see "RESULTS OF OPERATIONS - Provision for Loan Losses" and "CRITICAL ACCOUNTING POLICIES AND ESTIMATES - Allowance for Loan Losses" for additional information regarding the allowance.

NON-PERFORMING ASSETS

Non-performing assets consist of: (a) non-accrual loans; (b) loans which have been renegotiated to provide for a reduction or deferral of interest or principal because of deterioration in the financial condition of the borrower; (c) loans past due 90 days or more as to principal or interest; and, (d) other real estate owned. Loans are placed on non-accrual status when scheduled principal or interest payments are past due for 90 days or more or when the borrower's ability to repay becomes doubtful. Uncollected interest accrued in the current year is reversed against income at the time a loan is placed on non-accrual. Loans are charged-off at 120 days past due, or earlier if deemed uncollectible. Exceptions to the non-accrual and charge-off policies are made when the loan is well secured and in the process of collection. The following table presents an analysis of the Company's non-performing assets.

Non-performing Assets			December 31,		
dollars in thousands	**2006**	**2005**	**2004**	**2003**	**2002**
Non-accrual Loans	**$ 9,652**	$ 14,763	$ 5,750	$ 1,817	$ 1,773
Past Due Loans (90 days or more)	—	944	831	962	1,095
Restructured Loans	—	—	—	—	365
Total Non-performing Loans	**9,652**	15,707	6,581	2,779	3,233
Other Real Estate	**845**	506	213	749	1,812
Total Non-performing Assets	**$ 10,497**	$ 16,213	$ 6,794	$ 3,528	$ 5,045
Non-performing Loans to Total Loans	**1.21%**	2.41%	1.04%	0.45%	0.53%
Allowance for Loan Losses to Non-performing Loans	**73.86%**	58.99%	133.73%	297.41%	256.76%

The Company's level of overall non-performing assets declined by approximately $5.7 million and non-performing loans declined by approximately $6.1 million during 2006 compared with year-end 2005. The decline in the level of non-accrual loans largely resulted from the resolution of an approximately $4.2 million credit facility, which was extended to a borrower operating a retail grocery store chain. Under an approved bankruptcy plan, the Company was paid approximately 90% of the amount owed to it during April 2006. The remaining decline in non-accrual loans was principally the result of partial charge-offs that totaled $2.1 million on two other commercial credit facilities that remain in work-out status and are discussed in detail below.

The level of non-performing loans remains at higher than historic levels, but is largely attributable to two specific credit facilities that were placed on non-accrual status during 2005. The first of these credits is an approximately $881,000 loan (after a partial charge-off during 2006) to a manufacturing entity which has ceased operations. During the third quarter of 2005, the real estate and equipment of the manufacturing entity were sold at auction to an unrelated third party. The closing of this auction sale has been delayed on a number of instances as various covenants and conditions included in the sales agreement have not been fully performed or satisfied. Based on current information available, the Company expects that this sale will be completed by the end of the third quarter of 2007. The indebtedness owed the Company on this credit is secured by a first priority lien on substantially all of the borrower's assets, including those sold at auction.

The second of these specific credits, which totals approximately $3.6 million (after a partial charge-off during 2006), was extended to a borrower operating two hotel facilities. This credit is secured by a first priority lien on the hotel facilities. The Company has initiated foreclosure action and taken steps to place the properties under control of an

independent management company upon receipt of title to the properties.

The Company will continue to assess the internal classification of these credits and the level of specific allocation of the loan loss reserve attributable to these credits based upon the best information that is available from time to time, including the status of the sale of the manufacturing facility and the status of the hotel facilities.

During 2005, the Company, in accordance with its standard methodology for the identification of potential problem credits, downgraded the internal risk classification on the above mentioned credits and placed them on non-accrual status. The net effect of this activity was to increase the level of non-performing loans for the Company at year-end 2005 as compared with year-end 2004. Interest income recognized on non-performing loans for 2006 was $351,000. The gross interest income that would have been recognized in 2006 on non-performing loans if the loans had been current in accordance with their original terms was $1,846,000. Loans are typically placed on non-accrual status when scheduled principal or interest payments are past due for 90 days or more, unless the loan is well secured and in the process of collection.

Loan impairment is reported when full repayment under the terms of the loan is not expected. If a loan is impaired, a portion of the allowance is allocated so that the loan is reported net, at the present value of estimated future cash flows using the loan's existing rate, or at the fair value of collateral if repayment is expected solely from the collateral. Commercial and agricultural loans are evaluated individually for impairment. Smaller balance homogeneous loans are evaluated for impairment in total. Such loans include real estate loans secured by one-to-four family residences and loans to individuals for household, family and other personal expenditures. Individually evaluated loans on non-accrual are generally considered impaired. Impaired loans, or portions thereof, are charged off when deemed uncollectible. The total dollar amount of impaired loans at December 31, 2006 was $8,155,000. For additional detail on impaired loans, see Note 3 to the Company's consolidated financial statements included in Item 8 of this Report.

LIQUIDITY AND INTEREST RATE RISK MANAGEMENT

Liquidity is a measure of the ability of the Company's subsidiary bank to fund new loan demand, existing loan commitments and deposit withdrawals. The purpose of liquidity management is to match sources of funds with anticipated customer borrowings and withdrawals and other obligations to ensure a dependable funding base, without unduly penalizing earnings. Failure to properly manage liquidity requirements can result in the need to satisfy customer withdrawals and other obligations on less than desirable terms. The liquidity of the parent company is dependent upon the receipt of dividends from its bank subsidiary, which are subject to certain regulatory limitations explained in Note 9 to the Company's consolidated financial statements included in Item 8 of this Report, as enhanced by its ability to draw upon term financing arrangements and a line of credit established by the parent company with a correspondent bank lender as described under "SOURCES OF FUNDS - Parent Company Funding Sources", above. The affiliate bank's source of funding is predominately core deposits, maturities of securities, repayments of loan principal and interest, federal funds purchased, securities sold under agreements to repurchase and borrowings from the Federal Home Loan Bank.

Interest rate risk is the exposure of the Company's financial condition to adverse changes in market interest rates. In an effort to estimate the impact of sustained interest rate movements to the Company's earnings, the Company monitors interest rate risk through computer-assisted simulation modeling of its net interest income. The Company's simulation modeling monitors the potential impact to net interest income under various interest rate scenarios. The Company's objective is to actively manage its asset/liability position within a one-year interval and to limit the risk in any of the interest rate scenarios to a reasonable level of tax-equivalent net interest income within that interval. The Company's Asset/Liability Committee monitors compliance within established guidelines of the Funds Management Policy. See Item 7A. Quantitative and Qualitative Disclosures About Market Risk section for further discussion regarding interest rate risk.

OFF-BALANCE SHEET ARRANGEMENTS

The Company has no off-balance sheet arrangements other than stand-by letters of credit as disclosed in Note 14 to the Company's consolidated financial statements included in Item 8 of this Report.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

The Company's exposure to market risk is reviewed on a regular basis by the Asset/Liability Committees and Board of Directors. Primary market risks, which impact the Company's operations, are liquidity risk and interest rate risk, as discussed above.

As discussed previously, the Company monitors interest rate risk by the use of computer simulation modeling to estimate the potential impact on its net interest income under various interest rate scenarios. Another method by which the Company's interest rate risk position can be estimated is by computing estimated changes in its net portfolio value ("NPV"). This method estimates interest rate risk exposure from movements in interest rates by using interest rate sensitivity analysis to determine the change in the NPV of discounted cash flows from assets and liabilities. NPV represents the market value of portfolio equity and is equal to the estimated market value of assets minus the estimated market value of liabilities. Computations are based on a number of assumptions, including the relative levels of market interest rates and prepayments in mortgage loans and certain types of investments. These computations do not contemplate any actions management may undertake in response to changes in interest rates, and should not be relied upon as indicative of actual results. In addition, certain shortcomings are inherent in the method of computing NPV. Should interest rates remain or decrease below current levels, the proportion of adjustable rate loans could decrease in future periods due to refinancing activity. In the event of an interest rate change, prepayment levels would likely be different from those assumed in the table. Lastly, the ability of many borrowers to repay their adjustable rate debt may decline during a rising interest rate environment.

The following table provides an assessment of the risk to NPV in the event of sudden and sustained 1% and 2% increases and decreases in prevailing interest rates. The table indicates that as of December 31, 2006 the Company's estimated NPV might be expected to decrease under both an increase or decrease in prevailing interest rates (dollars in thousands).

Interest Rate Sensitivity as of December 31, 2006

Changes in Rates	**Net Portfolio Value**		**Net Portfolio Value as a % of Present Value of Assets**	
	$ Amount	**% Change**	**NPV Ratio**	**Change**
+2%	$ 123,537	-5.53%	11.61%	(34)b.p.
+1%	127,349	-2.61%	11.80%	(15)b.p.
Base	130,763	—	11.95%	—
-1%	129,271	-1.14%	11.68%	(27)b.p.
-2%	125,102	-4.33%	11.21%	(74)b.p.

The above discussion, and the portions of MANAGEMENT'S DISCUSSION AND ANALYSIS in Item 7 of this Report that are referenced in the above discussion contain statements relating to future results of the Company that are considered "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. These statements relate to, among other things, simulation of the impact on net interest income from changes in interest rates. Actual results may differ materially from those expressed or implied therein as a result of certain risks and uncertainties, including those risks and uncertainties expressed above, those that are described in MANAGEMENT'S DISCUSSION AND ANALYSIS in Item 7 of this Report, and those that are described in Item 1 of this Report, "Business," under the caption "Forward-Looking Statements and Associated Risks," which discussions are incorporated herein by reference.

Item 8. Financial Statements and Supplementary Data.

Report of Independent Registered Public Accounting Firm on Financial Statements

Board of Directors and Shareholders
German American Bancorp, Inc.
Jasper, Indiana

We have audited the accompanying consolidated balance sheets of German American Bancorp, Inc. as of December 31, 2006 and 2005, and the related consolidated statements of income, changes in shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2006. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). 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 examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes 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 German American Bancorp, Inc. as of December 31, 2006 and 2005, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2006 in conformity with U.S. generally accepted accounting principles.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company's internal control over financial reporting as of December 31, 2006, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 27, 2007 expressed an unqualified opinion thereon.

Louisville, Kentucky — /s/ Crowe Chizek and Company LLC
February 27, 2007 — Crowe Chizek and Company LLC

Consolidated Balance Sheets
Dollars in thousands, except per share data

	December 31, 2006	December 31, 2005
ASSETS		
Cash and Due from Banks	**$ 23,960**	$ 27,644
Federal Funds Sold and Other Short-term Investments	**5,735**	5,287
Cash and Cash Equivalents	**29,695**	32,931
Interest-bearing Time Deposits with Banks	**200**	—
Securities Available-for-Sale, at Fair Value	**179,222**	181,150
Securities Held-to-Maturity, at Cost (Fair value of $6,192 and $8,811 on December 31, 2006 and 2005, respectively)	**6,135**	8,684
Loans Held-for-Sale	**1,601**	1,901
Loans	**798,635**	653,514
Less: Unearned Income	**(2,376)**	(1,558)
Allowance for Loan Losses	**(7,129)**	(9,265)
Loans, Net	**789,130**	642,691
Stock in FHLB of Indianapolis and Other Restricted Stock, at Cost	**10,621**	14,095
Premises, Furniture and Equipment, Net	**23,245**	20,233
Other Real Estate	**845**	506
Goodwill	**9,655**	3,813
Intangible Assets	**4,924**	2,388
Company Owned Life Insurance	**21,710**	19,067
Accrued Interest Receivable and Other Assets	**16,441**	19,008
TOTAL ASSETS	**$ 1,093,424**	$ 946,467
LIABILITIES		
Non-interest-bearing Demand Deposits	**$ 137,671**	$ 130,383
Interest-bearing Demand, Savings, and Money Market Accounts	**329,690**	307,007
Time Deposits	**400,257**	309,431
Total Deposits	**867,618**	746,821
FHLB Advances and Other Borrowings	**119,889**	105,394
Accrued Interest Payable and Other Liabilities	**13,526**	11,997
TOTAL LIABILITIES	**1,001,033**	864,212
SHAREHOLDERS' EQUITY		
Preferred Stock, $10 par value; 500,000 shares authorized, no shares issued	—	—
Common Stock, no par value, $1 stated value; 20,000,000 shares authorized	**11,008**	10,643

Additional Paid-in Capital	**68,216**	63,784
Retained Earnings	**13,450**	9,391
Accumulated Other Comprehensive Loss	**(283**)	(1,563)
TOTAL SHAREHOLDERS' EQUITY		