EYI INDUSTRIES INC.
Form 10QSB
November 20, 2006

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

FORM 10-QSB

x Quarterly Report under Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended **September 30, 2006**

¨ Transition Report under Section 13 or 15(d) of the Exchange Act

For the transition period from __________ to __________

Commission File Number: **000-29803**

EYI INDUSTRIES, INC.
(Exact name of small business issuer as specified in its charter)

NEVADA	**88-0407078**
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)
7865 Edmonds Street **Burnaby, BC CANADA**	**V3N 1B9**
(Address of principal executive offices)	(Zip Code)
Issuer's telephone number:	**(604) 759-5031**

NOT APPLICABLE
(Former name, former address and former fiscal year end, if changed since last report)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 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:

Yes x No ¨

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

State the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 336,267,350 shares of common stock issued and outstanding as of November 17, 2006.

Transitional Small Business Disclosure Format (check one): Yes ¨ No x

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

The accompanying unaudited financial statements have been prepared in accordance with the instructions to Form 10-QSB and Item 310(b) of Regulation S-B, and, therefore, do not include all information and footnotes necessary for a complete presentation of financial position, results of operations, cash flows, and stockholders' equity in conformity with accounting principles generally accepted in the United States of America. In the opinion of management, all adjustments considered necessary for a fair presentation of the results of operations and financial position have been included and all such adjustments are of a normal recurring nature. Operating results for the nine month period ended September 30, 2006 are not necessarily indicative of the results that can be expected for the year ending December 31, 2006.

As used in this quarterly report, the terms "we", "us", "our", “EYI” and "our company" mean EYI Industries, Inc. and its subsidiaries unless otherwise indicated. All dollar amounts in this quarterly report are in U.S. dollars unless otherwise stated.

EYI INDUSTRIES, INC.
CONSOLIDATED BALANCE SHEETS

	September 30, 2006 (Unaudited)	December 31, 2005
ASSETS		
CURRENT ASSETS		
Cash	$ 1,879,075	$ 25,639
Accounts receivable, net of allowance	36,193	48,783
Related party receivables	31,250	-
Prepaid expenses	97,795	12,387
Inventory	511,625	295,248
TOTAL CURRENT ASSETS	2,555,938	382,057
OTHER ASSETS		
Property, plant and equipment, net	75,714	49,671
Deposits	26,011	67,603
TOTAL OTHER ASSETS	101,725	117,274
INTANGIBLE ASSETS	13,387	15,044
TOTAL ASSETS	$ 2,671,050	$ 514,375
LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)		
CURRENT LIABILITIES		
Accounts payable and accrued liabilities	$ 1,374,522	$ 1,929,049
Accounts payable - related parties	460,149	328,038
Convertible debt - related party, net of discount	2,549,263	-
Derivative on convertible debt	1,354,824	-
Interest payable, convertible debt	149,681	-
Notes payable - related party	50,000	90,000
TOTAL CURRENT LIABILITIES	5,938,439	2,347,087
Net liabilities from discontinued operations	375,344	375,344
COMMITMENTS AND CONTINGENCIES MINORITY INTEREST IN SUBSIDIARY	140,813	262,057
STOCKHOLDERS' EQUITY (DEFICIT)		
Preferred stock, $0.001 par value; 10,000,000 shares authorized, no shares issued and outstanding	-	-
Common stock, $0.001 par value; 3,000,000,000 shares authorized, 294,011,932 and 217,600,875 shares issued and outstanding, respectively	294,011	217,600
Additional paid-in capital	9,114,960	6,155,518
Stock options and warrants	4,446,082	2,698,984
Subscription receivable	(195,000)	(195,000)
Accumulated deficit	(17,443,599)	(11,347,215)

TOTAL STOCKHOLDERS' EQUITY (DEFICIT)		(3,783,546)		(2,470,113)
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)	$	2,671,050	$	514,375

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EYI INDUSTRIES, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended September 30, 2006 (Unaudited)	Three Months Ended September 30, 2005 (Unaudited)	Nine Months Ended September 30, 2006 (Unaudited)	Nine Months Ended September 30, 2005 (Unaudited)
REVENUE, NET OF RETURNS AND ALLOWANCES	$ 949,429	$ 1,335,963	$ 3,068,166	$ 3,850,246
COST OF GOODS SOLD	268,763	350,188	947,611	840,125
GROSS PROFIT BEFORE COMMISSION EXPENSE	680,666	985,775	2,120,555	3,010,121
COMMISSION EXPENSE	355,556	513,449	1,120,273	1,435,911
GROSS PROFIT AFTER COST OF GOODS SOLD AND COMMISSION EXPENSE	325,110	472,326	1,000,282	1,574,210
OPERATING EXPENSES				
Consulting fees	259,639	273,026	743,738	751,836
Legal and professional fees	266,908	107,333	428,150	254,090
Customer service	62,718	9,771	169,721	161,776
Finance and administration	214,835	299,735	643,529	663,213
Sales and marketing	59,339	42,569	271,631	47,560
Telecommunications	32,930	118,881	97,955	361,139
Wages and benefits	264,899	252,095	864,292	995,247
Warehouse expense	98,995	66,220	229,668	128,066
TOTAL OPERATING EXPENSES	1,260,263	1,169,630	3,448,684	3,362,927
LOSS FROM OPERATIONS	(935,153)	(697,304)	(2,448,403)	(1,788,717)
OTHER INCOME (EXPENSES)				
Interest and other income	2,162	158	2,405	3,625
Interest expense	(117,803)	(103,581)	(174,537)	(158,159)
Financing fees	(285,534)	30,318	(592,471)	-
Loss on derivatives	(1,731,034)	-	(3,026,542)	-
Foreign currency gain (discount)	5,587	-	21,919	(119,169)
TOTAL OTHER INCOME (EXPENSES)	(2,126,622)	(73,105)	(3,769,226)	(273,703)
NET LOSS BEFORE TAXES	(3,061,775)	(770,409)	(6,217,628)	(2,062,420)
PROVISION FOR INCOME TAXES	-	-	-	-
NET LOSS BEFORE ALLOCATION TO MINORITY INTEREST	(3,061,775)	(770,409)	(6,217,628)	(2,062,420)
ALLOCATION OF LOSS TO MINORITY INTEREST	59,705	14,886	121,244	47,635
ALLOCATION OF LOSS TO DISCONTINUED OPERATIONS	-	7,093	-	(380,368)
NET LOSS	$ (3,002,070)	$ (748,430)	(6,096,384)	$ (2,395,153)
BASIC AND DILUTED NET LOSS PER COMMON SHARE	$ nil	$ (0.01)	$ nil	$ (0.02)

WEIGHTED AVERAGE NUMBER OF COMMON STOCK SHARES OUTSTANDING FOR BASIC AND DILUTED CALCULATION	286,014,193	172,702,928	286,014,193	168,678,060

The accompanying condensed notes are an integral part of these financials

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EYI INDUSTRIES, INC.
CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY (DEFICIT)

	Common Stock		Additional				
	Number of Shares	Amount	Paid-in Capital	Subscription Receivable	Option/ Warrants	Accumulated Deficit	Total
Balance December 31, 2004	162,753,292	$ 162,753	$ 3,048,606	$ (15,000)	$ 2,563,044	$ (7,085,205)	$ (1,325,802)
Stock issued at $0.06 per Share for promissory note for exercise of options	3,000,000	3,000	177,000	(180,000)	-	-	-
Vested stock options issued for consulting at an average price of $0.07 per share	-	-	-	-	35,250	-	35,250
Vested stock options issued for employee compensation at an average price of $0.07 per share	-	-	-	-	133,750	-	133,750
Stock issued to employee for financing guaranty & pledge valued at $0.05 per share	800,000	800	39,200	-	-	-	40,000
Consultant-options exercised	250,000	250	14,750	-	(5,000)	-	10,000
Gladys Sargeant 506 Subscription Agreement	1,000,000	1,000	4,000	-	15,000	-	20,000
Vested stock option issued for consulting at an average price of $0.03 per share	-	-	-	-	62,250	-	62,250
Cancelled stock options issued for compensation and consulting at an average price of $0.08	-	-	425,300	-	(425,300)	-	-

per option							
Cancelled stock options issued for compensation at $0.20	-	-	2,400	-	(2,400)	-	-
Stock issued to TAIB Bank to retire $75,000 of $300,000 debenture	2,027,027	2,027	72,973	-	-	-	75,000
Stock issued to TAIB Bank to retire $170,000 of $300,000 debenture plus interest of $10,830	4,487,096	4,487	176,343	-	-	-	180,830
Stock issued to TAIB Bank to retire $5,000 debenture plus interest of $14,245	375,146	375	18,870	-	-	-	19,245
Stock issued to Agora as part of contract	250,000	250	12,250	-	-	-	12,500
Stock issued to Consultant as part of contract	500,000	500	34,500	-	-	-	35,000
Stock issued for exercise of options at $0.08 per share	100,000	100	7,900	-	-	-	8,000
Stock issued to Cornell to retire prom note	22,789,581	22,789	1,008,099	-	-	-	1,030,888
Vested stock options issued for consulting at an average price of $0.20 per share	-	-	-	-	33,500	-	33,500
Vested stock options issued for employee and management compensation at an average price of $0.20 per share	-	-	-	-	27,840	-	27,840
Stock issued to Cornell in exchange for $700,000 pursuant	19,268,733	19,269	680,731	-	-	-	700,000

to SEDA							
Cancelled stock options issued for compensation	-	-	10,500	-	(10,500)	-	-
Vested stock options for consulting at an average price of $0.20 per share	-	-	-	-	271,550	-	271,550
Beneficial conversion of convertible debt	-	-	422,096	-	-	-	422,096
Net loss for year ended December 31, 2005	-	-	-	-	-	(4,262,010)	(4,262,010)
Balance, December 31, 2005	217,600,875	$ 217,600	$ 6,155,518	$ (195,000)	$ 2,698,984	(11,347,215)	$ (2,470,113)
Vested stock options issued for consulting at an average price of $0.20 per share	-	-	-	-	3,750	-	3,750
Stock issued to Cornell in exchange for $1,084,565 pursuant to the SEDA	42,941,686	42,942	1,041,623	-	-	-	1,084,565
Shares returned to treasury	(268,639)	(269)	269	-	-	-	-
Beneficial conversion of convertible debt	-	-	200,207	-	-	-	200,207
Stock issued to Cornell to retire portion of debenture	1,497,006	1,497	23,503	-	-	-	25,000
Stock issued to Certain Wealth to retire portion of debenture	664,671	665	10,435	-	-	-	11,100
Stock issued to TAIB Bank to retire portion of debenture	832,335	832	13,068	-	-	-	13,900
Warrants issued to Cornell Capital for	-	-	-	-	3,148,413	-	3,148,413

financing services							
Vested stock options for consulting at $0.10 per share	-	-	-	-	5,000	-	5,000
Vested stock options issued to employees at $0.02 per share	-	-	-	-	1,400	-	1,400
Expired Consultant stock options	-	-	961,300	-	(961,300)	-	-
Expired employee stock options	-	-	311,717	-	(311,717)	-	-
Stock issued to Cornell to retire portion of debenture	15,371,998	15,372	95,864	-	-	-	111,236
Stock issued to Certain Wealth to retire portion of debenture	6,825,244	6,825	42,331	-	-	-	49,156
Stock issued to TAIB Bank to retire portion of debenture	8,546,756	8,547	53,033	-	-	-	61,580
Vested stock options issued to employees at $0.06 per share	-	-	-	-	40	-	40
Expired consultant stock options	-	-	38,500	-	(38,500)	-	-
Expired employee stock options	-	-	99,988	-	(99,988)	-	-
Beneficcial conversion of convertible debt	-	-	67,604	-			67,604
Net loss for period ended September 30, 2006	-	-	-	-	-	(6,096,384)	(6,096,384)
Balance September 30, 2006 (Unaudited)	294,011,932	$ 294,011	$ 9,114,960	$ (195,000)	$ 4,446,082	$ (17,443,599)	(3,783,546)

The accompanying condensed notes are an integral part of these financials

EYI INDUSTRIES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Nine Months Ended September 30, 2006 (Unaudited)	Nine Months Ended September 30, 2005 (Unaudited)
CASH FLOWS PROVIDED (USED) BY OPERATING ACTIVITIES		
Net loss	$ (6,096,383)	$ (2,395,153)
Loss allocated to minority interest	121,244	47,635
	$ (6,217,627)	(2,442,778)
Adjustments to reconcile net loss		
to net cash used by operating activities:		
Depreciation and amortization	16,007	52,504
Stock and warrants issued for employee compensation and consulting	10,190	292,590
Stock issued for options exercised in lieu of debt	-	11,500
Stock issued for options exercised in lieu of consulting and legal fees	-	57,500
Stock issued for interest on convertible debt	-	44,570
Loss (gain) on valuation of derivative	3,026,541	-
Stock issued for financing guaranty & pledge	-	40,000
Beneficial conversion of convertible debt	267,811	-
Discount recognized on convertible debt	267,931	120,276
Liabilities in excess of assets on discontinued operations	-	(30,494)
Decrease (increase) in:		
Related party receivables	(31,250)	(800)
Accounts receivable	12,590	(7,874)
Prepaid expenses	(85,408)	287,187
Inventory	(216,377)	11,159
Deposits	41,592	(45,925)
Increase (decrease) in:		
Accounts payable and accrued liabilities	(554,527)	352,495
Accounts payable - related parties	132,111	535,548
Notes payable, related party	(40,000)	-
Interest payable	-	(10,616)
Interest payable, convertible debt	149,681	-
Net cash used by operating activities	(3,220,736)	(733,168)
CASH FLOWS PROVIDED (USED) BY INVESTING ACTIVITIES		
Decrease (increase) in restricted cash	-	100,248
Decrease (increase) in property, plant, and equipment	(40,393)	(50,505)
Purchase of trademarks and formulas	-	(674)
Net cash provided by investing activities	(40,393)	49,069
CASH FLOWS PROVIDED (USED) BY FINANCING ACTIVITIES		
Net change in bank indebtedness	-	(72,456)
Issuance of stock, net of private placement costs & warrants	-	16,500
Proceeds from Cornell SEDA	1,084,565	-
Repayment of convertible debt	-	(250,000)
Proceeds from Cornell Promissory Note	-	1,000,000
Net proceeds from convertible debt	4,030,000	-
Net cash provided by financing activities	5,114,565	694,044

Net increase in cash and cash equivalents		1,853,436		9,946
CASH - Beginning of Year		25,639		-
CASH - End of Period	$	1,879,075	$	9,946
SUPPLEMENTAL CASH FLOW DISCLOSURES:				
Interest expense paid	$	174,537	$	158,159
Income taxes paid	$	-	$	-
NON-CASH INVESTING AND FINANCING TRANSACTIONS:				
Stock options and warrants vested for consulting and compensation	$	10,190	$	-
Beneficial conversion of convertible debt	$	267,811	$	-
Gain on valuation of derivative	$	(3,026,541)	$	-
Discount recognized on convertible debt	$	267,931	$	120,276
Stock issued for options exercised in lieu of debt	$	-	$	11,500
Stock issued for options exercised in lieu of consulting and legal fees	$	-	$	57,500
Stock options vested for consulting and compensation	$	-	$	292,590
Stock issued for options exercised in lieu of legal fees	$	-	$	10,000
Stock issued to retire part of promissory note	$	-	$	175,000
Stock issued for redemption of convertible debenture	$	-	$	250,000
Stock issued for interest on convertible debenture	$	-	$	44,570
Stock and warrants issued through 506 Private Placement	$	-	$	20,000
Stock issued for financing guaranty & pledge	$	-	$	40,000

The accompanying condensed notes are an integral part of these financials

EYI INDUSTRIES, INC.
CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2006

NOTE 1 - DESCRIPTION OF BUSINESS

Essentially Yours Industries, Inc. ("EYI") was incorporated on June 21, 2002 in the State of Nevada. The main business activities of Essentially Yours Industries, Inc. were acquired through a merger with the former entity, Burrard Capital, Inc., and other entities concerning EYI's reorganization. On December 31, 2003, EYI entered into a share exchange agreement of its stock with Safe ID Corporation ("Safe ID"). This transaction was accounted for as a share exchange and recapitalization. As a result of this transaction, Safe ID changed its name to EYI Industries, Inc. ("the Company") and is acting as the parent holding company for the operating subsidiaries.

The principal business of the Company is the marketing of health and wellness care products. The Company sells its products primarily through network marketing distributors, which in turn sell the products to the end customers. The Company also sells product directly and through affiliates. The Company maintains its principal business office in Burnaby, British Columbia. Effective for the period ended December 31, 2003, the Company elected to change its year-end from June 30 to December 31.

The Company has six wholly owned subsidiaries. The first subsidiary is Halo Distribution LLC ("Halo"), which was organized on January 15, 1999 in the State of Kentucky. Halo was the distribution center for the Company's product, in addition to other products, until April 30, 2005 at which time the Company made the decision to discontinue its operations. Halo was dissolved on November 1, 2005. The second subsidiary is RGM International Inc., which was incorporated on July 3, 1997, in the State of Nevada. RGM International Inc. is a dormant investment company which owns one percent of Halo. The third subsidiary is Essentially Yours Industries (Canada) Inc. (hereinafter "EYI Canada"), which was incorporated on September 13, 2002 under the *Canada Business Corporations Act*. EYI Canada markets health and wellness care products for use in Canada. The fourth subsidiary is 642706 B.C. Ltd., doing business as EYI Management, which was organized on February 22, 2002 in the province of British Columbia, Canada. EYI Management provides accounting, customer service and marketing services to the consolidated entity. The fifth subsidiary is Essentially Yours Industries (Hong Kong) Limited ("EYI HK"). EYI HK was organized on August 23, 2005 in Hong Kong. EYI HK markets health and wellness care products for use in Hong Kong and China. The sixth subsidiary is Essentially Yours Industries (International) Limited ("EYI INTL"). EYI INTL was organized on December 6, 2005 to facilitate our expansion throughout other Southeast Asian countries.

In addition, the Company owns approximately 98% of Essentially Yours Industries, Inc. ("EYI"), incorporated on June 21, 2002 in the State of Nevada. EYI markets health and wellness care products for use in USA. The Company also owns 51% of World Wide Buyers' Club Inc. ("WWBC"), a Nevada corporation, which was organized by a joint venture agreement effective May 6, 2004.

<u>Basis of Presentation</u>

The accompanying interim condensed financial statements are prepared in accordance with rules set forth in Regulation SB of the Securities and Exchange Commission. As said, these statements do not include all disclosures required under generally accepted principles and should be read in conjunction with the audited financial statements for the year ended December 31, 2005. In the opinion of management, all required adjustments which consist of normal re-occurring accruals have been made to the financial statements.

The preparation of financial statements in accordance with generally accepted accounting principles requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities known to exist as of the date the financial statements are published, and the reported amounts of revenues and expenses during the reporting period. Uncertainties with respect to such estimates and assumptions are inherent in the preparation of the Company's financial statements. Accordingly, it is possible that the actual results could differ from these estimates and assumptions that could have a material effect on the reported amounts of the Company's financial position and results of operations.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING PRINCIPLES

This summary of significant accounting policies of EYI Industries, Inc., is presented to assist in understanding the Company's financial statements. The financial statements and notes are representations of the Company's management, which is responsible for their integrity and objectivity. These accounting policies conform to accounting principles generally accepted in the United States of America, and have been consistently applied in the preparation of the financial statements.

Concentration of Credit Risk

The Company maintains its cash in one commercial bank. Although the financial institution is considered creditworthy, at September 30, 2006 the Company's cash balance exceeded Federal Deposit Insurance Corporation (FDIC) limits by $1,768,624 (see Note 13).

Derivative Instruments

The Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" (hereinafter "SFAS No. 133"), as amended by SFAS No. 137, "Accounting for Derivative Instruments and Hedging Activities - Deferral of the Effective Date of FASB No. 133", and SFAS No. 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities", and SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities". These statements establish accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. They require that an entity recognize all derivatives as either assets or liabilities in the balance sheet and measure those instruments at fair value.

If certain conditions are met, a derivative may be specifically designated as a hedge, the objective of which is to match the timing of gain or loss recognition on the hedging derivative with the recognition of (i) the changes in the fair value of the hedged asset or liability that are attributable to the hedged risk or (ii) the earnings effect of the hedged forecasted transaction. For a derivative not designated as a hedging instrument, the gain or loss is recognized in income in the period of change.

The Company has determined that derivatives existed because of features of the convertible debt as of the balance sheet date of September 30, 2006 (See Note 4.)

Fair Value of Financial Instruments

The Company's financial instruments as defined by Statement of Financial Accounting Standards No. 107, "Disclosures about Fair Value of Financial Instruments," include cash, trade accounts receivable, and accounts payable and accrued expenses. All instruments are accounted for on a historical cost basis, which, due to the short maturity of these financial instruments, approximates fair value at September 30, 2006 and December 31, 2005.

Inventory

The Company records inventories at the lower of cost or market on a first-in, first-out basis. The Company's product inventory is reviewed each month and also when the re-order of the product is necessary. On a monthly basis, the Company's inventory is reviewed based on the expiration of our existing inventory. Product that has a shelf-life of less than 60 days is written off or discounted. The Company expensed $48,981 and $6,494 for the nine months ended September 30, 2006 and twelve months ended December 31, 2005 respectively.

A re-order review consists of an evaluation of the Company's current monthly sales volume of the product, cost of product, shelf-life of the product, and the manufacturers minimum purchase requirement, which all determine the overall potential profitability or loss of re-ordering. If the re-order of the product has an assessed loss, then the recommendation to management is to remove the product from the product line.

Revenue Recognition

The Company is in the business of selling nutritional products in three categories: dietary supplements, personal care products, and water filtration systems. Sales of personal care products and water filtration systems represent less than 5% of the overall revenue and therefore are not classified separately in the financial statements. The Company recognizes revenue from product sales when the products are shipped and title passes to the customer. Administrative fees charged to the Independent Business Associates are included in the gross sales and amounted to $32,620 and $26,370 for the three months ended September 30, 2006 and September 30, 2005 respectively.

Stock Options and Warrants Granted to Employees and Non-Employees

Statement of Financial Accounting Standards No. 123R, "Accounting for Stock-Based Compensation" ("SFAS No. 123R"), defines a fair value-based method of accounting for stock options and other equity instruments. The Company has adopted this method, which measures compensation costs based on the estimated fair value of the award and recognizes that cost over the service period.

Going Concern

As shown in the accompanying financial statements, the Company had negative working capital of approximately $3,382,501 and an accumulated deficit at September 30, 2006. The Company also has a history of recurring losses. These factors raise substantial doubt about the Company's ability to continue as a going concern. The financial statements do not include any adjustments relating to the recoverability and classification of recorded assets, or the amounts and classification of liabilities that might be necessary in the event the Company cannot continue in existence.

Management has established plans designed to increase the sales of the Company's products and decrease debt. The Company plans on continuing to reduce expenses, and with small gains in any combination of network sales, direct sales, international sales, and warehouse sales, believe that they will eventually be able to reverse the present deficit. Management intends to seek additional capital from new equity securities offerings that will provide funds needed to increase liquidity, fund internal growth and fully implement its business plan. Management plans include negotiations to convert significant portions of existing debt into equity.

The timing and amount of capital requirements will depend on a number of factors, including demand for products and services and the availability of opportunities for international expansion through affiliations and other business relationships.

NOTE 3 - CONVERTIBLE DEBT

On April 24, 2006 the Company entered into a Securities Purchase Agreement with Cornell, TAIB Bank, and Certain Wealth (collectively the "Buyers" and together with the Company, the "Parties"). Pursuant to the Securities Purchase Agreement, the Company shall sell to the Buyers, and the Buyers shall purchase from the Company, convertible debentures in the aggregate principal amount of Four Million Five Hundred Thousand Dollars ($4,500,000), plus accrued interest, which are convertible into shares of the Company's common stock, par value $0.001 per, at the Buyers discretion. Of this aggregate amount, (a) One Million Five Hundred Thousand Dollars ($1,500,000) was funded on April 28, 2006, (b) One Million Five Hundred Thousand Dollars ($1,500,000) was funded two (2) business days prior to the date the registration statement ("Registration Statement") was filed with the U.S. Securities and Exchange Commission ("SEC") and (c) One Million Five Hundred Thousand Dollars ($1,500,000) was funded two (2) business days prior to the date that such Registration Statement is declared effective by the SEC.

The Debentures mature on April 24, 2009, accrue interest at an annual rate of ten percent (10%) and shall be convertible into shares of the Company's common stock at the option of the holder, in whole or in part at any time and from time to time, at a conversion price equal to (a) $0.06 or (b) eighty percent (80%) of the lowest Volume Weighted Average Price of the Company's common stock during the five (5) trading days immediately preceding the date of conversion as quoted by Bloomberg, LP. During the quarter ended September 30, 2006, the Company recognized embedded derivatives in the convertible debentures. (See Note 4.)

The Company also executed a registration rights agreement pursuant to which the Company agreed to provide certain registration rights to the Investors. The Parties have also executed a Security Agreement, pursuant to which the Company has agreed to provide to the Buyers, a security interest in Pledged Collateral to secure the Company's obligations under the Debentures, the Securities Purchase Agreement, the Investor Registration Rights Agreement, the Irrevocable Transfer Agent Instructions, the Security Agreement, or any other obligations of the Company to the Buyer.

On April 24, 2006 the Company issued to Cornell seventeen (17) warrants to purchase up to an aggregate 124,062,678 shares of the Company's common stock at $0.02 and $0.40 per share. Each Warrant has "piggy back" registration rights and shall expire five (5) years from the date of issuance, on or about April 24, 2011. Following EITF 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settle in, a Company's Own Stock," and SFAS No. 133, the Company has recognized an embedded equity derivative in the warrant. For accounting and fair value purposes, the equity derivative will be accounted for as a stock option, following SFAS No. 123(R) for valuation purposes. (See Note 9.)

NOTE 4 - DERIVATIVES

Derivatives have been accounted for in accordance with SFAS 133, as amended, and EITF No. 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock." The Company has identified that the debentures described in Notes 3 and 5 have embedded derivatives. These embedded derivatives have been bifurcated from their respective host debt contracts and accounted for as derivative liabilities in accordance with EITF 00-19. When multiple derivatives exist within the loan agreements, they have been bundled together as a single hybrid compound instrument in accordance with SFAS No. 133, Derivatives Implementation Group Implementation Issue No. B-15, "Embedded Derivatives: Separate Accounting for Multiple Derivative Features Embedded in a Single Hybrid Instrument".

The embedded derivatives within the loan agreements have been recorded at fair value at the date of issuance and are marked-to-market each reporting period with changes in fair value recorded on the Company's income statement as gain (loss) on derivatives.

The fair value of the derivative liabilities are subject to the changes in the trading value of the Company's common stock, as well as other factors. As a result, the Company's financial statements may fluctuate from quarter-to-quarter based on factors such as the price of the Company's stock at the balance sheet date and the amount of shares converted by note holders. Consequently, the Company's financial position and results of operations may vary from quarter-to-quarter based on conditions other than its operating revenues and expenses.

The initial fair value of the derivative embedded in the April 2006 $1,500,000 convertible debenture was $1,093,089 and at June 30, 2006 the embedded derivative was revalued to its fair value of $725,565. The initial fair value of the derivative embedded in the June 8, 2006 $1,500,000 convertible debenture was $842,338 and at June 30, 2006 the embedded derivative was revalued to its fair value of $725,565. The initial fair value of the derivative embedded in the June 20, 2006 $1,500,000 convertible debenture was $865,425 and at June 30, 2006 the embedded derivative was revalued to its fair value of $725,565. Any change to the fair value of the derivatives is recognized on the income statement and recorded as gain/(loss) on derivatives. At June 30, 2006 the Company recognized an increase in the fair value of the derivatives of $624,157 and a corresponding gain on derivatives on the consolidated statements of operation.

At September 30, 2006, the Company revalued the derivative embedded in each of the three convertible debentures at $440,275 each or a total of $1,320,825. As a result, the Company recognized a corresponding gain of $855,870.

At September 30, 2006, the Company also calculated a marked-to-market adjustment for the warrants issued to Cornell Capital in connection with the convertible debenture. The Company recognized a loss of $3,244,046 as a result of this valuation.

NOTE 5 - ACCOUNTS RECEIVABLE AND CREDIT RISK

Accounts receivable at September 30, 2006 and December 31, 2005 consist primarily of amounts due from direct retail clients of EYI.

NOTE 6 - PROPERTY AND EQUIPMENT

Capital assets are recorded at cost. Depreciation is calculated using the straight line method over three to seven years.

NOTE 7 - INTANGIBLE ASSETS

Intangible assets consist of rights, title, and interest in and to the contracts with the Company’s independent business associates, as well as the rights and licenses to trademarks and formula for the Company’s primary products. These rights and licenses were obtained from the Company’s former parent, pursuant to a transfer agreement, as well as from the Company’s primary shareholder.

Trademarks and Formulas

Costs relating to the purchase of trademarks and formulas were capitalized and amortized using the straight-line method over ten years, representing the estimated life of the assets.

NOTE 8 - CAPITAL STOCK

Preferred Stock

The Company is authorized to issue 10,000,000 shares of preferred stock with a par value of $0.001. As of September 30, 2006 and December 31, 2005 the Company has not issued any preferred stock.

Common Stock

The Company is authorized to issue 3,000,000,000 shares of common stock. All shares have equal voting rights, are non-assessable and have one vote per share. Voting rights are not cumulative and, therefore, the holders of more than 50% of the common stock could, if they choose to do so, elect all of the directors of the Company.

Between January 1, 2006 and March 31, 2006, the Company issued 42,941,686 shares to Cornell Capital in exchange for $1,084,565.

On February 6, 2006 the Jay Sargeant Trust was dissolved and the related shares were disbursed to the beneficiaries. In connection with this transaction, 268,639 common shares were returned to treasury at par value.

On June 27, 2006, The Company issued 1,497,006 common shares to Cornell Capital to retire $25,000 of the convertible debt.

On June 27, 2006, The Company issued 664,671 common shares to Certain Wealth to retire $11,100 of the convertible debt.

On June 27, 2006, The Company issued 832,335 common shares to TAIB Bank to retire $13,900 of the convertible debt.

Between July 1, 2006 and September 30, 2006, the Company issued 15,371,998 shares to Cornell Capital to retire $111,236 of the convertible debt.

Between July 1, 2006 and September 30, 2006, the Company issued 6,825,244 shares to Certain Wealth to retire $49,156 of the convertible debt.

Between July 1, 2006 and September 30, 2006, the Company issued 8,546,756 shares to TAIB Bank to retire $61,580 of the convertible debt.

NOTE 9 - COMMON STOCK OPTIONS AND WARRANTS

Financial Accounting Standards No. 123R, "Accounting for Stock-Based Compensation" (hereinafter "SFAS No. 123R"), defines a fair value-based method of accounting for stock options and other equity instruments. The Company has adopted this method, which measures compensation costs based on the estimated fair value of the award and recognizes that cost over the service period.

In accordance with SFAS No. 123R, the fair value of stock options and warrants granted are estimated using the Black-Scholes Option Price Calculation. The following assumptions were made to value the warrants for the period ended September 30, 2006: estimated risk-free interest rate of 5.125%; no dividends to be paid; estimated volatility of 140% and term of five years.

<u>Stock Options</u>

During the year ending December 31, 2004, the Company’s board of directors approved the Stock Compensation Program to allow up to 25,000,000 shares of stock to be issued under the program. This plan enables the Company to grant stock options to directors, officers, employees and eligible consultants of the Company. There was no Company stock option plan in effect prior to 2004.

During the three months ended September 30, 2006, the Company recognized an expense to wages of $40 for all vested options.

Following is a summary of the status of the stock options during the nine months:

	Number of Shares		Weighted Average Exercise Price
Outstanding at December 31, 2005	16,252,390	$	0.14
Granted	20,000		0.06
Exercised	-		-
Forfeited or cancelled	9,562,390		-
Options outstanding at September 30, 2006	6,710,000	$	0.10
Options exercisable at September 30, 2006	6,640,000	$	0.10
Weighted average fair value of options granted		$	0.06

Summarized information about stock options outstanding and exercisable at September 30, 2006 is as follows:

	Options Outstanding			
Exercise Price Range	Number of Shares	Weighted Ave. Remaining Life		Weighted Ave. Exercise Price
$0.02 - $0.26	6,710,000	0.76	$	0.09

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	Options Exercisable			
Exercise Price Range	Number of Shares	Weighted Ave. Remaining Life		Weighted Ave. Exercise Price
$0.02 - $0.26	6,640,000	0.75	$	0.10

Summarized information about non-vested but granted stock options outstanding at September 30, 2006 is as follows:

	Non-vested Granted Options Outstanding			
Exercise Price Range	Number of Shares	Weighted Ave. Remaining Life		Weighted Ave. Exercise Price
$0.02 - $0.10	70,000	1.16	$	0.02

Warrants

In consideration of the Convertible Debenture (See Note 3), the Company has also issued an aggregate of 124,062,678 common stock purchase warrants dated April 24, 2006 to Cornell, each exercisable for a period of five years commencing April 24, 2006 for the purchase of one share of common stock. The warrants provide that the holder cannot exercise the warrants to the extent such exercise would cause the holder and its affiliates to own more than 4.99% of our outstanding common shares. The warrants have exercise prices, subject to adjustment, ranging from $0.02 to $0.40 per share. Each Warrant has “piggy back’ registration rights and shall expire five (5) years for the date of issuance, on or about April 24, 2011.

	Number of Warrants	Weighted Average Remaining Life		Average Exercise Price
Outstanding and exercisable	129,538,868	4.56	$	0.09

NOTE 10 - COMMITMENTS AND CONTINGENCIES

<u>Joint Venture Agreement</u>

On August 12, 2006 we entered into a joint venture agreement with Internet Marketing Consortium to provide multi media strategies, promotional, direct and targeted marketing services for an undetermined period of time. In consideration for the services provided by IMC, we paid a fee of $25,000.

<u>Purchase Agreement</u>

On June 30, 2002, EYI entered into a distribution and license agreement with a company in which one of EYI's directors has an ownership interest. The agreement gives EYI the exclusive right to market, sell and distribute certain products for a five-year renewable term. Management estimates that 87% of EYI's sales volume results from products supplied under this licensing agreement.

Pursuant to the agreement, EYI is required to purchase a minimum amount of $6,035,000 of product in each of the remaining years.

In the event that EYI is unable to meet the minimum purchase requirements of the licensing agreement or the terms requiring it to pay 15% of the difference between the minimum purchase amount referred to above and actual purchases for that year in which there is a shortfall, then the licensor has various remedies available to it including renegotiating the agreement, removing exclusivity rights, or terminating the agreement.

As of the date of these financial statements, the purchase requirements have not been made. The period for which the Licensor could request payment per the penalty clause has expired for the year and therefore we have not made any accrual to the Financial Statements. EYI continues to purchase Nutri Diem products on a regular basis.

Lease Payments

The Company has operating lease commitments for its premises and office equipment. The minimum annual lease commitments are as follows:

Year ended December 31,	Minimum Amount
2006	$ 218,679
2007	164,546
2008	143,101
2009	148,064
2010 and thereafter	309,544

Regulatory Risks and Claims

The Company's products are subject to regulation by a number of federal and state entities, as well as those of foreign countries in which the Company's products are sold. These regulatory entities may prohibit or restrict the sale, distribution, or advertising of the Company's products for legal, health or safety related reasons. In addition to the potential risk of adverse regulatory actions, the Company is subject to the risk of potential product liability claims.

Standby Equity Distribution Agreement

On May 13, 2005 the Company entered into a Standby Equity Distribution Agreement with Cornell Capital Partners, LP ("Cornell") pursuant to which we entered into the following agreements: a Registration Rights Agreement, an Escrow Agreement, and a Placement Agent Agreement. Pursuant to the terms of the new Standby Equity Distribution Agreement, we may, at our discretion, periodically issue and sell shares of our common stock for a total purchase price of $10 million. If we request advances under the Standby Equity Distribution Agreement, Cornell will purchase shares of our common stock for 98% of the lowest volume weighted average price on the Over-the-Counter Bulletin Board or other principal market on which our common stock is traded for the 5 days immediately following the advance notice date. Cornell will retain 5% of each advance under the new Standby Equity Distribution Agreement. We may not request advances in excess of a total of $10 million. Pursuant to the terms of our Registration Rights Agreement and the Standby Equity Agreement with Cornell, we agreed to register and qualify, among other things, the additional shares due to Cornell under the Standby Equity Agreement under a registration statement filed with the SEC.

On April 3, 2006 we signed a Termination Agreement with Cornell Capital Partners, L.P for the purpose of terminating our Standby Equity Distribution Agreement, Registration Rights Agreement and Escrow Agreement all of which are dated as of May 13, 2005.

Other Matters

The Company's predecessor organization, Essentially Yours Industries Corp. ("EYIC"), a British Columbia corporation, has outstanding claims from the Internal Revenue Service for penalties and interest of approximately $2,000,000. Furthermore, one or more states may have claims against EYIC for unpaid state sales taxes. Management believes that these claims are limited solely to EYIC and that any prospective unpaid tax claims against the Company are remote and unable to be estimated.

Action By Suhl, Harris and Babich

In 2003, a consolidated action was brought by the plaintiffs Wolf Suhl, Christine Harris and Edward Babich in the Supreme Court of British Columbia pursuant to an order pronounced in the New Westminster Registry under Action No. S061589 on May 7, 2003, which allowed the plaintiffs to proceed with an action against EYIC. In February 2006, the Supreme Court of British Columbia made an order that the Company and Mr. Jay Sargeant be added to the lawsuit. The Plaintiffs' total claim was approximately $478,000. On April 13, 2006, the plaintiffs amended their pleadings to assert claims against the Company and Jay Sargeant An order was pronounced on August 15, 2006 for the substitutional service of Mr. Jay Sargeant. On September 5, 2006 the Company paid $200,000 in full and final settlement of this matter.

On September 20, 2006 Essentially Yours Industries (International) Limited entered into a consignment and distribution licensing agreement with Orientrends, Inc. Orientrends will act as an exclusive agent and qualified distributor to market EYI Products within the Philippines. The agreement is for a period of five years.

NOTE 11 - DISCONTINUED OPERATIONS

During the year ended December 31, 2005, the Company elected to discontinue the operations of Halo Distribution LLC (hereinafter "Halo"), a subsidiary of the Company. The Company's balance sheet reports net liabilities from discontinued operations of $375,344 as at September 30, 2006 and December 31, 2005.

In June 2002, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards, No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" (hereinafter "SFAS No. 146"). SFAS No. 146 addresses significant issues regarding the recognition, measurement, and reporting of costs associated with exit and disposal activities, including restructuring activities. SFAS No. 146 also addresses recognition of certain costs related to terminating a contract that is not a capital lease, costs to consolidate facilities or relocate employees, and termination benefits provided to employees that are involuntarily terminated under the terms of a one-time benefit arrangement that is not an ongoing benefit arrangement or an individual deferred-compensation contract. SFAS No. 146 was issued in June 2002, effective December 31, 2002. The Company's financial position and results of operations have not been affected by adopting SFAS No. 146.

NOTE 12 - RELATED PARTY NOTE PAYABLE

The Company issued a promissory note for a total of $40,000 in December 2003. The note is unsecured, non-interest bearing and payable upon demand.

NOTE 13 - CONCENTRATIONS

Bank Accounts

The Company maintains its cash accounts in one commercial bank. During the year, the Company may maintain balances in excess of the federally insured amounts in the accounts that are maintained in the United States. The Company also maintains funds in commercial banks in Vancouver, British Columbia, in which funds in U.S. dollars are not insured. Additionally, the Company maintains funds in Hong Kong where none of the funds are insured. At September 30, 2006 and December 31, 2005, a total of $1,768,624 and $56,088 respectively, was not insured.

Economic Dependence

During the year, the Company purchased approximately 90% of its products for resale from one company, Nutri-Diem Inc., which is the sole supplier of the Company's flagship product Calorad. Pursuant to a purchase agreement, the Company is subject to minimum purchases per annum. (See Note 10.)

NOTE 14 - RELATED PARTY TRANSACTIONS

On May 27, 2002, Mr. Jay Sargeant, a shareholder of Essentially Yours Industries, Corp. ("EYI Corp.") agreed to acquire all of the shares of the Essentially Yours Industries, Inc. ("EYI"), along with the transfer agreement, license agreement, and agency appointment agreement, in settlement of amounts owed to him. As part of this transaction, EYI Corp. agreed to provide to EYI the services outlined in a management agreement.

The Company acquired, through agreements with Essentially Yours Industries, Corp. ("EYI Corp"), the rights, title, and interest in and to the contracts with the Company's Independent Business Associates as well as the rights and licenses to trademarks and formula for the Company's primary products.

Accounts payable to related parties represents amounts due to the President and Chief Executive Officer and to the Chief Operations Officer for services preformed during the last year, as well as to other related parties and the company with which they have a signed management agreement. These payables are non-interest bearing and non-collateralized.

The Company purchases approximately 90% of its products for resale from one company, Nutri-Diem Inc., which is owned in part by a director of the Company.

On September 19, 2006 the Company entered into a letter agreement with James Toll and Fred Erickson whereby the Company has agreed to compensate their sales efforts during the pre-launch phase of the ME2 product.

Promissory Notes

At September 30, 2006, the Company is owed $31,250 from two consultants pursuant to terms of Promissory Notes and advances made pursuant to a letter agreement.

NOTE 15 - SUBSEQUENT EVENTS

On October 19, 2006 the Company entered into a consulting agreement with Creative Life Enterprises, Inc. on a month to month basis. Creative Life received 500,000 shares of the Company's restricted common stock as compensation for their services.

On October 12, 2006 the Company entered into a definitive agreement with Mach 3 Technologies Group, LLC. ("Mach 3") who will provide EYI with the exclusive rights to the fuel enhancement product ME2 in the US, Canada and Mexico for a period of three years. Pursuant to the agreement, the Company must purchase $1,000,000, $6,000,000, and $12,000,000 respectively in each of the three years. In addition to the unit price of the ME2 product, Mach 3 will also receive warrants to purchase the Company's common stock with each product purchase order. The maximum number of warrants that can be issued to Mach 3 is 15,000,000. In connection with purchase orders issued in October 2006, the Company issued Mach 3 a total of 967,680 warrants with an exercise price of $0.06.

On October 1, 2006 the Company entered into a two year agreement with Agoracom Investor Relations Corp. to provide investor relations services. Agoracom will receive $2,500 per month plus a warrant to purchase up to 500,000 shares of the Company's common stock at $0.06 per share.

Between October 1, 2006 and November 7, 2006, The Company issued 12,681,159 common shares to Cornell Capital to retire $60,000 of the convertible debt.

Between October 1, 2006 and November, 2006, The Company issued 12,922,254 common shares to Certain Wealth to retire $55,269 of the convertible debt.

Between October 1, 2006 and November , 2006, The Company issued 16,152,007 common shares to TAIB Bank to retire $69,081 of the convertible debt.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION.

FORWARD LOOKING STATEMENTS

The information in this discussion contains forward-looking statements. These forward-looking statements involve risks and uncertainties, including statements regarding EYI's capital needs, business strategy and expectations. Any statements contained herein that are not statements of historical facts may be deemed to be forward-looking statements. In some cases, you can identify forward-looking statements by terminology such as "may", "should", "expect", "plan", "intend", "anticipate", "believe", "estimate", "predict", "potential" or "continue", the negative of such terms or other comparable terminology. Actual events or results may differ materially. In evaluating these statements, you should consider various factors, including the risks outlined in the Risk Factors section below, and, from time to time, in other reports we file with the Securities and Exchange Commission (the "SEC"). These factors may cause our actual results to differ materially from any forward-looking statement.

OVERVIEW

We are in the business of selling, marketing, and distributing a product line consisting of approximately 25 products in four categories, dietary supplements, personal care products, water filtration systems and a fuel additive product. Our most successful product is Calorad, a liquid collagen-based dietary supplement presently available on the market. These products are marketed through a network marketing program in which IBAs (Independent Business Associates) purchase products for resale to retail customers as well as for their own personal use. We have a list of over 385,000 IBAs, of which approximately 7,400 we consider "active". An "active" IBA is one who purchased our products within the preceding 12 months. Approximately 1,300 of these IBAs are considered "very active". A "very active" IBA is one who is on our automatic Auto-ship Program and is current with their annual administration fee. Our Auto-ship Program, recently re-named Convenience Program, allows our IBAs to set up a reoccurring order that is automatically shipped to them each month.

The IBAs in our network are encouraged to recruit interested people to become new distributors of our products. New IBAs are placed beneath the recruiting IBA in the "network" and are referred to as being in that IBA's "down-line" organization. Our marketing plan is designed to provide incentives for IBAs to build, maintain and motivate an organization of recruited distributors in their down-line organization to maximize their earning potential. IBAs generate income by purchasing our products at wholesale prices and reselling them at retail prices. IBAs also earn commissions on product purchases generated by their down-line organization. Qualified IBAs may also earn additional commissions under the Management Matching Bonus ("MMB") program.

On an ongoing basis we review our product line for duplication and sales trends and make adjustments accordingly. As of September 30, 2006, our product line consisted of: (i) 17 dietary supplement products; (ii) 5 personal care products consisting primarily of cosmetic and skin care products; (iii) 2 water filtration system products and (iv) 1 fuel additive product. Our products are primarily manufactured by Nutri-Diem, Inc., a related party, and sold by us under a license and distribution agreement with Nutri-Diem. Certain of our own products are manufactured for us by third party manufacturers pursuant to formulations developed for us. Our products are sold to our IBAs or retail customers located in the United States, Canada and Asia.

We believe that our network marketing system is suited to marketing dietary supplements, personal care products, water filtration systems, and fuel additive products because sales of such products are strengthened by ongoing personal contact between IBAs and their customers. We also believe that our network marketing system appeals to a broad cross-section of people, particularly those looking to supplement family income or who are seeking part-time work. IBAs are given the opportunity, through our sponsored events and training sessions, to network with other distributors, develop selling skills and establish personal goals. We supplement monetary incentives with other forms of recognition, in order to motivate IBAs.

Recent Corporate Developments

We experienced the following significant developments through the date of this filing and during fiscal 2006:

· On October 20, 2006 EYI entered into a non-binding letter of intent with Mach 3 Technologies, LLC (“Mach 3”) for the exclusive distribution rights for the fuel enhancement product Ultimate ME2 in the Philippines.

· On October 19, 2006 EYI entered into a consulting agreement with Creative Life Enterprises, Inc. (“Creative Life”) on a month to month basis. Creative Life received 500,000 shares of restricted common stock as compensation for their services.

· On October 12, 2006 EYI entered into a definitive agreement with Mach 3 for the exclusive residential rights for the fuel enhancement product ME2 in the US, Canada and Mexico for a period of three years. Pursuant to the agreement, Mach 3 received 967,680 warrants at $0.06 per share expiring October 12, 2008.

· On October 1, 2006 we entered into an agreement with Agoracom Investor Relations Corp. (“Agoracom”) to provide investor relations services. Agoracom is to receive $2,500 per month compensation along with a warrant for the purchase of up to 500,000 shares of common stock at $0.06 for a period of two years. The agreement expires on October 1, 2007.

· On September 20, 2006 Essentially Yours Industries (International) Limited entered into a consignment and distribution licensing agreement with Orientrends, Inc. The agreement is for five years commencing January 1, 2007 for the sale of our products in the Philippines.

· On August 12, 2006 we entered into a Joint Venture Agreement with Internet Marketing Consortium ("IMC") to provide multi media strategies, promotional, direct and targeted marketing services for an undetermined period of time. In consideration for the services provided by IMC, we paid a fee of $25,000.

· On July 27, 2006 we entered into an addendum (the "Addendum") to the China Agency Agreement dated September 15, 2005 between Essentially Yours Industries (Hong Kong) Limited and Guangzhou Zhongdian Enterprises (Group) Co. Ltd. and China Electronics Import and Export South China Corporation. Pursuant to the Addendum, we agreed to extend the purchasing and exclusivity terms of the China Agency Agreement for an additional one year period.

· On July 12, 2006 and July 14, 2006 we received letters from Metals & Arsenic Removal Technology, Inc. ("MARTI") advising that the worldwide license for the ARTI-64 technology used for the production of the Code Blue™ product had been transferred from Hydroflo, Inc. to MARTI. MARTI has also transferred some of its inventory to Markus Group Ltd. ("Markus Group") and in the event MARTI is unable to meet production requirements they have granted the rights to produce Code Blue™ to Markus Group. On July 20, 2006 Markus Group provided EYI with an Indemnity in connection with the letters provided by MARTI.

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On July 1, 2006 EYII entered into a Consulting Agreement with James Toll. Mr. Toll provided training and marketing services for a period of three (3) months. Mr. Toll received $3,750 per month as compensation for his services.

2006 Growth Strategy

New Product Introduction. In 2005, we introduced Code Blue™, a water filtration system product. The initial shipment of Code Blue Filters did not meet EYI's product specifications. However, these product concerns were corrected with a later version of the Code Blue filter called the G-4 which we introduced and began promoting in 2006. It was our intent to create mass awareness of this new product through a year long promotional tour campaign. Early results of this campaign indicated that product sales were not meeting sales targets and objectives. Management assessed these results and concluded that the problems surrounding the initial product version significantly hindered the public's confidence in the Code Blue product line. Management still believes that this is a quality product with the unique performance feature of removing arsenic and other contaminants from water through a tabletop unit. Management intends to continue to market this product along side it's other products but has scaled back the allocation of future marketing dollars earmarked for the tour campaign.

In September 2006, EYI entered into a Letter of Intent with Mach 3 Technologies, Inc. (“Mach 3”) and subsequently, in October 2006, EYI signed a definitive agreement with Mach 3. Through this agreement, Mach 3 has granted EYI the right to market the fuel enhancement product Ultimate ME2 (“ME2”). ME2 is a non-polluting fuel enhancement additive that enhances and creates efficient combustion that cools the engine of vehicles. Test results indicate that automobiles using ME2 will create fewer emissions for the environment, their engines will run smoother and will consume less fuel. In October 2006, EYI placed its first purchase order of the ME2 product and is expecting delivery in the middle of November. In anticipation of this delivery, EYI has created a pre-launch campaign which will allow interested individuals to secure their initial bottle of the product.

International Expansion. Our Hong Kong office was opened in September 2005 with the fundamental objective to service the local Hong Kong distributors and provides a product pick up depot for Code Blue™, Calorad®, Prosoteine®, Agrisept-L® and Definition® drops and cream, and Calorad® Cream. Although sales in the region have not met management’s expectations to-date, we intend to maintain this facility as it also serves as our resource and support center for other international expansion projects including the CEIEC agency agreement.

In April 2006, our subsidiary, Essentially Yours Industries (International) Limited, signed a Letter of Intent and Good Faith Commitment with Raul Bautista and Rommel Panganiban to act as managing partners and distributors for the Philippines. On September 20, 2006 we signed a definitive agreement with Orientrends, Inc. (“Orientrends”) in connection with the Letter of Intent. Orientrends has since leased a new office in Makati which will be used for training new Filipino IBAs and will serve as a distribution center of EYI’s products within that region.

Distributor Commission Pay Plan Enhancement. On July 28, 2006 the Company launched a new component of its commission pay plan for its independent distributors called the Management Matching Bonus (“MMB”). We believe that this enhancement will give our distributors additional incentive to sell more of our products, recruit new sales people and assist their existing and new customers.

RESULTS OF OPERATIONS

Three Months and Ninth Months Summary

Summary of Quarterly Results

	Three months ended				Nine months ended			
	30-Sep-06	30-Sep-05	Variance		30-Sep-06	30-Sep-05	Variance	
Revenue	$ 949,429	$ 1,335,963	($386,534)	(29%)	3,068,166	3,850,246	(782,080)	(20%)
Cost of goods sold	$ 268,763	$ 350,188	($81,425)	(23%)	947,611	840,125	107,486	13%
Gross profit before commissions expense	$ 680,666	$ 985,775	(305,109)	(31%)	2,120,555	3,010,121	(889,566)	(30%)
Commission expense	$ 355,556	$ 513,449	($157,893)	(31%)	1,120,273	1,435,911	(315,638)	(22%)
Gross profit after cost of goods sold and commissions	$ 325,110	$ 472,326	($147,216)	(31%)	1,000,282	1,574,210	(573,928)	(36%)
	$ 1,260,264	$ 1,169,630	$ 90,634	8%	3,448,685	3,362,927	85,758	3%

Operating expenses								
Operating loss	($935,154)	($697,304)	($237,850)	34%	(2,448,403)	(1,788,717)	(659,686)	37%

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Revenues

During the three months ended September 30, 2006 we had total revenues of $949,429 as compared to revenues of $1,335,963 for the same period in 2005 which represents a decline of $386,534 or 29%. The year-to-date results for 2006 compared with 2005 indicate a revenue decline of $782,080 or 20%.The decrease in our revenues can be primarily attributed to:

· Our inability to attract new IBA's

· Lack of IBA participation in our auto-ship program

Gross Profit before Commission Expense

During the three months ended September 30, 2006, as compared to the same period in 2005, we had gross profits of $680,666 and $985,775 respectively. This represents a decline of $305,109 or 31%. The nine month period ending September 30, 2006 compared with the same period in 2005 indicate that the gross profit has declined $889,566 or 30%. The decline in our gross profit is primarily attributed to our decreased binary sales in relation to other revenue segments that have a higher percentage of cost-of-goods.

Revenue by Segments

The following table summarizes our four revenue segments as a percentage of total revenue, respectively, for the periods indicated:

Revenue by Segments

	Three months ended				Nine months ended			
	30-Sep-06	30-Sep-05	Variance		30-Sep-06	30-Sep-05	Variance	
Administration fees	$ 32,620	$ 26,370	$ 6,250	24%	$ 111,581	$ 101,016	$ 10,565	10%
Binary Sales	$ 670,514	$ 1,050,894	($380,380)	(36%)	$ 2,147,295	$ 2,901,814	($754,519)	(26%)
Direct sales	$ 159,634	$ 188,210	($28,576)	(15%)	$ 517,016	$ 614,482	($97,465)	(16%)
Affiliate sales	$ 85,501	$ 67,466	$ 18,035	27%	$ 285,388	$ 224,266	$ 61,121	27%
Sales Aids	$ 1,160	$ 3,022	($1,862)	(62%)	$ 6,886	$ 8,669	($1,782)	(21%)
	$ 949,429	$ 1,335,963	($386,536)	(29%)	$ 3,068,166	$ 3,850,246	($782,080)	(20%)

Details of the most significant changes for the periods presented are detailed below:

Binary sales - The binary sales segment represents $670,514 or 71% of the total revenue earned during the quarter ended September 30, 2006, as compared to $1,050,894 or 79% of the total revenues earned during the quarter ended September 30, 2005. A comparison of the three month and nine month results for 2006 and 2005 indicate a decline of 36% and 26% respectively.

Direct sales - The direct sales segment represents $159,634 or 17% of the total revenue earned during the quarter ended September 30, 2006, as compared to $188,210 or 14% of the total revenues earned during the quarter ended September 30, 2005. A comparison of the quarterly and nine month results for 2006 and 2005 indicate a decline of 15% and 16% respectively.

Affiliate sales - The affiliate sales segment represents $85,501 or 9% of the total revenue earned during the quarter ended September 30, 2006, as compared to $67,466 or 5% of the total revenues earned during the quarter ended

September 30, 2005. A comparison of the quarterly and nine month results for 2006 and 2005 indicate a increase of 27% and 27% respectively.

Expenses

Operating expenses:

The following table summarizes operating expenditures for the periods indicated:

Operating Expenses	Three months ended				Nine months ended			
	30-Sep-06	30-Sep-05	Variance		30-Sep-06	30-Sep-05	Variance	
Consulting fees	$ 259,639	$ 273,026	($13,387)	(5%)	$ 743,738	$ 751,836	($8,098)	(1%)
Legal and professional fees	$ 266,908	$ 107,333	$ 159,575	149%	$ 428,150	$ 254,090	$ 174,060	69%
Customer service	$ 62,718	$ 9,771	$ 52,947	542%	$ 169,721	$ 161,776	$ 7,945	5%
Finance and administration	$ 214,835	$ 299,735	($84,900)	(28%)	$ 643,529	$ 663,213	($19,684)	(3%)
Sales and marketing	$ 59,339	$ 42,569	$ 16,770	39%	$ 271,631	$ 47,560	$ 224,071	471%
Telecommunications	$ 32,930	$ 118,881	($85,951)	(72%)	$ 97,955	$ 361,139	($263,184)	(73%)
Wages and benefits	$ 264,899	$ 252,095	$ 12,804	5%	$ 864,292	$ 995,247	($130,955)	(13%)
Warehouse expense	$ 98,995	$ 66,220	$ 32,775	49%	$ 229,668	$ 128,066	$ 101,602	79%
	$ 1,260,264	$ 1,169,630	$ 90,634	8%	$ 3,448,685	$ 3,362,927	$ 85,758	3%

Operating Expenses

We incurred total operating expenses in the amount of $3,448,685 during the nine months ended September 30, 2006, compared to $3,362,927 for the nine months ended September 30, 2005. The results for the three and nine months ended September 30, 2006 compared with the same periods in 2005 indicate that the total Operating expenses increased 8% and 3% respectively. The following explains the most significant changes for the periods presented:

Legal and Professional fees - The results for the three and nine months ended September 30, 2006 compared with the same periods in 2005 indicate that Legal and Professional fees increased 149% and 69% respectively. This increase is associated with the additional fees incurred in connection with the review of SEC filings. In addition, during the September 2006 quarter, the Company paid out $200,000 in connection with the settlement of the Suhl, Harris, and Babich legal matter.

Sales & Marketing - The results for the three and nine months ended September 30, 2006 compared with the same periods in 2005 indicate that Sales & Marketing expenses increased 39% and 471% respectively. This increase is largely associated with the following:

- Hong Kong marketing initiatives for the Grand Opening
- Registration costs for Code Blue in China
- North American Training event expenditures

Telecommunications - The results for the three and nine months ended September 30, 2006 compared with the same periods in 2005 indicate that Telecommunications expenses declined 72% and 73% respectively. This decrease is attributed to the elimination of a third party service provider of our website and shopping cart. We have replaced these systems with systems built and managed in-house.

Wages and benefits - The results for the three and nine months ended September 30, 2006 compared with the same periods in 2005 indicate that Wages and Benefits increased 5% and declined 13% respectively. The year-to-date decline is the result of less stock options issued and vesting during 2006 over the same periods in 2005.

Warehouse expenses - The results for the three and nine months ended September 30, 2006 compared with the same periods in 2005 indicate that Warehouse expenses increased 49% and 79% respectively. The increase is primarily attributed to the rental fees associated with the Hong Kong operation.

Other Income (Expense):

At September 30, 2006, the Company revalued the derivative embedded in each of the three convertible debentures at $440,275 each or a total of $1,320,825. As a result, the Company recognized a corresponding gain of $855,870.

At September 30, 2006, the Company also calculated a marked-to-market adjustment for the warrants issued to Cornell Capital in connection with the convertible debenture. The Company recognized a loss of $3,244,046 as a result of this valuation.

FINANCIAL CONDITION

Cash and Working Capital

			300,416	6.09	
Total	$ 46,796	$ 4,247			$ 563,030

The following table sets forth the scheduled repayments of fixed- and adjustable-rate loans at September 30, 2006 that are contractually due after September 30, 2007.

	Due After September 30, 2007		
	Fixed	Adjustable (In thousands)	Total
Residential first mortgage loans:			
One- to four-family	$ 396,189	55,972	452,161
Construction	5,773		5,773
Commercial	3,260	558	3,818
Commercial real estate	18,396	23,479	41,875
Home equity loans and lines of credit	28,018	18,704	46,722
Other	1,935		1,935
Total	$ 453,571	$ 98,713	$ 552,284

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Loan Originations and Repayments. Historically, we have originated residential mortgage loans pursuant to underwriting standards that generally conform to Fannie Mae and Freddie Mac guidelines. Loan origination activities are primarily concentrated in Monroe and Northampton Counties, Pennsylvania. New loans are generated primarily from walk-in customers, customer referrals, a network of mortgage brokers, and other parties with whom we do business, and from the efforts of employees and advertising. Loan applications are underwritten and processed at our corporate center.

One- to Four-Family Residential Loans. Historically, our primary lending activity has consisted of the origination of one- to four-family residential mortgage loans secured primarily by properties located in Monroe and Northampton Counties, Pennsylvania. At September 30, 2006, approximately $452.4 million, or 80.4% of our loan portfolio, consisted of one- to four-family residential loans. Our origination of one- to four-family loans increased in fiscal year 2006 compared to fiscal years 2005 and 2004, although such loans are declining as a percentage of our total loan portfolio. Generally, one- to four-family residential mortgage loans are originated in amounts up to 80% of the lesser of the appraised value or purchase price of the property, although loans may be made with higher loan-to-value ratios at a higher interest rate to compensate for the risk. Private mortgage insurance is generally required on loans with a loan-to-value ratio in excess of 80%. Fixed-rate loans are originated for terms of 10, 15, 20 and 30 years. At September 30, 2006, our largest loan secured by one- to four-family real estate had a principal balance of approximately $605,000 and was secured by a single-family residence. This loan was performing in accordance with its terms.

We also offer adjustable-rate mortgage loans which have fixed terms of one, three, five or ten-years before converting to an annual adjustment schedule based on changes in a designated United States Treasury index. We originated $11.9 million of adjustable rate one- to four-family residential loans during the year ended September 30, 2006 and $13.7 million during the year ended September 30, 2005. Our adjustable rate mortgage loans provide for maximum rate adjustments of 200 basis points per adjustment, with a lifetime maximum adjustment of 600 basis points. Our adjustable rate mortgage loans amortize over terms of up to 30 years.

Adjustable rate mortgage loans decrease the risk associated with changes in market interest rates by periodically repricing, but involve other risks because, as interest rates increase, the interest payments on the loan increase, thus increasing the potential for default by the borrower. At the same time, the marketability of the underlying collateral may be adversely affected by higher interest rates. Upward adjustment of the contractual interest rate is also limited by the maximum periodic and lifetime interest rate adjustments permitted by our loan documents, and therefore, is potentially limited in effectiveness during periods of rapidly rising interest rates. At September 30, 2006, $56.0 million, or 12.4%, of our one- to four-family residential loans had adjustable rates of interest.

All one- to four-family residential mortgage loans that we originate include due-on-sale clauses, which give us the right to declare a loan immediately due and payable in the event that, among other things, the borrower sells or otherwise disposes of the real property subject to the mortgage and the loan is not repaid.

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Regulations limit the amount that a savings bank may lend relative to the appraised value of the real estate securing the loan, as determined by an appraisal of the property at the time the loan is originated. For all loans, we utilize outside independent appraisers approved by the Board of Directors. All borrowers are required to obtain title insurance. We also require fire and casualty insurance and, where circumstances warrant, flood insurance.

Commercial Real Estate Loans. At September 30, 2006, $47.5 million, or 8.4% of our total loan portfolio consisted of commercial real estate loans. Commercial real estate loans are secured by office buildings, mixed-use properties and other commercial properties. We generally originate adjustable rate commercial real estate loans with an initial term of five years and a repricing option, and a maximum term of up to 25 years. The maximum loan-to-value ratio of our commercial real estate loans is 85%. At September 30, 2006, we had 202 commercial real estate loans with an outstanding balance of $47.5 million. At September 30, 2006, our largest commercial real estate loan balance was $2.8 million. At September 30, 2006, all but one of our loans secured by commercial real estate were performing in accordance with their terms. One secured commercial line of credit totaling approximately $50,000 was between 60 and 90 days past due at September 30, 2006.

We consider a number of factors in originating commercial real estate loans. We evaluate the qualifications and financial condition of the borrower, including credit history, profitability and expertise, as well as the value and condition of the mortgaged property securing the loan. When evaluating the qualifications of the borrower, we consider the financial resources of the borrower, the borrower s experience in owning or managing similar property and the borrower s payment history with us and other financial institutions. In evaluating the property securing the loan, the factors we consider include the net operating income of the mortgaged property before debt service and depreciation, the ratio of the loan amount to the appraised value of the mortgaged property and the debt service coverage ratio (the ratio of net operating income to debt service) to ensure that it is at least 120% of the monthly debt service. All commercial real estate loans in excess of $250,000 are appraised by outside independent appraisers approved by the Board of Directors. Personal guarantees are obtained from commercial real estate borrowers although we will consider waiving this requirement based upon the loan-to-value ratio of the proposed loan. All purchase money and asset refinance borrowers are required to obtain title insurance. We also require fire and casualty insurance and, where circumstances warrant, flood insurance.

Loans secured by commercial real estate generally are considered to present greater risk than one- to four-family residential loans. Commercial real estate loans often involve large loan balances to single borrowers or groups of related borrowers. Repayment of these loans depends to a large degree on the results of operations and management of the properties securing the loans or the businesses conducted on such property, and may be affected to a greater extent by adverse conditions in the real estate market or the economy in general. Accordingly, the nature of these loans makes them more difficult for management to monitor and evaluate.

***First Mortgage Construction Loans*.** At September 30, 2006, $5.9 million, or 1.1%, of our total loan portfolio consisted of first mortgage construction loans. Most of our first mortgage construction loans are for the first mortgage construction of residential properties. We currently offer fixed and adjustable-rate residential first mortgage construction loans. First mortgage

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construction loans are generally structured for permanent mortgage financing once the construction is completed. At September 30, 2006, our largest first mortgage construction loan balance was $600,000. The loan was performing in accordance with its terms. First mortgage construction loans, once converted to permanent financing, generally repay over a thirty-year period. First mortgage construction loans require only the payment of interest during the construction period. First mortgage construction loans will generally be made in amounts of up to 80% of the appraised value of the completed property, or the actual cost of the improvements. In certain circumstances first mortgage construction loans may be made in amounts up to 100% of the appraised value with appropriate credit enhancements such as private mortgage insurance. Funds are disbursed based on our inspections in accordance with a schedule reflecting the completion of portions of the project.

First mortgage construction loans generally involve a greater degree of credit risk than one- to four-family residential mortgage loans. The risk of loss on a construction loan depends upon the accuracy of the initial estimate of the value of the property at completion of construction compared to the estimated cost of construction. For all loans, we utilize outside independent appraisers approved by the Board of Directors. All borrowers are required to obtain title insurance. We also require fire and casualty insurance and, where circumstances warrant, flood insurance on properties.

Other Loans. We offer a variety of loans that are either unsecured or secured by property other than real estate. These loans include loans secured by deposits, personal loans and automobile loans. At September 30, 2006, these other loans totaled $4.2 million, or 0.7% of the total loan portfolio.

Loan Approval Procedures and Authority. The loan approval process is intended to assess the borrower s ability to repay the loan, the viability of the loan, and the adequacy of the value of the property that will secure the loan. To assess the borrower s ability to repay, we review each borrower s employment and credit history and information on the historical and projected income and expenses of mortgagors. All residential mortgage loans in excess of the conforming loan limit but less than $500,000 must be approved by any two of the following: President, Chief Lending Officer and the Vice President, Retail Lending. All loans in excess of $500,000 but less than $750,000 must be approved by the Chief Executive Officer and either the Chief Lending Officer or the Vice President, Retail Lending. All loans in excess of $750,000 must be approved by the Management Loan Committee and all loans in excess of $1.0 million must be approved by the Director Loan Committee.

Non-Performing Loans and Problem Assets

After a real estate secured loan becomes 15 days late, we deliver a computer generated late charge notice to the borrower and will attempt to contact the borrower by telephone. When a loan becomes 30 days delinquent, we send a delinquency letter to the borrower. We then attempt to make satisfactory arrangements to bring the account current, including interviewing the borrower, until the mortgage is brought current or a determination is made to recommend foreclosure, deed-in-lieu of foreclosure or other appropriate action. After 60 days, we will generally refer the matter to the Board of Directors who may authorize legal counsel to commence foreclosure proceedings.

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Mortgage loans are reviewed on a regular basis and such loans are placed on non-accrual status when they become more than 90 days delinquent. When loans are placed on non-accrual status, unpaid accrued interest is fully reserved, and further income is recognized only to the extent received.

Non-performing Loans. At September 30, 2006, $623,000 (or less than 1.0% of our total loans) were non-performing loans.

As of September 30, 2006, we had no outstanding non-performing commercial real estate loans.

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Non-Performing Assets. The table below sets forth the amounts and categories of our non-performing assets at the dates indicated. At each date presented, we had no troubled debt restructurings (loans for which a portion of interest or principal has been forgiven and loans modified at interest rates materially less than current market rates).

	At September 30,				At November 30,
	2006	2005	2004	2003	2002
	(Dollars in thousands)				
Non-accrual loans:					
Residential first mortgage loans:					
One- to four-family	$ 436	$ 554	$ 578	$ 379	$ 578
Construction					
Commercial					
Commercial real estate					
Home equity loans and lines of credit	40	50	79	98	17
Other		1	8	47	76
Total	476	605	665	524	671
Accruing loans 90 days or more past due:					
Residential first mortgage loans:					
One- to four-family					
Construction					
Commercial					
Commercial real estate					
Home equity loans and lines of credit					
Other					
Total loans 90 days or more past due					
Total non-performing loans	476	605	665	524	671
Real estate owned		19	101	202	101
Other non-performing assets					
Total non-performing assets	$ 476	$ 624	$ 766	$ 726	$ 772
Troubled debt restructurings:					
Residential first mortgage loans::					
One- to four-family	$ 53	$ 94	$ 167	$ 270	$ 372
Construction					
Commercial					
Commercial real estate					
Home equity loans and lines of credit					
Other					15
Total	$ 53	$ 94	$ 167	$ 270	$ 387
Ratios:					
Total non-performing loans to total loans	0.08%	0.12%	0.14%	0.12%	0.17%
Total non-performing loans to total assets	0.06%	0.09%	0.11%	0.10%	0.14%
Total non-performing assets to total assets	0.07%	0.10%	0.13%	0.14%	0.16%

For the year ended September 30, 2006, gross interest income that would have been recorded had our non-accruing loans been current in accordance with their original terms was insignificant.

Delinquencies. The following table sets forth certain information with respect to our loan portfolio delinquencies at the dates indicated. Loans delinquent for 90 days or more are generally classified as nonaccrual loans.

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	Loans Delinquent For					
	60-89 Days		90 Days and Over		Total	
	Number	Amount	Number	Amount	Number	Amount
			(Dollars in thousands)			
At September 30, 2006						
Residential first mortgage loans:						
One- to four-family			5	436	5	436
Construction						
Commercial						
Commercial real estate	1	49			1	49
Home equity loans and lines of credit			1	40	1	40
Other						
Total	1	$ 49	6	$ 476	7	$ 525
At September 30, 2005						
Residential first mortgage loans:						
One- to four-family	4	590	8	554	12	1,144
Construction						
Commercial						
Commercial real estate						
Home equity loans and lines of credit	1	16	3	50	4	66
Other			1	1	1	1
Total	5	$ 606	12	$ 605	17	$ 1,211
At September 30, 2004						
Residential first mortgage loans:						
One- to four-family	5	237	5	497	10	734
Construction						
Commercial						
Commercial real estate						
Home equity loans and lines of credit			5	79	5	79
Other	1	4	3	8	4	12
Total	6	$ 241	13	$ 584	19	$ 825
At September 30, 2003						
Residential first mortgage loans:						
One- to four-family	2	118	5	379	7	497
Construction						
Commercial						
Commercial real estate						
Home equity loans and lines of credit			6	98	6	98
Other	1	1	6	47	7	48
Total	3	$ 119	17	$ 524	20	$ 643
At September 30, 2002						
Residential first mortgage loans:						
One- to four-family	4	243	10	578	14	821
Construction						
Commercial						
Commercial real estate						
Home equity loans and lines of credit	1	5	1	16	2	21
Other	4	42	4	77	8	119

Total	9	$	290	15	$	671	24	$	961

Classified Assets. Banking regulations and our Asset Classification Policy provide that loans and other assets considered to be of lesser quality should be classified as substandard, doubtful or loss assets. An asset is considered substandard if it is inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Substandard assets include those characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected. Assets classified as doubtful have all of the weaknesses inherent in those classified substandard, with the added characteristic that the weaknesses present make collection or liquidation in full, on the basis of

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currently existing facts, conditions, and values, highly questionable and improbable. Assets classified as loss are those considered uncollectible and of such little value that their continuance as assets without the establishment of a specific loss reserve is not warranted. We classify an asset as special mention if the asset has a potential weakness that warrants management s close attention. While such assets are not impaired, management has concluded that if the potential weakness in the asset is not addressed, the value of the asset may deteriorate, thereby adversely affecting the repayment of the asset.

An institution is required to establish general allowances for loan losses in an amount deemed prudent by management for loans classified substandard or doubtful, as well as for other problem loans. General allowances represent loss allowances which have been established to recognize the inherent losses associated with lending activities, but which, unlike specific allowances, have not been allocated to particular problem assets. When an institution classifies problem assets as loss, it is required either to establish a specific allowance for losses equal to 100% of the amount of the asset so classified or to charge off such amount. An institution s determination as to the classification of its assets and the amount of its valuation allowances is subject to review by the Office of Thrift Supervision which can order the establishment of additional general or specific loss allowances.

On the basis of management s review of its assets, at September 30, 2006, we classified approximately $3.0 million of our assets as special mention and $586,000 as substandard. At September 30, 2006, none of our assets were classified as doubtful or loss.

The loan portfolio is reviewed on a regular basis to determine whether any loans require classification in accordance with applicable regulations. Not all classified assets constitute non-performing assets.

Allowance for Loan Losses

Our allowance for loan losses is maintained at a level necessary to absorb loan losses that are both probable and reasonably estimable. Management, in determining the allowance for loan losses, considers the losses inherent in its loan portfolio and changes in the nature and volume of loan activities, along with the general economic and real estate market conditions. Our allowance for loan losses consists of two elements: (1) an allocated allowance, which comprises allowances established on specific loans and class allowances based on historical loss experience and current trends, and (2) an unallocated allowance based on general economic conditions and other risk factors in our markets and portfolios. We maintain a loan review system, which allows for a periodic review of our loan portfolio and the early identification of potential impaired loans. Such system takes into consideration, among other things, delinquency status, size of loans, type and market value of collateral and financial condition of the borrowers. Specific loan loss allowances are established for identified losses based on a review of such information. A loan evaluated for impairment is considered to be impaired when, based on current information and events, it is probable that we will be unable to collect all amounts due according to the contractual terms of the loan agreement. All loans identified as impaired are evaluated independently. We do not aggregate such loans for evaluation purposes. Loan impairment is measured based on the fair value of collateral method, taking into account the appraised value,

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any valuation assumptions used, estimated costs to sell and trends in the market since the appraisal date. General loan loss allowances are based upon a combination of factors including, but not limited to, actual loan loss experience, composition of the loan portfolio, current economic conditions, management s judgment and losses which are probable and reasonably estimable. The allowance is increased through provisions charged against current earnings and recoveries of previously charged-off loans. Loans that are determined to be uncollectible are charged against the allowance. While management uses available information to recognize probable and reasonably estimable loan losses, future loss provisions may be necessary based on changing economic conditions. Payments received on impaired loans are applied first to accrued interest receivable and then to principal. The allowance for loan losses as of September 30, 2006 is maintained at a level that represents management s best estimate of losses inherent in the loan portfolio, and such losses were both probable and reasonably estimable.

In addition, the Office of Thrift Supervision and the Pennsylvania Department of Banking, as an integral part of its examination process, periodically reviews our allowance for loan losses. The banking regulators may require that we recognize additions to the allowance based on its analysis and review of information available to it at the time of its examination.

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The following table sets forth activity in our allowance for loan losses for the periods indicated.

	At or For the Years Ended September 30,			At or for the ten months ended	At or for the year ended
	2006	2005	2004	September 30, 2003	November 30, 2002
			(Dollars in thousands)		
Balance at beginning of year	$ 3,563	$ 3,027	$ 2,509	$ 2,154	$ 1,371
Charge-offs:					
Residential first mortgage loans:					
One- to four-family		(10)		(28)	(42)
Construction					
Commercial					
Commercial real estate					
Home equity loans and lines of credit	(7)		(31)	(6)	(11)
Other	(2)	(5)	(4)	(51)	(97)
Total charge-offs	$ (9)	$ (15)	$ (35)	$ (85)	$ (150)
Recoveries:					
Residential first mortgage loans:					
One- to four-family			7	2	12
Construction					
Commercial					
Commercial real estate					
Home equity loans and lines of credit					
Other	1	1	16	8	21
Total recoveries	$ 1	$ 1	$ 23	$ 10	$ 33
Net charge-offs	(8)	(14)	(12)	(75)	(117)
Provision for loan losses	300	550	530	430	900
Balance at end of year	$ 3,855	$ 3,563	$ 3,027	$ 2,509	$ 2,154
Ratios:					
Net charge-offs to average loans outstanding	%	%	%	(0.02)%	(0.03)%
Allowance for loan losses to non-performing loans at end of year	809.87%	588.93%	455.19%	478.82%	321.01%
Allowance for loan losses to total loans at end of year	0.69%	0.70%	0.63%	0.57%	0.55%

As indicated in the table above, we charged off a de minimus amount of loans since fiscal year 2004, due, in part, to a stable local economy with significant appreciation in real estate values, conservative underwriting of loans and aggressive monitoring of the loan portfolio to identify and address non-performing loans and potential problem assets at an early date. The amount of foreclosures we incurred in the last five years was not material to our financial statements taken as a whole and ESSA Bank & Trust suffered no material losses on foreclosed assets during that period. See Non-Performing Loans and Problem Assets. There can be no assurance that we will not experience a deterioration of its loan portfolio, including increases in non-performing loans, problem assets and charge-offs, in the future.

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Allocation of Allowance for Loan Losses. The following tables set forth the allowance for loan losses allocated by loan category, the percent of the allowance to the total allowance and the percent of loans in each category to total loans at the dates indicated. The allowance for loan losses allocated to each category is not necessarily indicative of future losses in any particular category and does not restrict the use of the allowance to absorb losses in other categories.

	At September 30,								
	2006			2005			2004		
	Amount	Percent of Allowance to Total Allowance	Percent of Loans in Category to Total Loans	Amount	Percent of Allowance to Total Allowance	Percent of Loans in Category to Total Loans	Amount	Percent of Allowance to Total Allowance	Percent of Loans in Category to Total Loans
	(Dollars in thousands)								
Residential first mortgage loans:									
One- to four-family	$ 2,026	52.56%	80.36%	$ 1,887	52.96%	81.68%	$ 1,397	46.15%	82.41%
Construction	86	2.23	1.06	104	2.92	1.47	108	3.57	1.72
Commercial	133	3.45	1.09	114	3.20	1.03	62	2.05	0.51
Commercial real estate	773	20.05	8.43	471	13.22	7.17	332	10.97	6.08
Home equity loans and lines of credit	746	19.35	8.31	661	18.55	7.82	504	16.65	7.07
Other	46	1.19	0.75	39	1.09	0.83	106	3.50	2.21
Total allocated allowance	3,810	98.83	100.00%	3,276	91.94	100.00%	2,509	82.89	100.00%
Unallocated allowance	45	1.17		287	8.06		518	17.11	
Total allowance for loan losses	$ 3,855	100.00%	100.00%	$ 3,563	100.00%	100.00%	$ 3,027	100.00%	100.00%

	At September 30, 2003			At November 30, 2002		
	Amount	Percent of Allowance to Total Allowance	Percent of Loans in Category to Total Loans	Amount	Percent of Allowance to Total Allowance	Percent of Loans in Category to Total Loans
	(Dollars in thousands)					
Residential first mortgage loans:						
One- to four-family	$ 1,326	52.87%	85.16%	$ 1,177	54.65%	84.88%
Construction	87	3.47	1.37	95	4.41	1.89
Commercial	44	1.75	0.51	42	1.95	0.35
Commercial real estate	208	8.29	4.19	184	8.54	2.63
Home equity loans and lines of credit	393	15.66	5.99	252	11.70	6.48
Other	123	4.90	2.78	150	6.96	3.77
Total allocated allowance	2,181	86.94	100.00%	1,900	88.21	100.00%
Unallocated allowance	328	13.06		254	11.79	
Total allowance for loan losses	$ 2,509	100.00%	100.00%	$ 2,154	100.00%	100.00%

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We use the accrual method of accounting for all performing loans. The accrual of interest income is generally discontinued when the contractual payment of principal or interest has become 90 days past due or management has serious doubts about further collectibility of principal or interest, even though the loan is currently performing. When a loan is placed on nonaccrual status, unpaid interest previously credited to income is reversed. Interest received on nonaccrual loans generally is either applied against principal or reported as interest income, according to management s judgment as to the collectibility of principal. Generally, residential and consumer loans are restored to accrual status when the obligation is brought in accordance with the contractual terms for a reasonable period of time and ultimate collectibility of total contractual principal and interest is no longer in doubt. Commercial loans are restored to accrual status when the obligation is brought current, has performed in accordance with the contractual terms for a reasonable period of time and ultimate collectibility of total contractual principal and interest no longer is in doubt.

In its collection efforts, we will first attempt to cure any delinquent loan. If a real estate secured loan is placed on nonaccrual status, it will be subject to transfer to the real estate owned (REO) portfolio (properties acquired by or in lieu of foreclosure), upon which our loan servicing department will pursue the sale of the real estate. Prior to this transfer, the loan balance will be reduced, if necessary, to reflect its current market value less estimated costs to sell. Write downs of REO that occur after the initial transfer from the loan portfolio and costs of holding the property are recorded as other operating expenses, except for significant improvements which are capitalized to the extent that the carrying value does not exceed estimated net realizable value.

Fair values for determining the value of collateral are estimated from various sources, such as real estate appraisals, financial statements and from any other reliable sources of available information. For those loans deemed to be impaired, collateral value is reduced for the estimated costs to sell. Reductions of collateral value are based on historical loss experience, current market data, and any other source of reliable information specific to the collateral.

This analysis process is inherently subjective, as it requires us to make estimates that are susceptible to revisions as more information becomes available. Although we believe that we have established the allowance at levels to absorb probable and estimable losses, future additions may be necessary if economic or other conditions in the future differ from the current environment.

Securities Activities

Our securities investment policy is established by our Board of Directors. This policy dictates that investment decisions be made based on the safety of the investment, liquidity requirements, potential returns, cash flow targets, and consistency with our interest rate risk management strategy. Our investment policy is reviewed annually by our ALCO/Investment Committee. All policy changes recommended by this Committee must be approved by the Board of Directors. The Committee is composed of three members of the Board of Directors,

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one to serve as chairperson. The Chief Financial Officer, Controller, Chairman of the Board of Directors and Chief Executive Officer are ex-officio members of the Investment Committee. Authority to make investments under the approved guidelines will be delegated by the Committee to appropriate officers. While general investment strategies will be developed and authorized by the ALCO/Investment Committee, the execution of specific actions rests with the Chief Financial Officer.

The approved investment officers are authorized to execute investment transactions up to $4.0 million per transaction without the prior approval of the ALCO/Investment Committee and within the scope of the established investment policy. These officers are also authorized to execute investment transactions between $4.0 million and $6.0 million with the additional approval from two of the following officers: Chief Executive Officer, Chief Operating Officer, or Chief Lending Officer. Each transaction in excess of $6.0 million must receive prior approval of the Investment Committee.

Our current investment policy generally permits securities investments in debt securities issued by the U.S. government and U.S. agencies, municipal bonds, and corporate debt obligations, as well as investments in preferred and common stock of government agencies and government sponsored enterprises such as Fannie Mae, Freddie Mac and the Federal Home Loan Bank of Pittsburgh (federal agency securities) and, to a much lesser extent, other equity securities. Securities in these categories are classified as investment securities for financial reporting purposes. The policy also permits investments in mortgage-backed securities, including pass-through securities issued and guaranteed by Fannie Mae, Freddie Mac and Ginnie Mae as well as commercial paper, corporate debt and municipal securities. As of September 30, 2006, we held no asset-backed securities, and other equity securities consisted almost exclusively of securities issued by Fannie Mae and the Federal Home Loan Bank of Pittsburgh. Our current investment strategy uses a risk management approach of diversified investing in fixed-rate securities with short- to intermediate-term maturities, as well as adjustable-rate securities, which may have a longer term to maturity. The emphasis of this approach is to increase overall investment securities yields while managing interest rate risk.

SFAS No. 115 requires that, at the time of purchase, we designate a security as held to maturity, available-for-sale, or trading, depending on our ability and intent. Securities available-for-sale are reported at fair value, while securities held to maturity are reported at amortized cost.

Mortgage-Backed Securities. We purchase mortgage-backed securities in order to generate positive interest rate spreads with minimal administrative expense, lower credit risk as a result of the guarantees provided by Freddie Mac, Fannie Mae and Ginnie Mae, and increased liquidity. We invest primarily in mortgage-backed securities issued or sponsored by Fannie Mae, Freddie Mac, and Ginnie Mae. To a lesser extent, we also invest in securities backed by U.S. government agencies. At September 30, 2006 our mortgage-backed securities portfolio had a fair value of $54.4 million, consisting of Freddie Mac, Fannie Mae and Ginnie Mae mortgage-backed securities.

Mortgage-backed securities are created by pooling mortgages and issuing a security collateralized by the pool of mortgages with an interest rate that is less than the interest rate on

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the underlying mortgages. Mortgage-backed securities typically represent a participation interest in a pool of single-family or multi-family mortgages, although most of our mortgage-backed securities are collateralized by single-family mortgages. The issuers of such securities (generally U.S. government agencies and U.S. government sponsored enterprises, including Fannie Mae, Freddie Mac and Ginnie Mae) pool and resell the participation interests in the form of securities to investors, such as ESSA Bank & Trust, and guarantee the payment of principal and interest to these investors. Investments in mortgage-backed securities involve a risk that actual prepayments will be greater or less than the prepayment rate estimated at the time of purchase, which may require adjustments to the amortization of any premium or accretion of any discount relating to such instruments, thereby affecting the net yield on such securities. We review prepayment estimates for our mortgage-backed securities at the time of purchase to ensure that prepayment assumptions are reasonable considering the underlying collateral for the securities at issue and current interest rates, and to determine the yield and estimated maturity of the mortgage-backed securities portfolio. Periodic reviews of current prepayment speeds are performed in order to ascertain whether prepayment estimates require modification that would cause amortization or accretion adjustments.

Equity Securities. At September 30, 2006, our equity securities consisted almost entirely of securities issued by Fannie Mae, which are classified as available-for-sale.

In addition, we hold Federal Home Loan Bank of Pittsburgh common stock to qualify for membership in the Federal Home Loan Bank System and to be eligible to borrow funds under the Federal Home Loan Bank of Pittsburgh advance program. There is no market for the common stock.

The aggregate fair value of our Federal Home Loan Bank of Pittsburgh common stock as of September 30, 2006 was $13.7 million based on its par value. No unrealized gains or losses have been recorded because we have determined that the par value of the common stock represents its fair value. We owned shares of Federal Home Loan Bank of Pittsburgh common stock at September 30, 2006 with a par value that was $189,000 more than we were required to own to maintain our membership in the Federal Home Loan Bank System and to be eligible to obtain advances. We are required to purchase additional stock as our outstanding advances increase. Any excess stock we own is redeemed monthly by the Federal Home Loan Bank of Pittsburgh.

We review equity and debt securities with significant declines in fair value on a periodic basis to determine whether they should be considered temporarily or other than temporarily impaired. If a decline in the fair value of a security is determined to be other than temporary, we are required to reduce the carrying value of the security to its fair value and record a non-cash impairment charge in the amount of the decline, net of tax effect, against our current income.

Our investment securities portfolio contains unrealized losses of securities, including mortgage-related instruments issued or backed by the full faith and credit of the United States government, or generally viewed as having the implied guarantee of the U.S. government, and debt obligations of a U.S. state or political subdivision.

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Our policy is to recognize an other-than-temporary impairment of equity securities where the fair value has been significantly below cost for three consecutive quarters. For fixed maturity investments with unrealized losses due to interest rates where we have the positive intent and ability to hold the investment for a period of time sufficient to allow a market recovery, declines in value below cost are not assumed to be other than temporary. We review our position quarterly and concluded that at September 30, 2006, the declines outlined in the table below represent temporary declines due to interest rate change, and we have the intent and ability to hold those securities either to maturity or to allow a market recovery. However, as of September 30, 2005, we recognized a loss of $130,000 on equity securities that we deemed, through analysis of the security, to be other than a temporary loss.

The following table sets forth the composition of our securities portfolio (excluding Federal Home Loan Bank of Pittsburgh common stock) at the dates indicated.

	At September 30,					
	2006		2005		2004	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(In thousands)					
Investment securities available for sale:						
U.S. Government agency obligations	$ 41,960	$ 41,815	$ 34,989	$ 34,729	$ 14,981	$ 14,992
Obligations of state and political subdivisions	6,240	6,465	5,102	5,377	5,341	5,691
Mortgage-backed securities	40,327	39,907	18,799	18,491	20,482	20,444
Corporate notes			3,039	3,030	3,041	3,039
Total debt securities	88,527	88,187	61,929	61,627	43,845	44,166
Equity securities	882	935	882	879	1,012	908
Total investment securities available-for-sale	$ 89,409	$ 89,122	$ 62,811	$ 62,506	$ 44,857	$ 45,074
Investment securities held-to-maturity:						
U.S. Government agency obligations	$ 4,730	$ 4,681	$ 4,730	$ 4,704	$	$
Mortgage-backed securities	14,985	14,512	16,775	16,593	10,263	10,282
Total securities held to maturity	$ 19,715	$ 19,193	$ 21,505	$ 21,297	$ 10,263	$ 10,282

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Portfolio Maturities and Yields. The composition and maturities of the investment securities portfolio at September 30, 2006 are summarized in the following table. Maturities are based on the final contractual payment dates, and do not reflect the impact of prepayments or early redemptions that may occur.

	One Year or Less		More than One Year through Five Years		More than Five Years through Ten Years		More than Ten Years		Total Securities		
	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Fair Value	Weighted Average Yield
	(Dollars in thousands)										
Investment securities available for sale:											
U.S. Government agency obligations	$ 22,968	3.95%	$ 17,070	4.73%	$ 1,922	5.00%	$	%	$ 41,960	$ 41,815	4.32%
Obligations of state and political subdivisions							6,240	4.72	6,240	6,465	4.72
Mortgage-backed securities	511	5.29	12,538	4.46	169	5.50	27,109	4.88	40,327	39,907	4.76
Corporate notes											
Total debt securities	23,479	3.98%	29,608	4.62%	2,091	5.04%	33,349	4.85%	88,527	88,187	4.55%
Equity securities	882								882	935	
Total investment securities available for-sale	$ 24,361		$ 29,608		$ 2,091		$ 33,349		$ 89,409	$ 89,122	
Investment securities held-to-maturity:											
U.S. Government agency obligations	$	%	$ 4,730	4.35%	$	%	$	%	$ 4,730	$ 4,681	4.35%
Mortgage-backed securities			7,261	4.54	3,312	4.76	4,412	4.64	14,985	14,512	4.62
Total securities held to maturity	$	%	$ 11,991	4.46%	$ 3,312	4.76%	$ 4,412	4.64%	$ 19,715	$ 19,193	4.55%

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Sources of Funds

General. Deposits, borrowings, repayments and prepayments of loans and securities, proceeds from maturing securities and cash flows from operations are the primary sources of our funds for use in lending, investing and for other general purposes.

Deposits. We offer a variety of deposit accounts with a range of interest rates and terms. Our deposit accounts consist of savings accounts, NOW accounts, checking accounts, money market accounts, club accounts, certificates of deposit and IRAs and other qualified plan accounts. We provide commercial checking accounts for businesses.

At September 30, 2006, our deposits totaled $402.2 million. Interest-bearing NOW, savings and club and money market deposits totaled $168.9 million at September 30, 2006. At September 30, 2006, we had a total of $209.6 million in certificates of deposit. Noninterest-bearing demand deposits totaled $23.7 million. Although we have a significant portion of our deposits in shorter-term certificates of deposit, we monitor activity on these accounts and, based on historical experience and our current pricing strategy, we believe we will retain a large portion of these accounts upon maturity.

Our deposits are obtained predominantly from the areas in which our branch offices are located. We rely on our favorable locations, customer service and competitive pricing to attract and retain these deposits. While we accept certificates of deposit in excess of $100,000 for which we may provide preferential rates, we generally do not solicit such deposits as they are more difficult to retain than core deposits. At September 30, 2006, we had a total of $28.4 million of brokered certificates of deposits, an increase of $7.1 million from the prior fiscal year end. Our brokered certificates of deposits range from one- to five-year terms, and are purchased only through pre-approved brokers.

The following table sets forth the distribution of total deposit accounts, by account type, at the dates indicated.

	For the Years Ended September 30,								
	2006			2005			2004		
	Average Balance	Percent	Weighted Average Rate	Average Balance	Percent	Weighted Average Rate	Average Balance	Percent	Weighted Average Rate
	(Dollars in thousands)								
Deposit type:									
Noninterest bearing demand accounts	$ 21,383	5.49%	%	$ 17,527	5.00%	%	$ 13,281	4.01%	%
Interest bearing NOW	59,709	15.34	0.07	61,562	17.57	0.13	61,792	18.66	0.16
Money market	31,618	8.12	2.17	33,386	9.53	1.26	33,078	9.99	0.74
Savings and club	79,452	20.41	0.45	88,727	25.32	0.44	90,853	27.44	0.49
Certificates of deposit	197,064	50.64	4.47	149,267	42.58	3.32	132,119	39.90	3.20
Total deposits	$ 389,226	100.00%	2.32%	$ 350,469	100.00%	1.67%	$ 331,123	100.00%	1.51%

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As of September 30, 2006, the aggregate amount of outstanding certificates of deposit in amounts greater than or equal to $100,000 was approximately $81.0 million. The following table sets forth the maturity of those certificates as of September 30, 2006.

	At September 30, 2006 (In thousands)
Three months or less	$ 15,157
Over three months through six months	17,882
Over six months through one year	22,969
Over one year	25,027
Total	$ 81,035

At September 30, 2006, $147.2 million of our certificates of deposit had maturities of one year or less. We monitor activity on these accounts and, based on historical experience and our current pricing strategy, we believe we will retain a large portion of these accounts upon maturity.

The following tables sets forth, by interest rate ranges, information concerning certificates of deposit.

	At September 30, 2006 Period to Maturity					
	Less Than or Equal to One Year	More Than One to Two Years	More Than Two to Three Years	More Than Three Years	Total	Percent of Total
	(Dollars in thousands)					
Interest Rate Range:						
2.00% and below	$ 49	$	$	$	$ 49	$ 0.02%
2.01% to 3.00%	3,991	670			4,661	2.22%
3.01% to 4.00%	42,910	11,314	8,683	1,860	64,767	30.90%
4.01% to 5.00%	57,345	15,300	6,024	14,695	93,364	44.56%
5.01% to 6.00%	42,949	1,911	200	1,673	46,733	22.30%
6.01% and above	3				3	%
Total	$ 147,247	$ 29,195	$ 14,907	$ 18,228	$ 209,577	$ 100%

The following table sets forth time deposits classified by interest rate at the dates indicated.

	At September 30,		
	2006	2005	2004
	(In thousands)		
Interest Rate			
2.00% and below	$ 49	$ 4,737	$ 44,520
2.01% to 3.00%	4,661	37,440	16,395
3.01% to 4.00%	64,767	80,140	24,755
4.01% to 5.00%	93,364	31,470	19,560
5.01% to 6.00%	46,733	19,131	20,783
6.01% and above	3	226	1,502
Total	$ 209,577	$ 173,144	$ 127,515

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Borrowings. Our short-term borrowings consist of Federal Home Loan Bank advances. The following table sets forth information concerning balances and interest rates on all of our short-term borrowings at the dates and for the years indicated.

	At or For the Years Ended September 30,		
	2006	2005	2004
	(Dollars in thousands)		
Balance at end of year	$ 35,299	$ 27,479	$ 11,134
Maximum outstanding at any month end	$ 35,299	$ 27,479	$ 16,878
Average balance during year	$ 21,957	$ 18,991	$ 10,388
Weighted average interest rate at end of year	5.40%	3.84%	1.96%
Average interest rate during year	4.92%	2.92%	1.36%

At September 30, 2006, we had the ability to borrow approximately $496.1 million under our credit facilities with the Federal Home Loan Bank of Pittsburgh.

Competition

We face significant competition in both originating loans and attracting deposits. The counties in which we operate have a significant concentration of financial institutions, many of which are significantly larger institutions and have greater financial resources than we, and many of which are our competitors to varying degrees. Our competition for loans comes principally from commercial banks, savings banks, mortgage banking companies, credit unions, leasing companies, insurance companies and other financial service companies. Our most direct competition for deposits has historically come from commercial banks, savings banks and credit unions. We face additional competition for deposits from nondepository competitors such as the mutual fund industry, securities and brokerage firms and insurance companies.

We seek to meet this competition by the convenience of our branch locations, emphasizing personalized banking and the advantage of local decision-making in our banking business. Specifically, we promote and maintain relationships and build customer loyalty within local communities by focusing our marketing and community involvement on the specific needs of individual neighborhoods. As of June 30, 2006 ESSA Bank & Trust had the second largest deposit market share in Monroe County, Pennsylvania. We do not rely on any individual, group, or entity for a material portion of our deposits.

Employees

As of September 30, 2006, we had 142 full-time employees and 28 part-time employees. The employees are not represented by a collective bargaining unit and we consider our relationship with our employees to be good.

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Properties

As of September 30, 2006, the net book value of our properties was $6.4 million. The following is a list of our offices:

Location	Leased or Owned	Year Acquired or Leased	Square Footage
Main Office:			
200 Palmer Street Stroudsburg, PA 18360	Owned	2003	36,000
Full Service Branches:			
Route 940 HC 1 Box 1192 Blakeslee, PA 18610	Owned	2002	2,688
Route 209 & Lake Mineola Road P.O. Box 35 Brodheadsville, PA 18301	Owned	1983	4,100
Route 209 7001 Milford Road East Stroudsburg, PA	Leased	1997	1,700
Routes 209 & 447 695 North Courtland Street East Stroudsburg, PA 18301	Leased	1999	420
75 Washington Street East Stroudsburg, PA 18301	Owned	1966	3,300
Route 209 P.O. Box 1009 Marshalls Creek, PA 18335	Leased	1991	1,560
Mount Pocono Plaza 601 Route 940 Mt. Pocono, PA 18344	Leased	1999	536
1309 Blue Valley Drive Pen Argyl, PA 18072	Leased	2001	444
744 Main Street P.O. Box L	Owned	1985	12,000

Stroudsburg, PA 18360			
Route 611 1070 North Ninth Street Stroudsburg, PA 18360	Leased	2000	488
Route 611 RR1 Box 402 Tannersville, PA 18372	Leased	1993	611
Route 209 & Weir Lake Road P.O. Box 271 Brodheadsville, PA 18322	Leased	1997	576
Other Properties			
746-752 Main Street Stroudsburg, PA 18360	Owned	2004	4,650

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Subsidiary Activities

ESSA Bank & Trust has two wholly-owned subsidiaries, ESSACOR, Inc. and Pocono Investment Company. ESSACOR, Inc. is a Pennsylvania corporation that is currently inactive. Pocono Investment Company is a Delaware corporation formed as an investment company subsidiary to hold and manage certain investments of ESSA Bank & Trust, including certain intellectual property.

Legal Proceedings

We are not involved in any pending legal proceedings other than routine legal proceedings occurring in the ordinary course of business, which, in the aggregate, involve amounts which we believe are immaterial to our consolidated financial condition and results of operations.

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REGULATION

General

ESSA Bancorp, Inc. is a Pennsylvania corporation. As a savings and loan holding company, we are required to file certain reports with, and otherwise comply with the rules and regulations of the Office of Thrift Supervision.

ESSA Bank & Trust is a Pennsylvania-chartered savings association and its deposit accounts are insured up to applicable limits by the Federal Deposit Insurance Corporation under the Deposit Insurance Fund (DIF). We are subject to extensive regulation by the Pennsylvania Department of Banking, as its chartering agency, and by the Office of Thrift Supervision, as its primary federal regulator. We must file reports with the Pennsylvania Department of Banking and the Office of Thrift Supervision concerning its activities and financial condition in addition to obtaining regulatory approvals prior to entering into certain transactions including, but not limited to, mergers with or acquisitions of other savings institutions. There are periodic examinations by the Pennsylvania Department of Banking and the Office of Thrift Supervision to test our compliance with various regulatory requirements. This regulation and supervision establishes a comprehensive framework of activities in which an institution can engage and is intended primarily for the protection of the Federal Deposit Insurance Corporation insurance fund and depositors. The regulatory structure also gives the regulatory authorities extensive discretion in connection with their supervisory and enforcement activities and with their examination policies, including policies with respect to the classification of assets and the establishment of adequate loan loss reserves for regulatory purposes. Any change in such regulation, whether by the Pennsylvania Department of Banking or the Office of Thrift Supervision could have a material adverse impact on us and our operations.

Regulation by the Pennsylvania Department of Banking

The Pennsylvania Savings Association Code of 1967, as amended (the Savings Association Code) contains detailed provisions governing the organization, location of offices, rights and responsibilities of directors, officers, employees, and depositors, as well as corporate powers, savings and investment operations and other aspects of ESSA Bank & Trust and its affairs. The Savings Association Code delegates extensive rulemaking power and administrative discretion to the Pennsylvania Department of Banking so that the supervision and regulation of state-chartered savings associations may be flexible and readily responsive to changes in economic conditions and in savings and lending practices.

One of the purposes of the Savings Association Code is to provide savings associations with the opportunity to be competitive with each other and with other financial institutions existing under other Pennsylvania laws as well as other state, federal and foreign laws. A Pennsylvania savings association may locate or change the location of its principal place of business and establish an office anywhere in Pennsylvania, with the prior approval of the Pennsylvania Department of Banking.

The Department generally examines each savings association not less frequently than once every two years. Although the Department may accept the examinations and reports of the

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Office of Thrift Supervision in lieu of the Department s examination, the current practice is for the Department to conduct individual examinations. The Department may order any savings association to discontinue any violation of law or unsafe or unsound business practice and may direct any trustee, officer, attorney, or employee of a savings association engaged in an objectionable activity, after the Department has ordered the activity to be terminated, to show cause at a hearing before the Department why such person should not be removed.

Regulation by the Office of Thrift Supervision

ESSA Bank & Trust is also subject to extensive regulation, examination and supervision by the Office of Thrift Supervision, as its primary federal regulator. Such regulation and supervision:

- establishes a comprehensive framework of activities in which the Bank can engage;
- limits the ability of ESSA Bank & Trust to extend credit to any given borrower;
- significantly limits the transactions in which ESSA Bank & Trust may engage with its affiliates;
- requires ESSA Bank & Trust to meet a qualified thrift lender test which requires ESSA Bank & Trust to invest in qualified thrift investments, which include primarily residential mortgage loans and related investments;
- places limitations on capital distributions by savings associations, such as ESSA Bank & Trust, including cash dividends;
- imposes assessments to the Office of Thrift Supervision to fund their operations;
- establishes a continuing and affirmative obligation, consistent with ESSA Bank & Trust s safe and sound operation, to help meet the credit needs of its community, including low and moderate income neighborhoods;
- establishes various capital categories resulting in various levels of regulatory scrutiny applied to the institutions in a particular category; and
- establishes standards for safety and soundness.

The Office of Thrift Supervision generally examines each savings association not less frequently than once every two years. The Office of Thrift Supervision has the authority to order any savings association or its directors, trustees, officers, attorneys or employees to discontinue any violation of law or unsafe or unsound banking practice. See - Regulatory Enforcement Authority.

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Transactions with Affiliates

Sections 23A and 23B of the Federal Reserve Act and its implementing regulations, govern transactions between depository institutions and their affiliates. These provisions are made applicable to savings associations, such as ESSA Bank & Trust, by the Home Owners Loan Act and Office of Thrift Supervision regulation. In a holding company context, the parent holding company of a savings association and any companies that are controlled by the parent holding company, are affiliates of the savings association.

Section 23A limits the extent to which the savings association or its subsidiaries may engage in certain transactions with its affiliates. These transactions include, among other things, the making of loans or other extensions of credit to an affiliate and the purchase of assets from an affiliate. Generally, these transactions between the savings association and any one affiliate cannot exceed 10% of the savings association s capital stock and surplus, and these transactions between the savings institution and all of its affiliates cannot, in the aggregate, exceed 20% of the savings institution s capital stock and surplus. Section 23A also establishes specific collateral requirements for loans or extensions of credit to an affiliate, and for guarantees or acceptances on letters of credit issued on behalf of an affiliate. Applicable regulations prohibit a savings association from lending to any affiliate engaged in activities not permissible for a bank holding company or for the purpose of acquiring the securities of most affiliates.

Section 23B requires that transactions covered by Section 23A and a broad list of other specified transactions be on terms and under circumstances substantially the same, or no less favorable to the savings association or its subsidiary, as similar transactions with non-affiliates. In addition to the restrictions on transactions with affiliates that Sections 23A and 23B of the Federal Reserve Act impose on depository institutions, the regulations of the Office of Thrift Supervision also generally prohibit a savings association from purchasing or investing in securities issued by an affiliate.

Insurance of Accounts and Regulation by the Federal Deposit Insurance Corporation

Deposit accounts in ESSA Bank & Trust are insured by the Federal Deposit Insurance Corporation generally up to a maximum of $100,000 per separately insured depositor and up to a maximum of $250,000 for self-directed retirement accounts. ESSA Bank & Trust s deposits, therefore, are subject to Federal Deposit Insurance Corporation deposit insurance assessments.

On February 15, 2006, federal legislation to reform federal deposit insurance was enacted. This new legislation required, among other things, that the Federal Deposit Insurance Corporation adopt regulations increasing the maximum amount of federal deposit insurance coverage per separately insured depositor to $130,000 (with a cost of living adjustment to become effective in five years) and modifying the deposit fund s reserve ratio for a range between 1.15% and 1.50% of estimated insured deposits.

On November 2, 2006, the Federal Deposit Insurance Corporation adopted final regulations establishing a risk-based assessment system that will enable the Federal Deposit Insurance Corporation to more closely tie each financial institution s premiums to the risk it

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poses to the deposit insurance fund. Under the new risk-based assessment system, which becomes effective in the beginning of 2007, the Federal Deposit Insurance Corporation will evaluate the risk of each financial institution based on three primary sources of information: (1) its supervisory rating, (2) its financial ratios, and (3) its long-term debt issuer rating, if the institution has one. The new rates for nearly all of the financial institution industry will vary between five and seven cents for every $100 of domestic deposits. At the same time, the Federal Deposit Insurance Corporation also adopted final regulations designating the reserve ratio for the deposit insurance fund during 2007 at 1.25% of estimated insured deposits.

Effective March 31, 2006, the Federal Deposit Insurance Corporation merged the Bank Insurance Fund (BIF) and the Savings Association Insurance Fund (SAIF) into a single insurance fund called the Deposit Insurance Fund. As a result of the merger, the BIF and SAIF were abolished. The merger of the BIF and SAIF into the Deposit Insurance Fund does not affect the authority of the Financing Corporation (FICO) to impose and collect, with approval of the Federal Deposit Insurance Corporation, assessments for anticipated payments, insurance costs and custodial fees on bonds issued by the FICO in the 1980s to recapitalize the Federal Savings and Loan Insurance Corporation. The bonds issued by the FICO are due to mature in 2017 through 2019. For the quarter ended June 30, 2006, the FICO assessment was equal to 1.28 basis points for each $100 in domestic deposits maintained at an institution.

Capital Requirements

Any savings institution that fails any of the capital requirements is subject to possible enforcement actions by the Office of Thrift Supervision. Such actions could include a capital directive, a cease and desist order, civil money penalties, the establishment of restrictions on an institution s operations, termination of federal deposit insurance, and the appointment of a conservator or receiver. Certain actions are required by law. The Office of Thrift Supervision s capital regulation provides that such actions, through enforcement proceedings or otherwise, could require one or more of a variety of corrective actions.

We are also subject to more stringent capital guidelines of the Department. Although not adopted in regulation form, the Department utilizes capital standards of 6% leverage capital and 10% risk-based capital. The components of leverage and risk-based capital are substantially the same as those defined by the Office of Thrift Supervision.

Loans-to-One Borrower Limitation

Under federal regulations, with certain limited exceptions, a Pennsylvania chartered savings association may lend to a single or related group of borrowers on an unsecured basis an amount equal to 15% of its unimpaired capital and surplus. An additional amount, equal to 10% of unimpaired capital and surplus, may be lent if such loan is secured by readily marketable collateral, which is defined to include certain securities, but generally does not include real estate. Our internal policy, however, is to not make loans either individually or in the aggregate to one entity in excess of $3.0 million in commercial relationships, nor $3.5 million in total loan relationships, including the borrower s residential mortgage and consumer loans. However, in special circumstances this limit may be exceeded subject to the approval of the Management Loan Committee in addition to a majority of the members of the Board of Directors.

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Prompt Corrective Action

Under federal regulations, a savings association is deemed to be (i) well capitalized if it has total risk-based capital of 10.0% or more, has a Tier 1 risk-based capital ratio of 6.0% or more, has a Tier I leverage capital ratio of 5.0% or more and is not subject to any written capital order or directive; (ii) adequately capitalized if it has a total risk-based capital ratio of 8.0% or more, a Tier I risk-based capital ratio of 4.0% or more and a Tier I leverage capital ratio of 4.0% or more (3.0% under certain circumstances) and does not meet the definition of well capitalized ; (iii) undercapitalized if it has a total risk-based capital ratio that is less than 8.0%, a Tier I risk-based capital ratio that is less than 4.0% or a Tier I leverage capital ratio that is less than 4.0% (3.0% under certain circumstances); (iv) significantly undercapitalized if it has a total risk-based capital ratio that is less than 6.0%, a Tier I risk-based capital ratio that is less than 3.0% or a Tier I leverage capital ratio that is less than 3.0%; and (v) critically undercapitalized if it has a ratio of tangible equity to total assets that is equal to or less than 2.0%. Federal regulations also specify circumstances under which a federal banking agency may reclassify a well capitalized institution as adequately capitalized and may require an adequately capitalized institution to comply with supervisory actions as if it were in the next lower category (except that the Office of Thrift Supervision may not reclassify a significantly undercapitalized institution as critically undercapitalized). As of September 30, 2006, the Bank was a well-capitalized institution for this purpose.

The USA PATRIOT Act

The USA PATRIOT Act of 2001 gave the federal government new powers to address terrorist threats through enhanced domestic security measures, expanded surveillance powers, increased information sharing and broadened anti-money laundering requirements. The USA PATRIOT Act also required the federal banking agencies to take into consideration the effectiveness of controls designed to combat money laundering activities in determining whether to approve a merger or other acquisition application of a member institution. Accordingly, if we engage in a merger or other acquisition, our controls designed to combat money laundering would be considered as part of the application process. We have established policies, procedures and systems designed to comply with these regulations.

Holding Company Regulation

Upon completion of the conversion, ESSA Bancorp, Inc. will be a unitary savings and loan holding company, subject to regulation and supervision by the Office of Thrift Supervision. The Office of Thrift Supervision will have enforcement authority over ESSA Bancorp and its non-savings institution subsidiaries. Among other things, this authority permits the Office of Thrift Supervision to restrict or prohibit activities that are determined to be a risk to ESSA Bank & Trust.

Under prior law, a unitary savings and loan holding company generally had no regulatory restrictions on the types of business activities in which it could engage, provided that its subsidiary savings association was a qualified thrift lender. The Gramm-Leach-Bliley Act of 1999, however, restricts unitary savings and loan holding companies not existing on, or applied

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for before, May 4, 1999 to those activities permissible for financial holding companies or for multiple savings and loan holding companies. The Company will not be a grandfathered unitary savings and loan holding company and, therefore, will be limited to the activities permissible for financial holding companies or for multiple savings and loan holding companies. A financial holding company may engage in activities that are financial in nature, including underwriting equity securities and insurance as well as activities that are incidental to financial activities or complementary to a financial activity. A multiple savings and loan holding company is generally limited to activities permissible for bank holding companies under Section 4(c)(8) of the Bank Holding Company Act, subject to the prior approval of the Office of Thrift Supervision, and certain additional activities authorized by Office of Thrift Supervision regulations.

Federal law prohibits a savings and loan holding company, directly or indirectly, or through one or more subsidiaries, from acquiring control of another savings institution or holding company thereof, without prior written approval of the Office of Thrift Supervision. It also prohibits the acquisition or retention of, with specified exceptions, more than 5% of the equity securities of a company engaged in activities that are not closely related to banking or financial in nature or acquiring or retaining control of an institution that is not federally insured. In evaluating applications by holding companies to acquire savings institutions, the Office of Thrift Supervision must consider the financial and managerial resources and future prospects of the savings institution involved, the effect of the acquisition on the risk to the insurance fund, the convenience and needs of the community, the effectiveness of each parties anti-money laundering program, and competitive factors.

Federal Securities Laws

Shares of ESSA Bancorp, Inc. s common stock are registered with the SEC under Section 12(g) of the Securities Exchange Act of 1934, as amended (the Exchange Act). ESSA Bancorp, Inc. is also subject to the proxy rules, tender offer rules, insider trading restrictions, annual and periodic reporting, and other requirements of the Exchange Act.

Sarbanes-Oxley Act of 2002

The Sarbanes-Oxley Act of 2002 was enacted in response to public concerns regarding corporate accountability in connection with certain accounting scandals. The stated goals of the Sarbanes-Oxley Act are to increase corporate responsibility, to provide for enhanced penalties for accounting and auditing improprieties at publicly traded companies, and to protect investors by improving the accuracy and reliability of corporate disclosures pursuant to the securities laws. The Sarbanes-Oxley Act generally applies to all companies that file or are required to file periodic reports with the Securities and Exchange Commission, under the Securities Exchange Act of 1934.

The Sarbanes-Oxley Act includes specific additional disclosure requirements, requires the Securities and Exchange Commission and national securities exchanges to adopt extensive additional disclosure, corporate governance and other related rules, and mandates further studies of certain issues by the Securities and Exchange Commission. The Sarbanes-Oxley Act represents significant federal involvement in matters traditionally left to state regulatory systems, such as the regulation of the accounting profession, and to corporate law, such as the relationship between a board of directors and management and between a board of directors and its committees.

Although we will incur additional expense in complying with the provisions of the Sarbanes-Oxley Act and the resulting regulations, management does not expect that such compliance will have a material impact on our results of operations or financial condition.

Regulatory Enforcement Authority

Federal law provides federal banking regulators with substantial enforcement powers. This enforcement authority includes, among other things, the ability to assess civil money penalties, to issue cease-and-desist or removal orders, and to initiate injunctive actions against banking organizations and institution-affiliated parties, as defined. In general, these enforcement actions may be initiated for violations of laws and regulations and unsafe or unsound practices. Other actions or inactions may provide the basis for enforcement action, including misleading or untimely reports filed with regulatory authorities.

Dividends

Our ability to pay dividends depends, to a large extent, upon ESSA Bank & Trust s ability to pay dividends to ESSA Bancorp. The Savings Association Code states, in part, that dividends may be declared and paid by the Bank only out of net earnings for the then current year. A dividend may not be declared or paid if it would impair the general reserves of ESSA Bank & Trust required to be maintained under the Savings Association Code. In addition, we are required to notify the Office of Thrift Supervision prior to declaring a dividend to the Company, and receive the nonobjection of the Office of Thrift Supervision to any such dividend.

TAXATION

Federal Taxation

General. ESSA Bancorp, Inc. and ESSA Bank & Trust are subject to federal income taxation in the same general manner as other corporations, with some exceptions discussed below. The following discussion of federal taxation is intended only to summarize material federal income tax matters and is not a comprehensive description of the tax rules applicable to ESSA Bancorp, Inc. and ESSA Bank & Trust.

Method of Accounting. For federal income tax purposes, ESSA Bank & Trust currently reports its income and expenses on the accrual method of accounting and uses a tax year ending September 30th for filing its consolidated federal income tax returns. The Small Business Protection Act of 1996 eliminated the use of the reserve method of accounting for bad debt reserves by savings institutions, effective for taxable years beginning after 1995.

Bad Debt Reserves. Prior to the Small Business Protection Act of 1996, ESSA Bank & Trust was permitted to establish a reserve for bad debts for tax purposes and to make annual additions to the reserve. These additions could, within specified formula limits, be deducted in arriving at ESSA Bank & Trust s taxable income. As a result of the Small Business Protection Act of 1996, ESSA Bank & Trust must use the specific charge off method in computing its bad debt deduction for tax purposes.

Taxable Distributions and Recapture. Prior to the Small Business Protection Act of 1996, bad debt reserves created prior to 1988 were subject to recapture into taxable income if ESSA Bank & Trust failed to meet certain thrift asset and definition tests. The Small Business Protection Act of 1996 eliminated these thrift-related recapture rules. However, under current law, pre-1988 reserves remain subject to tax recapture should ESSA Bank & Trust make certain distributions from its tax bad debt reserve or cease to maintain a financial institution charter. At September 30, 2006, ESSA Bank & Trust s total federal pre-1988 reserve was approximately $4.3 million. This reserve reflects the cumulative effects of federal tax deductions by ESSA Bank & Trust for which no federal income tax provision has been made.

Minimum Tax. The Internal Revenue Code of 1986, as amended, imposes an alternative minimum tax at a rate of 20% on a base of regular taxable income plus certain tax preferences, referred to as alternative minimum taxable income. The alternative minimum tax is payable to the extent alternative minimum taxable income is in excess of an exemption amount. Net operating losses can, in general, offset no more than 90% of alternative minimum taxable income. Certain payments of alternative minimum tax may be used as credits against regular tax liabilities in future years. At September 30, 2006, ESSA Bank & Trust had no minimum tax credit carryforward.

Net Operating Loss Carryovers. A financial institution may carry back net operating losses to the preceding two taxable years (five years for losses incurred in 2001 and 2002) and forward to the succeeding 20 taxable years. At September 30, 2006, ESSA Bank & Trust had no net operating loss carryforward for federal income tax purposes.

Corporate Dividends. We may exclude from our income 100% of dividends received from ESSA Bank & Trust as a member of the same affiliated group of corporations.

Audit of Tax Returns. ESSA Bank & Trust s federal income tax return for the 2004 tax year remains open.

State Taxation

Pennsylvania State Taxation. As a Pennsylvania business corporation, ESSA Bancorp, Inc. will be required to file annual returns and pay annual fees to the State of Pennsylvania.

MANAGEMENT OF ESSA BANCORP, INC.

Shared Management Structure

The directors of ESSA Bancorp, Inc. are those same persons who are the directors of ESSA Bank & Trust. In addition, each executive officer of ESSA Bancorp, Inc. is also an executive officer of ESSA Bank & Trust. We expect that ESSA Bancorp, Inc. and ESSA Bank & Trust will continue to have common executive officers until there is a business reason to establish separate management structures. To date, executive officers have been compensated for their services by ESSA Bank & Trust.

Executive Officers of ESSA Bancorp, Inc. and ESSA Bank & Trust

The following individuals are the executive officers of ESSA Bancorp, Inc. and ESSA Bank & Trust, their ages as of September 30, 2006 and the position they hold.

Name	Age	Position
Gary S. Olson	52	President and Chief Executive Officer
Allan A. Muto	46	Executive Vice President and Chief Financial Officer
Robert S. Howes, Jr.,	53	Senior Vice President, Lending Services Division
Diane K. Reimer	50	Vice President, Administrative Services Division
V. Gail Warner	50	Vice President, Retail Services Division
Thomas J. Grayuski	45	Vice President, Human Resource Services Division

The executive officers of ESSA Bancorp, Inc. are elected annually.

Directors of ESSA Bank & Trust and ESSA Bancorp, Inc.

Composition of our Board. ESSA Bancorp, Inc. has nine directors. Directors serve three-year staggered terms so that approximately one-third of the directors are elected at each annual meeting. Directors of ESSA Bank & Trust are elected by ESSA Bancorp, Inc. as its sole stockholder.

The following table states our directors names, their ages as of September 30, 2006, and the years when they began serving as directors of ESSA Bank & Trust and when their current term expires:

Name	Position(s) Held With ESSA Bancorp, Inc.	Age	Director Since	Current Term Expires
Daniel J. Henning	Director	54	1995	2007
Frederick E. Kutteroff	Director	63	2005	2007
Elizabeth B. Weekes	Director	47	2001	2007
John E. Burrus	Chairman of the Board	67	1970	2008
John S. Schoonover, Jr.	Director	65	1989	2008
Robert C. Selig, Jr.	Director	58	1990	2008
William P. Douglass	Director	64	1978	2009
Gary S. Olson	Director, President and Chief Executive Officer	52	2000	2009
William A. Viechnicki, D.D.S.	Director	62	1981	2009

The Business Background of Our Directors and Executive Officers. The business experience for the past five years of each of our directors and executive officers is set forth below. Unless otherwise indicated, directors and executive officers have held their positions for the past five years.

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Directors

John E. Burrus has served as Chairman of the Board of ESSA Bank & Trust since 1989. In 2005, Mr. Burrus retired as the owner of John E. Burrus Landscape which designs, sells, installs and maintains landscapes for private homes, and commercial properties in Monroe County, Easton and Scranton, Pennsylvania. Mr. Burrus is a graduate of Rutgers University.

William P. Douglass has been President of Douglass Enterprises, Inc., doing business as Olde Engine Works Market Place which is an antiques and collectibles co-operative. Mr. Douglass is a graduate of Texas Christian University.

Daniel J. Henning is a builder/real estate developer has been the Owner/President of A.C. Henning Enterprises, Inc., a general contract of custom built homes, multi-family townhouses and light commercial construction and renovation, since 1982. Mr. Henning is a graduate of Spring Garden College.

Frederick E. Kutteroff served as President, Chief Executive Officer of Keystone Savings Bank from 1990 until his retirement in 2003. Mr. Kutteroff holds a Certificate of Business Administration from Temple University.

Gary S. Olson has been President and Chief Executive Officer of ESSA Bank & Trust since 2000. Mr. Olson began his career at ESSA Bank & Trust in 1977. Mr. Olson is a graduate of East Stroudsburg University.

John S. Schoonover, Jr. has been a registered architect/principal in the architectural firm of Schoonover and Vanderhoof, LLC since 1978. He is a licensed architect registered to practice in Pennsylvania, New Jersey, New York and North Carolina. Mr. Schoonover served in the United States Marine Corps from 1962 through 1967.

Robert C. Selig, Jr. has served as President of Selig Construction Company since 1972. Selig Construction Company is in the business of building primary and vacation residences. Mr. Selig is a graduate of West Side Area Vocational/Technical School.

William A. Viechnicki, D.D.S. has been in the private practice of orthodontics in East Stroudsburg, Pennsylvania since 1971. Dr. Viechnicki is a graduate of Pennsylvania State University and Temple University School of Dentistry where he serves as a professor of orthodontics.

Elizabeth B. Weekes has been a partner in the law firm Bensinger and Weekes, P.A. since 1987. Ms. Weekes practice focuses on real estate, civil litigation, domestic relations, banking, municipalities and estates. Ms. Weekes is a graduate of Colgate University and Dickinson School of Law.

Executive Officers of ESSA Bank & Trust Who Are Not Also Directors

Allan A. Muto has been the Executive Vice President and Chief Financial Officer of ESSA Bank & Trust since January 2006. Prior to that time Mr. Muto served as Executive Vice

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President, Chief Operating Officer beginning in 2001. Mr Muto previously served as Senior Vice President, Chief Financial Officer at Pioneer American Bank, N.A. in Carbondale, Pennsylvania.

Robert S. Howes, Jr. has been with ESSA Bank & Trust in various capacities since 1985 and has been Senior Vice President, Lending Services Division since 2001. Previously, Mr. Howes served as Branch Manager at Franklin First Federal Savings and Loan Association in Wilkes-Barre, Pennsylvania.

Diane K. Reimer has been Vice President, Administrative Services Division since 1998 and first joined ESSA Bank & Trust in 1983.

V. Gail Warner has been Vice President, Retail Services Division since 1999. Previously, Ms. Warner served as Assistant Vice President, Branch Sales Manager at First Eastern Bank in Mount Pocono, Pennsylvania.

Thomas J. Grayuski has been Vice President, Human Resources Services Division since 2000. Previously, Mr. Grayuski was the Senior Personnel Management Specialist at the United States Army Armament Research, Development and Engineering Center in Dover, New Jersey.

Meetings and Committees of the Board of Directors of ESSA Bancorp, Inc.

We conduct business through meetings of our Board of Directors and its committees. During the fiscal year ended September 30, 2006, the Board of Directors of ESSA Bancorp, Inc. did not meet and the Board of Directors of ESSA Bank & Trust met 13 times. The Board of Directors of ESSA Bancorp, Inc. has established the following standing committees: the Compensation Committee, the Corporate Governance Committee and the Audit Committee.

The Audit Committee, currently consisting of Messrs. Henning (Chair), Douglass, Kutteroff and Viechnicki, is responsible for providing oversight relating to our financial statements and financial reporting process, systems of internal accounting and financial controls, internal audit function, annual independent audit and the compliance and ethics programs established by management and the board. Each member of the Audit Committee is independent in accordance with the listing standards of the Nasdaq Stock Market. The Board of Directors believes that Mr. Kutteroff qualifies as an audit committee financial expert as that term is defined in the rules and regulations of the Securities and Exchange Commission. The Audit Committee of ESSA Bank & Trust met four times in fiscal year 2006.

The Compensation Committee, currently consisting of Messrs. Douglass (Chair), Burrus, Viechnicki and Olson and Ms. Weekes, is responsible for human resources policies, salaries and benefits, incentive compensation, executive development and management succession planning. Each member of the Compensation Committee, except for Mr. Olson, is independent in accordance with the listing standards of the Nasdaq Stock Market.

The Corporate Governance Committee, currently consisting of Messrs. Douglass (Chair), Henning, Selig, Burrus and Olson and Ms. Weekes, is responsible for identifying individuals qualified to become board members and recommending a group of nominees for election as directors at each annual meeting of stockholders, ensuring that the board and its committees have the benefit of qualified and experienced independent directors, and developing a set of corporate governance policies and procedures.

Each of these committees operates under a written charter, which governs its composition, responsibilities and operations.

In addition, ESSA Bank & Trust maintains an Operations Committee (chaired by Mr. Selig), ALCO/Investment Committee (chaired by Mr. Viechnicki), Trust Audit Committee (chaired by Mr. Schoonover) and Trust Committee (chaired by Ms. Weekes) and an Executive Committee.

Corporate Governance Policies and Procedures

In addition to having established committees of the Board of Directors, ESSA Bancorp, Inc. has adopted policies to govern the activities of both ESSA Bancorp, Inc. and ESSA Bank & Trust, including a corporate governance policy and a code of business conduct and ethics. The corporate governance policy sets forth:

- the duties and responsibilities of each director;
- the composition, responsibilities and operation of the Board of Directors;
- the establishment and operation of board committees, including audit, nominating and compensation committees;
- succession planning;
- convening executive sessions of independent directors;
- the Board of Directors interaction with management and third parties; and
- the evaluation of the performance of the Board of Directors and the chief executive officer.

ESSA Bancorp, Inc. has adopted a code of ethics that applies to its principal executive officer, principal financial officer, principal accounting officer and persons performing similar functions. The code of ethics is designed to deter wrongdoing and to promote honest and ethical conduct, the avoidance of conflicts of interest, full and accurate disclosure and compliance with all applicable laws, rules and regulations.

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Director Fees

Director Fees. Each of the individuals who serves as a director of ESSA Bancorp, Inc. also serves as a director of ESSA Bank & Trust and earns director fees in that capacity. Each non-employee director (except for the Chairman of the Board) is paid a fee of $2,000 per month for their service and $1,000 for each Board meeting attended. In addition, the Chairperson of a committee is paid $750 for each committee meeting attended and committee members are paid $500 for each committee meeting attended. In lieu of the above mentioned fees, the Chairman of the Board is paid an annual retainer of $60,000 and $1,500 for each Board meeting attended. The Chairman of the Board is not compensated for attendance at any committee meetings.

Executive Officer Compensation

Summary Compensation Table. The following table sets forth for the fiscal year ended September 30, 2006, certain information as to the total remuneration paid by ESSA Bank & Trust to its Chief Executive Officer as well as to the four most highly compensated executive officers of ESSA Bank & Trust, other than the Chief Executive Officer, who received total annual salary and bonus in excess of $100,000. Each of the individuals listed in the table below is referred to as a Named Executive Officer.

		Annual Compensation (1)			
Name and Principal Position	**Fiscal Year**	**Salary (2)**	**Bonus**	**Other Annual Compensation (3)**	**All Other Compensation (4)**
Gary S. Olson, President and Chief Executive Officer	2006	$ 201,500	$ 94,000		$ 18,700
Allan A. Muto, Executive Vice President and Chief Financial Officer	2006	$ 131,500	$ 49,000		$ 11,900
Robert S. Howes, Jr., Senior Vice President, Lending Services Division	2006	$ 112,800	$ 37,000		$ 10,800
V. Gail Warner, Vice President, Retail Services Division	2006	$ 103,500	$ 34,000		$ 11,900
Diane K. Reimer, Vice President, Administrative Services Division	2006	$ 92,700	$ 26,000		$ 12,800

(1) Summary compensation information is excluded for the fiscal years ended September 30, 2005 and 2004, as ESSA Bancorp, Inc. was not a public company during those periods.

(2) Current base salaries for Messrs. Olson, Muto and Howes and Mmes. Warner and Reimer are $211,900, $141,700, $117,100, $111,500 and $97,200, respectively.

(3) ESSA Bank & Trust provides certain of its executive officers with non-cash benefits and perquisites. Management believes that the aggregate value of these benefits for fiscal year 2006 did not, in the case of the named executive officers, exceed the greater of $50,000 or 10% of the aggregate salary and annual bonus reported for them in the Summary Compensation Table.

(4) Represents employer contributions under ESSA Bank & Trust s 401(k) Plan for Named Executive Officer as well as health, life and disability insurance premiums.

Benefit Plans

Employment Agreements. ESSA Bancorp, Inc. intends to enter into employment agreements with each of Messrs. Olson, Muto, Howes and Grayuski and Ms. Warner and Ms. Reimer. The agreements with Messrs. Olson and Muto will have an initial term of three years. The agreements with Messrs. Howes and Grayuski and Ms. Warner and Ms. Reimer will have terms of two years. Unless notice of non-renewal is provided, the agreements renew annually. Under the agreements, the initial base salaries for Messrs. Olson, Muto, Howes, Ms. Warner, Ms. Reimer and Mr. Grayuski are $211,900, $141,700, $117,100, $111,500, $97,200 and $80,000, respectively. Base salaries will be reviewed at least annually and may be increased, but not

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decreased. In addition to the base salary, each agreement will provide for, among other things, participation in bonus programs and other employee pension benefit and fringe benefit plans applicable to executive employees and use of an automobile (in the case of Mr. Olson). The executive s employment may be terminated for cause at any time, in which event the executive would have no right to receive compensation or other benefits for any period after termination.

Each of the executives is entitled to severance payments and benefits in the event of his or her termination of employment under specified circumstances. In the event the executive s employment is terminated for reasons other than for cause, disability or retirement, or in the event the executive resigns within 90 days following (1) the failure to elect or reelect or to appoint or reappoint the executive to his executive position, (2) a material change in the executive s functions, duties, or responsibilities, which change would cause executive s position to become one of lesser responsibility, importance or scope, (3) the relocation of executive s principal place of employment to a location that is more than 50 miles from the location of the Bank s principal executive offices as of the date of the agreement, (4) a material reduction in benefits and perquisites including base salary (except for any Bank-wide or officer-wide reduction), (5) the liquidation or dissolution of ESSA Bancorp, Inc. or ESSA Bank & Trust, (6) a change in control of ESSA Bancorp, Inc. or (7) a breach of the employment agreement by ESSA Bancorp, Inc., the executive would be entitled to a severance payment equal to three times (in the case of Messrs. Olson and Muto, two times for Mr. Howes, Ms. Warner, Ms. Reimer and Mr. Grayuski) the sum of the executive s base salary and the highest rate of bonus awarded to the executive during the prior three years, payable in a lump sum. In addition, the executive would be entitled, at ESSA Bancorp, Inc. s sole expense, to the continuation of life, medical, dental, vision and disability coverage for 36 months (in the case of Messrs. Olson and Muto; twenty-four months for all other executives) after termination of the agreement. The executive would also receive a lump sum payment of the excess, if any, of the present value of the benefits he would be entitled to under the ESSA Bancorp, Inc. or ESSA Bank & Trust s defined benefit pension plan if he had continued working for ESSA Bancorp, Inc. for 36 months (in the case of Messrs. Olson and Muto; twenty-four months for all other executives) over the present value of the benefits to which he is actually entitled as of the date of termination. In the event that the severance payment provisions of the employment agreement are triggered for one of the covered executives at September 30, 2006, the executive would be entitled to a cash severance benefit in the amount of approximately $__________, $__________, $__________, $__________ and $__________, in the case of Messrs. Olson, Muto, Howes, Ms. Warner, Ms. Reimer or Mr. Grayuski, respectively. The executive would be entitled to no additional benefits under the employment agreement upon retirement at age 65.

Upon termination of the executive s employment other than in connection with a change in control, the executive agrees not to compete with ESSA Bancorp, Inc. for one year following termination of employment within 50 miles of any existing branch of ESSA Bank & Trust or 50 miles of any office for which ESSA Bank & Trust or a subsidiary has filed an application for regulatory approval. Should the executive become disabled, ESSA Bancorp, Inc. would continue to pay the executive his base salary for the longer of the remaining term of the agreement or one year, provided that any amount paid to the executive pursuant to any disability insurance would reduce the compensation he would receive. In the event the executive dies while employed by ESSA Bancorp, Inc., the executive s estate will be paid the executive s base salary for one year and the executive s family will be entitled to continuation of medical, dental and vision benefits for one year after the executive s death.

The employment agreements for Messrs. Howes and Grayuski and Ms. Warner and Ms. Reimer also provide for an automatic reduction in the amount of any payments made in connection with a change in control which would otherwise constitute excess parachute payments under Section 280G of the Internal Revenue Code. The total payment owed to the executive upon a change in control will be reduced to an amount that is $1.00 less than the amount that would otherwise be an excess parachute payment under Code Section 280G. Messrs. Olson and Muto may elect to have such reductions made in their sole discretion.

Change-in-Control Agreements. ESSA Bancorp, Inc. intends to enter into change-in-control agreements with up to six officers who are not entering into employment agreements, which would provide certain benefits in the event of a termination of employment following a change in control of ESSA Bancorp, Inc. or ESSA Bank & Trust. Each of the change-in-control agreements provides for a term of eighteen months. Commencing on each anniversary date, the agreements will be renewed for an additional year so that the remaining term will be eighteen months, subject to notice of non-renewal. The change-in-control agreements enable ESSA Bancorp, Inc. to offer to designated officers certain protections against termination without cause in the event of a change in control (as defined in the agreements). Such protections are frequently offered by other financial institutions, and ESSA Bancorp, Inc. may be at a competitive disadvantage in attracting and retaining key employees if it does not offer similar protections.

Following a change in control of ESSA Bancorp, Inc. or ESSA Bank & Trust, an officer is entitled under the agreement to a payment if the officer s employment is terminated during the term of such agreement, other than for cause, or if the officer voluntarily terminates employment during the term of such agreement as a result of a demotion, loss of title, office or significant authority (in each case, other than as a result of the fact that either ESSA Bank & Trust or ESSA Bancorp, Inc. is merged into another entity in connection with a change in control and will not operate as a stand-alone, independent entity), reduction in his annual compensation or benefits, or relocation of his or her principal place of employment by more than 30 miles from its location immediately prior to the change in control. In the event an officer who is a party to a change-in-control agreement is entitled to receive payments pursuant to the change-in-control agreement, he will receive a cash payment equal to 1.5 times his or her highest rate of base salary and the highest rate of bonus awarded to the executive during the prior two years, payable in a lump sum. In addition to the cash payment, each covered officer is entitled to receive life, medical, and dental coverage for a period of 18 months from the date of termination. Notwithstanding any provision to the contrary in the change-in-control agreement, payments under the change in control agreements are limited so that they will not constitute an excess parachute payment under Section 280G of the Internal Revenue Code.

Director Emeritus Plan. ESSA Bank & Trust maintains a director emeritus plan. Any director who is not an active employee of ESSA Bank & Trust upon retirement from board service as of the next annual meeting following his or her attainment of age 74, is eligible to participate in the plan. In order to receive retirement benefits under the plan, the director must remain a director emeritus in good standing after retirement, must agree to attend meetings if

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requested, provide advice and act as a goodwill ambassador (as requested) by the Board of Directors and must not engage in any business enterprise which competes with ESSA Bank & Trust nor disclose any confidential information relative to the business of ESSA Bank & Trust. At retirement, an eligible director will receive the then-current monthly Board meeting fee for five additional years (the current monthly board meeting fee for directors is $1,000). At retirement, the Chairman of the Board, will continue to receive the then-current monthly Board meeting fee for five additional years (the current monthly Chairman s Board meeting fee is $1,500).

Defined Benefit Pension Plan. Since 1969, ESSA Bank & Trust has maintained an individually designed, tax-qualified defined benefit plan (the Pension Plan). Effective January 1, 2007, the Plan operates on a calendar year basis. Effective January 1, 2007, the Pension Plan will be operated on a calendar year basis. All employees age 21 or older who have completed one year of employment with ESSA Bank & Trust are eligible for membership in the Pension Plan; however, only employees who have been credited with 1,000 or more hours of service with ESSA Bank & Trust are eligible to accrue benefits under the Pension Plan. ESSA Bank & Trust annually contributes an amount to the plan necessary to satisfy the minimum funding requirements established under the Employee Retirement Income Security Act of 1974, as amended (ERISA).

The regular form of retirement benefit is a straight life annuity (if single) and a joint and survivor annuity (if married), however, various alternative forms of joint and survivor annuities may be selected instead. Upon termination of employment at or after age 65 with at least 5 years of employment, a participant is entitled to a normal retirement annual benefit equal to a percentage of average monthly compensation determined over the participant s high 5-year average salary during the 10 years before the participant s retirement. If the participant terminates employment on or after attaining age 60 with 15 years of service, his normal retirement benefit will be reduced by 0.5% for each month by which the participant s actual retirement date precedes his or her normal retirement date. A participant may postpone retirement beyond normal retirement date, in which case the participant will continue earning service towards his or her accrued benefit. If a married participant dies while in active service and after having become fully vested (i.e., completed 5 years of service), a qualified 50% survivor spouse benefit will be payable to the participant s beneficiary. No pre-retirement death benefits are available to unmarried participants. Upon termination of employment due to disability, the participant will be entitled to an early or normal retirement benefit, where the participant s accrued benefit is determined based on service performed through the disability date.

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The following table indicates the annual retirement benefit that would be payable under the plan upon retirement at age 65 during the plan year ended November 30, 2006, expressed in the form of a single life annuity for the final average salary and benefit service classification specified below:

Final Average	Years of Benefit Service and Benefit Payable at Retirement				
Annual Compensation	5	10	20	30	40
$ 10,000	$ 750	$ 1,500	$ 3,000	$ 4,500	$ 5,000
$ 30,000	$ 2,250	$ 4,500	$ 9,000	$ 13,500	$ 15,000
$ 60,000	$ 4,500	$ 9,000	$ 18,000	$ 27,000	$ 30,000
$ 90,000	$ 6,750	$ 13,500	$ 27,000	$ 40,500	$ 45,000
$ 120,000	$ 9,000	$ 18,000	$ 36,000	$ 54,000	$ 60,000
$ 150,000	$ 11,250	$ 22,500	$ 45,000	$ 67,500	$ 75,000
$ 160,000	$ 12,000	$ 24,000	$ 48,000	$ 72,000	$ 80,000
$ 170,000	$ 12,750	$ 25,500	$ 51,000	$ 76,500	$ 85,000
$ 200,000	$ 15,000	$ 30,000	$ 60,000	$ 90,000	$ 100,000
$ 220,000 and above(1)	$ 16,500	$ 33,000	$ 66,000	$ 99,000	$ 110,000

(1) Reflects the maximum benefit payable under the Defined Benefit Pension Plan due to tax law limitations.

At November 30, 2006, Messrs. Olson, Muto, Howes, Ms. Warner and Ms. Reimer had 29, 5, 20, 12 and 23 years of credited service, respectively, under the plan.

401(k) Plan. ESSA Bank & Trust maintains a non-standardized prototype 401(k) plan through Massachusetts Mutual Life Insurance Company (MassMutual). Effective January 1, 2007, the 401(k) plan will be operated on a calendar year basis. Employees may participate in the plan when they have attained age 21 and completed one year of service and have been credited with 1,000 hours during the year of service. Participants may make pre-tax salary deferrals to the plan not to exceed $15,500 (which is the 2007 limit; the limit is adjusted annual for IRS-announced cost-of-living increases). In addition, participants who are 50 or older may make pre-tax catch up contributions to the plan up to $5,000 (this limit is also adjusted annually by the IRS for cost-of-living increases). The plan is a 401(k) safe harbor which means that the employer matches participant pre-tax salary deferrals dollar for dollar up to 3% of compensation, then the employer matches pre-tax salary deferrals at the rate of 50 cents on the dollar for amounts up to 5% of compensation. All contributions are 100% vested. Distributions will be made upon death, disability, termination of employment, or attainment of age 59 1/2. In addition to the other self-directed investment alternatives offered under the plan, Participants will be offered the opportunity to purchase stock in the offering through a unitized employer stock fund, consisting of 95% stock and 5% cash. Benefits are paid in the form of lump sum, installments, partial withdrawals, or a joint and 100% survivor annuity.

Supplemental Retirement Plan. ESSA Bank & Trust has entered into Executive Salary Continuation Agreements (Supplemental Retirement Plan) with Mr. Olson, Ms. Reimer, Mr. Howes and Mr. Grayuski. If the designated executive has been employed with ESSA Bank & Trust for at least 30 years upon normal retirement age (65) or early retirement age (60), then the benefit described in the agreement will be paid to the executive for no less than 192 months following the executive s retirement, unless the executive elects to receive the present value of the payments as a lump sum. The amount of the normal benefit equals 70% of the executive s final compensation determined over the participant s high 5-year average salary during the 10 years before the participant s retirement. The normal retirement benefit is reduced by 0.05% for each month the executive terminates employment after early retirement age but prior to normal retirement age. If the executive voluntarily terminates employment before age 65 or has his or her employment involuntarily terminated other than for cause, the employer shall pay in a lump sum or 60 monthly installments, the amount accrued to fund the promised benefit as of the date of such termination. If a change in control occurs, then the benefits promised under the Supplemental Retirement Plan at normal retirement age will be paid to the executive at normal retirement age, even if the executive s employment terminates before normal retirement age (except no payment shall be made if the termination is due to cause). Benefits become vested after 5 years of service and before completing 5 years of service, benefits are zero percent vested. If the executive dies while actively employed by us, but before attaining age 65, the amount accrued under the plan as of the executive s date of death will be paid to the executive s designated beneficiaries. If the executive dies after the commencement of payment of benefits under the Supplemental Retirement Plan, remaining payments will be made to the executive s beneficiaries. We recorded an expense of $160,155 for the Supplemental Retirement Plan during the fiscal year ended September 30, 2006.

Stock Benefit Plans

Employee Stock Ownership Plan and Trust. We intend to implement an employee stock ownership plan in connection with the stock offering. As part of the stock offering, the employee stock ownership plan trust intends to borrow funds from ESSA Bancorp, Inc. and use those funds to purchase a number of shares equal to 8% of the common stock sold in the stock offering and issued to the Charitable Foundation. Collateral for the loan will be the common stock purchased by the employee stock ownership plan. The loan will be repaid principally from discretionary contributions by ESSA Bank & Trust to the employee stock ownership plan over a period of up to 30 years. The loan documents will provide that the loan may be repaid over a shorter period, without penalty for prepayments. We anticipate that the interest rate on the loan will equal the prime interest rate at the closing of the stock offering, and will adjust annually at the beginning of each calendar year. Shares purchased by the employee stock ownership plan will be held in a suspense account for allocation among participants as the loan is repaid.

Shares released from the suspense account will be allocated among employee stock ownership plan participants on the basis of compensation in the year of allocation. Benefits under the plan will not vest at all until a participant has three years of credited service at which time participants will become fully vested. Credit will be given for vesting purposes to participants for years of service with ESSA Bank & Trust prior to the adoption of the plan. A participant s interest in his account under the plan will also fully vest in the event of termination of service due to a participant s early or normal retirement, death, disability, or upon a change in control (as defined in the plan). Vested benefits will be payable generally in the form of common stock, or to the extent participants accounts contain cash, benefits will be paid in cash. ESSA Bank & Trust s contributions to the employee stock ownership plan are discretionary, subject to the loan terms and tax law limits. Therefore, benefits payable under the employee stock ownership plan cannot be estimated. Pursuant to SOP 93-6, we will be required to record compensation expense each year in an amount equal to the fair market value of the shares released from the suspense account. In the event of a change in control, the employee stock ownership plan will terminate.

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Transactions with Certain Related Persons

Loans and Extensions of Credit. The Sarbanes-Oxley Act of 2002 generally prohibits us from making loans to our executive officers and directors, but it contains a specific exemption from such prohibition for loans made by ESSA Bank & Trust to our executive officers and directors in compliance with federal banking regulations. Federal regulations require that all loans or extensions of credit to executive officers and directors of insured institutions must be made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other persons and must not involve more than the normal risk or repayment or present other unfavorable features. ESSA Bank & Trust is therefore prohibited from making any loans or extensions of credit to executive officers and directors at different rates or terms than those offered to the general public, except for loans made under a benefit program generally available to all other employees and that does not give preference to any executive officer or director over any other employee.

In addition, loans made to a director or executive officer must be approved in advance by a majority of the disinterested members of the Board of Directors. The aggregate amount of our loans to our officers and directors and their related entities was $2.0 million at September 30, 2006. As of September 30, 2006, these loans were performing according to their original terms.

Benefits to be Considered Following Completion of the Conversion

We intend to adopt and request stockholder approval of one or more stock-based incentive plans, including a stock option plan and a stock recognition and retention plan, no earlier than six months after the completion of the conversion. The stock option plan and stock recognition and retention plan may be established as separate plans or part of a single stock-based incentive plan.

Stock Option Plan. If adopted within one year of the conversion and approved by stockholders, the stock option plan would reserve an amount equal to 10% of the shares of common stock sold in the offering for issuance upon exercise of stock options. 10% of the shares of common stock issued in the offering would amount to 1,000,450 shares, 1,177,000 shares, 1,353,550 shares and 1,556,583 shares at the minimum, midpoint, maximum and adjusted maximum of the offering range, respectively. If we adopt the stock option plan after one year following the completion of the conversion, we may grant options in an amount greater than 10% of the shares of common stock sold in the offering. We have not yet determined whether we will present this plan for stockholder approval within 12 months following the completion of the conversion or whether we will present this plan for stockholder approval more than 12 months following the completion of the conversion. No options would be granted under the new stock option plan until stockholder approval of the plan is received. In the event that shares underlying options come from authorized but unissued shares of common stock, stockholders would experience dilution of approximately 9.1% of their ownership interest in ESSA Bancorp, Inc. We will have to recognize compensation expense for accounting purposes ratably over the vesting period, equal to the fair value of the options on the original grant date.

The exercise price of the options granted under the stock option plan will be equal to the fair market value of ESSA Bancorp, Inc. common stock on the date of grant of the stock options.

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If the stock option plan is adopted within one year following the conversion, options may vest no faster than 20% per year beginning 12 months after the date of grant. Options granted under the stock option plan would be adjusted for capital changes such as stock splits and stock dividends. Awards will be 100% vested upon termination of employment due to death, disability or following a change in control, and if the stock option plan is adopted more than one year after the conversion, awards would be 100% vested upon normal retirement. Under Office of Thrift Supervision regulations, if the stock option plan is adopted within one year of the conversion, no individual officer may receive more than 25% of the awards under the plan, no non-employee director may receive more than 5% of the awards under the plan and all non-employee directors as a group may receive in the aggregate no more than 30% of the awards under the plan.

The stock option plan would be administered by a committee of non-employee members of ESSA Bancorp, Inc. s Board of Directors. Options granted under the stock option plan to employees may be incentive stock options, which are designed to result in a beneficial tax treatment to the employee but no tax deduction to ESSA Bancorp, Inc. Non-qualified stock options may also be granted to employees under the stock option plan, and will be granted to the non-employee directors who receive stock options. In the event an option recipient terminated his or her employment or service as an employee or director, the options would terminate after certain specified periods following termination.

Stock Recognition and Retention Plan. If adopted within one year of the conversion and approved by stockholders, the stock recognition and retention plan would reserve an amount equal to 4% of the shares of common stock sold in the offering, or 400,180 shares, 470,800 shares, 541,420 shares and 622,633 shares at the minimum, midpoint, maximum and adjusted maximum of the offering range, respectively. If we adopt the recognition and retention plan after one year following the completion of the conversion, we may grant shares in an amount greater than 4% of the shares of common stock sold in the offering. We have not yet determined whether we will present this plan for stockholder approval within 12 months following the completion of the conversion or whether we will present this plan for stockholder approval more than 12 months following the completion of the conversion. We must recognize an expense for shares of common stock awarded over their vesting period at the fair market value of the shares on the date they are awarded. The recipients will be awarded shares of common stock under the stock recognition and retention plan at no cost to them. No awards would be made under the stock recognition and retention plan until the plan is approved by stockholders. If the shares awarded under the stock recognition and retention plan come from authorized but unissued shares of the common stock totaling 4% of the shares sold in the offering, stockholders would experience dilution of approximately 3.8% in their ownership interest in ESSA Bancorp, Inc.

Awards granted under the stock recognition and retention plan would be nontransferable and nonassignable. Under Office of Thrift Supervision regulations, if the stock recognition and retention plan is adopted within one year following the conversion, the shares of common stock which are subject to an award may vest no faster than 20% per year beginning 12 months after the date of grant of the award. Awards would be adjusted for capital changes such as stock dividends and stock splits. Awards would be 100% vested upon termination of employment or service due to death, disability or following a change in control, and if the stock recognition and retention plan is adopted more than one year after the conversion, awards also would be 100% vested upon normal retirement. Under Office of Thrift Supervision rules, if the stock recognition

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and retention plan is adopted within one year of the conversion, no individual officer may receive more than 25% of the awards under the plan, no non-employee director may receive more than 5% of the awards under the plan, and all non-employee directors as a group may receive no more than 30% of the awards under the plan in the aggregate.

The recipient of an award will recognize income equal to the fair market value of the stock earned, determined as of the date of vesting, unless the recipient makes an election under Section 83(b) of the Internal Revenue Code of 1986, as amended, to be taxed earlier. The amount of income recognized by the recipient would be a deductible expense of ESSA Bancorp, Inc. for tax purposes.

SUBSCRIPTIONS BY DIRECTORS AND EXECUTIVE OFFICERS

The following table sets forth information regarding intended common stock subscriptions by each of the directors and executive officers of ESSA Bank & Trust and their associates, and by all directors and executive officers as a group. In the event the individual maximum purchase limitation is increased, persons subscribing for the maximum amount may increase their purchase order. Directors and executive officers will purchase shares of common stock at the same $10.00 purchase price per share and on the same terms as other purchasers in the offering. This table excludes shares of common stock to be purchased by the employee stock ownership plan, as well as any recognition and retention plan awards or stock option grants that may be made no earlier than six months after the completion of the offering. The directors and officers have indicated their intention to subscribe in the offering for an aggregate of $4.3 million of shares of common stock, equal to 4.6% of the number of shares of common stock to be sold in the offering at the minimum of the offering range, assuming shares are available. Purchases by directors, executive officers and their associates will be included in determining whether the required minimum number of shares has been subscribed for in the offering.

Name	Number of Shares (1)	Aggregate Purchase Price (1)	Percent at Midpoint
John E. Burrus	10,000	$ 100,000	*%
William P. Douglass	15,000	150,000	*
Daniel J. Henning	50,000	500,000	*
Frederick E. Kutteroff	25,000	250,000	*
Gary S. Olson	50,000	500,000	*
John S. Schoonover, Jr.	2,000	20,000	*
Robert C. Selig, Jr.	50,000	500,000	*
William A. Viechnicki, D.D.S.	50,000	500,000	*
Elizabeth B. Weekes	5,000	50,000	*
Allan A. Muto	25,000	250,000	*
Robert S. Howes, Jr.	20,000	200,000	*
Diane K. Reimer	45,000	450,000	*
V. Gail Warner	35,000	350,000	*
Thomas J. Grayuski	45,000	450,000	*
All directors and executive officers as a group	427,000	$4.27 million	4.6%

* Less than 1%.

(1) Includes purchases by the individual s spouse and other relatives of the named individual living in the same household. The above named individuals are not aware of any other purchases by a person who, or entity which, would be considered an associate of the named individuals under the Plan of Conversion.

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THE CONVERSION

The Boards of Directors of ESSA Bancorp, Inc. and ESSA Bank & Trust have approved the plan of conversion. The plan of conversion must also be approved by the members of ESSA Bank & Trust (depositors and certain borrowers of ESSA Bank & Trust at _______). A special meeting of members has been called for this purpose. The Office of Thrift Supervision and the Pennsylvania Department of Banking have each conditionally approved the plan of conversion; however, such approval does not constitute a recommendation or endorsement of the plan of conversion by that agency.

General

Pursuant to the plan of conversion, ESSA Bank & Trust will convert from mutual to stock form and will be wholly owned by ESSA Bancorp, Inc., a new Pennsylvania corporation. When the conversion is completed, all of the capital stock of ESSA Bank & Trust will be owned by ESSA Bancorp, Inc., our newly formed Pennsylvania holding company, and all of the common stock of ESSA Bancorp, Inc. will be owned by public stockholders.

We intend to retain between $91.5 million and $124.2 million of the net proceeds of the offering, or $143.1 million if the offering range is increased by 15%, and to contribute the balance of the net proceeds to ESSA Bank & Trust. The conversion will be consummated only upon the issuance of at least 9,350,000 shares of our common stock offered pursuant to the plan of conversion.

The plan of conversion provides that we will offer shares of common stock for sale in the subscription offering to eligible account holders, our tax-qualified employee benefit plans, including the employee stock ownership plan and our 401(k), supplemental eligible account holders and other members (depositors and certain borrowers of ESSA Bank & Trust). If all shares are not subscribed for in the subscription offering, we may, at our discretion, offer common stock for sale in a community offering to members of the general public, with a preference given to natural persons residing in the Pennsylvania Counties of Monroe and Northampton.

We have the right to accept or reject, in whole or in part, any orders to purchase shares of the common stock received in the community offering. The community offering, if any, may begin at the same time as, during, or after the subscription offering, and must be completed within 45 days after the completion of the subscription offering unless otherwise extended by us with the approval of the Office of Thrift Supervision. See Community Offering.

We determined the number of shares of common stock to be offered in the offering based upon an independent valuation appraisal of the estimated consolidated pro forma market value of ESSA Bancorp, Inc. All shares of common stock to be sold in the offering will be sold at $10.00 per share. Investors will not be charged a commission to purchase shares of common stock in the offering. The independent valuation will be updated and the final number of the shares of common stock to be issued in the offering will be determined at the completion of the offering. See Determination of Share Price and Number of Shares to be Issued for more information as to the determination of the estimated pro forma market value of the common stock.

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The following is a brief summary of the conversion and is qualified in its entirety by reference to the provisions of the plan of conversion. A copy of the plan of conversion is available for inspection at each branch office of ESSA Bank & Trust and at the Northeast Regional and the Washington, D.C. offices of the Office of Thrift Supervision. The plan of conversion is also filed as an exhibit to ESSA Bank & Trust s application to convert from mutual to stock form of which this prospectus is a part, copies of which may be obtained from the Office of Thrift Supervision. See Where You Can Find Additional Information.

Reasons for the Conversion

The primary reasons for the conversion and related stock offering are:

- to support our internal growth through lending in communities we serve or may serve in the future;
- to enhance our existing products and services and to support the development of new products and services;
- to improve our overall competitive position;
- to provide additional financial resources to pursue limited *de novo* branching opportunities and future acquisition opportunities;
- to reduce a portion of our existing borrowings;
- to provide better capital management tools, including the ability to pay dividends and to repurchase shares of our common stock; and
- to retain and attract qualified personnel by establishing stock benefit plans for management and employees, including a stock option plan, a stock recognition and retention plan and an employee stock ownership plan.

In the stock holding company structure, we will have greater flexibility in structuring mergers and acquisitions. Potential sellers often want stock for at least part of the acquisition consideration. Our new stock holding company structure will enable us to offer stock or cash consideration, or a combination thereof, and will therefore enhance our ability to compete with other bidders when acquisition opportunities arise.

We have no current arrangements or agreements to acquire other banks, thrifts and financial service companies or branch offices. We have received regulatory approval to open a new branch office in Tannersville, Pennsylvania which we anticipate opening in May 2007. There can be no assurance that we will be able to consummate any acquisitions or establish any additional new branches.

Approvals Required

The affirmative vote of a majority of the total eligible votes of the members of ESSA Bank & Trust at the special meeting of members is required to approve the plan of conversion.

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The members of ESSA Bank & Trust will also be asked to approve the establishment and funding of ESSA Bank & Trust Foundation. The plan of conversion also must be approved by the Office of Thrift Supervision and the Pennsylvania Banking Department, which have each given its conditional approval.

A special meeting of members to consider and vote upon the plan of conversion and the charitable foundation has been set for __________.

Effects of Conversion on Depositors, Borrowers and Members

Continuity. While the conversion is being accomplished, the normal business of ESSA Bank & Trust of accepting deposits and making loans will continue without interruption. ESSA Bank & Trust will continue to be a Pennsylvania chartered savings association and will continue to be regulated by the Pennsylvania Department of Banking. After the conversion, ESSA Bank & Trust will continue to offer existing services to depositors, borrowers and other customers. The directors serving ESSA Bank & Trust, at the time of the conversion will be the directors of ESSA Bancorp, Inc., a Pennsylvania corporation, and ESSA Bank & Trust after the conversion.

Effect on Deposit Accounts. Pursuant to the plan of conversion, each depositor of ESSA Bank & Trust at the time of the conversion will automatically continue as a depositor after the conversion, and the deposit balance, interest rate and other terms of such deposit accounts will not change as a result of the conversion. Each such account will be insured by the Federal Deposit Insurance Corporation to the same extent as before the conversion. Depositors will continue to hold their existing certificates, passbooks and other evidences of their accounts.

Effect on Loans. No loan outstanding from ESSA Bank & Trust will be affected by the conversion, and the amount, interest rate, maturity and security for each loan will remain as it was contractually fixed prior to the conversion.

Effect on Voting Rights of Members. At present, all depositors and certain borrowers of ESSA Bank & Trust are members of, and have voting rights in, ESSA Bank & Trust as to all matters requiring membership action. Upon completion of the conversion, depositors and borrowers will cease to be members of ESSA Bank & Trust and will no longer have voting rights. Upon completion of the conversion, all voting rights in ESSA Bank & Trust will be vested in ESSA Bancorp, Inc. as the sole stockholder of ESSA Bank & Trust. The stockholders of ESSA Bancorp, Inc. will possess exclusive voting rights with respect to ESSA Bancorp, Inc. common stock.

Tax Effects. We will receive an opinion of counsel or tax advisor with regard to federal and state income tax consequences of the conversion to the effect that the conversion will not be taxable for federal or state income tax purposes to ESSA Bank & Trust, ESSA Bancorp, Inc., members of ESSA Bank & Trust, eligible account holders, supplemental eligible account holders, or ESSA Bank & Trust See Material Income Tax Consequences.

Effect on Liquidation Rights. Each depositor in ESSA Bank & Trust has both a deposit account in ESSA Bank & Trust and a pro rata ownership interest in the net worth of ESSA Bank & Trust based upon the deposit balance in his or her account. This ownership interest is tied to the depositor s account and has no tangible market value separate from the deposit account. This

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interest may only be realized in the event of a complete liquidation of ESSA Bank & Trust . Any depositor who opens a deposit account obtains a pro rata ownership interest in ESSA Bank & Trust without any additional payment beyond the amount of the deposit. A depositor who reduces or closes his or her account receives a portion or all, respectively, of the balance in the deposit account but nothing for his or her ownership interest in the net worth of ESSA Bank & Trust, which is lost to the extent that the balance in the account is reduced or closed.

Consequently, depositors in a stock subsidiary of a holding company normally have no way of realizing the value of their ownership interest, which has realizable value only in the unlikely event that ESSA Bank & Trust is completely liquidated. If this occurs, the depositors of record at that time, as owners, would share pro rata in any residual surplus and reserves of ESSA Bank & Trust after other claims, including claims of depositors to the amounts of their deposits, are paid.

In the unlikely event that ESSA Bank & Trust were to liquidate after the conversion, all claims of creditors, including those of depositors, also would be paid first, followed by distribution of the liquidation account to depositors as of ___________ and ____________________ who continue to maintain their deposit accounts as of the date of liquidation, with any assets remaining thereafter distributed to ESSA Bancorp, Inc. as the holder of ESSA Bank & Trust s capital stock. Pursuant to the rules and regulations of the Office of Thrift Supervision, a post-conversion merger, consolidation, sale of bulk assets or similar combination or transaction with another insured savings institution would not be considered a liquidation and, in such a transaction, the liquidation account would be assumed by the surviving institution. See Liquidation Rights.

Determination of Share Price and Number of Shares to be Issued

The plan of conversion and bank regulations require that the aggregate purchase price of the common stock sold in the offering be based on the appraised pro forma market value of the common stock, as determined by an independent valuation. ESSA Bank & Trust and ESSA Bancorp, Inc. have retained RP Financial, LC. to prepare an independent valuation appraisal. For its services in preparing the initial valuation, RP Financial will receive a fee of $90,000, and will be reimbursed for its expenses. RP Financial will receive an additional fee of $10,000 for each update to the valuation appraisal. ESSA Bank & Trust and ESSA Bancorp, Inc. have agreed to indemnify RP Financial and its employees and affiliates against specified losses, including any losses in connection with claims under the federal securities laws, arising out of its services as independent appraiser, except where such liability results from its negligence or bad faith.

The independent valuation appraisal considered the pro forma impact of the offering. Consistent with the Office of Thrift Supervision appraisal guidelines, the appraisal applied three primary methodologies: the pro forma price-to-book value approach applied to both reported book value and tangible book value; the pro forma price-to-earnings approach applied to reported and core earnings; and the pro forma price-to-assets approach. The market value ratios applied in the three methodologies were based upon the current market valuations of the peer group companies identified by RP Financial, subject to valuation adjustments applied by RP Financial to account for differences between ESSA Bancorp, Inc. and the peer group. RP

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Financial placed the greatest emphasis on the price-to-core earnings and price-to-book value approaches in estimating pro forma market value.

The independent valuation was prepared by RP Financial in reliance upon the information contained in this prospectus, including the consolidated financial statements of ESSA Bank & Trust. RP Financial also considered the following factors, among others:

- the present results and financial condition of ESSA Bank & Trust, and the projected results and financial condition of ESSA Bancorp, Inc., a Pennsylvania corporation;
- the economic and demographic conditions in ESSA Bank & Trust s existing market area;
- certain historical, financial and other information relating to ESSA Bank & Trust;
- a comparative evaluation of the operating and financial characteristics of ESSA Bank & Trust with those of other similarly situated publicly traded savings institutions located in the Commonwealth of Pennsylvania, and other states in the mid-Atlantic and midwest regions of the United States;
- the impact of the conversion and the offering on ESSA Bancorp, Inc. s stockholders equity and earnings potential;
- the proposed dividend policy of ESSA Bancorp, Inc.; and
- the trading market for securities of comparable institutions and general conditions in the market for such securities.

Included in RP Financial s independent valuation were certain assumptions as to the pro forma earnings of ESSA Bancorp, Inc. after the conversion that were utilized in determining the appraised value. These assumptions included estimated expenses, an assumed after-tax rate of return on the net offering proceeds and purchases in the open market of 4% of the common stock issued in the offering by the recognition and retention plan at the $10.00 purchase price. See Pro Forma Data for additional information concerning these assumptions. The use of different assumptions may yield different results.

The independent valuation states that as of November 24, 2006, the estimated pro forma market value of ESSA Bancorp, Inc. ranged from $100.0 million to $135.4 million, with a midpoint of $117.7 million. The Board of Directors of ESSA Bancorp, Inc. decided to offer the shares of common stock for a price of $10.00 per share primarily because it is the price most commonly used in mutual-to-stock conversions of financial institutions. The number of shares offered will be equal to the aggregate offering price of the shares divided by the price per share. Based on the valuation range and the $10.00 price per share, the minimum of the offering range will be 9,350,000 shares, the midpoint of the offering range will be 11,000,000 shares and the maximum of the offering range will be 12,650,000 shares, or 14,547,500 if the maximum amount is adjusted because of demand for shares or changes in market conditions.

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The following table presents a summary of selected pricing ratios for ESSA Bancorp, Inc. and our peer group companies identified by RP Financial. These ratios are based on earnings for the twelve months ended September 30, 2006 and book value as of September 30, 2006. Compared to the average pricing of the peer group, our pro forma pricing ratios at the maximum of the offering range indicated a premium of 22.5% on a price-to-earnings basis, a discount of 42.6% on a price-to-book value basis and a discount of 45.7% on a price-to-tangible book value basis. The pricing ratios result from our generally having higher levels of equity but lower earnings than the companies in the peer group on a pro forma basis. Our Board of Directors, in reviewing and approving the valuation, considered the range of price-to-core earnings multiples and the range of price-to-book value ratios and price-to-tangible book value ratios at the different amounts of shares to be sold in the offering. The appraisal did not consider one valuation approach to be more important than the other. Instead, the appraisal concluded that these ranges represented the appropriate balance of the two approaches to valuing ESSA Bancorp, Inc., and the number of shares to be sold, in comparison to the identified peer group institutions. Specifically, in approving the valuation, the board believed that ESSA Bancorp, Inc. would not be able to sell its shares at a price-to-book value that was in line with the peer group without unreasonably exceeding the peer group on a price-to-core earnings basis. The estimated appraised value and the resulting premium/discount took into consideration the potential financial impact of the conversion and offering.

	Pro forma price-to-earnings multiple	**Pro forma price-to-book value ratio**	**Pro forma price-to-tangible book value ratio**
ESSA Bancorp, Inc.			
Maximum	22.73x	81.04%	81.04%
Minimum	18.18	72.10	72.10
Valuation of peer group companies as of November 24, 2006			
Averages	18.55x	141.13%	149.25%
Medians	16.70	137.70	145.80

The Board of Directors of ESSA Bancorp, Inc. reviewed the independent valuation and, in particular, considered the following:

- ESSA Bank & Trust s financial condition and results of operations;
- comparison of financial performance ratios of ESSA Bank & Trust to those of other financial institutions of similar size; and
- market conditions generally and, in particular, for financial institutions.

All of these factors are set forth in the independent valuation. The Board of Directors also reviewed the methodology and the assumptions used by RP Financial, LC. in preparing the independent valuation and believes that such assumptions were reasonable. The offering range may be amended with the approval of the Office of Thrift Supervision, if required, as a result of subsequent developments in the financial condition of ESSA Bancorp, Inc. or ESSA Bank & Trust or market conditions generally.

The independent valuation is not intended, and must not be construed, as a recommendation of any kind as to the advisability of purchasing shares of our common

stock. RP Financial, LC. did not independently verify our consolidated financial statements and other information that we provided to them, nor did RP Financial, LC. independently value our assets or liabilities. The independent valuation considers ESSA Bank & Trust as a going concern and should not be considered as an indication of the liquidation value of ESSA Bank & Trust. Moreover, because the valuation is necessarily based upon estimates and projections of a number of matters, all of which may change from time to time, no assurance can be given that persons purchasing our common stock in the offering will thereafter be able to sell their shares at prices at or above the $10.00 offering price per share.

Following commencement of the subscription offering, the maximum of the valuation range may be increased by up to 15%, or up to $155.7 million, without resoliciting subscribers, which will result in a corresponding increase of up to 15% in the maximum of the offering range to up to 14,547,500 shares, in addition to the 1,018,325 shares to be issued to the ESSA Bank & Trust charitable foundation to reflect changes in the market and financial conditions or demand for the shares. We will not decrease the minimum of the valuation range and the minimum of the offering range without a resolicitation of subscribers. The subscription price of $10.00 per share will remain fixed. See Limitations on Common Stock Purchases as to the method of distribution and allocation of additional shares that may be issued in the event of an increase in the offering range to fill unfilled orders in the offering.

If the update to the independent valuation at the conclusion of the offering results in an increase in the maximum of the valuation range to more than $155.7 million and a corresponding increase in the offering range to more than 14,547,500 shares, or a decrease in the minimum of the valuation range to less than $100.0 million and a corresponding decrease in the offering range to fewer than 9,350,000 shares, then, with regulatory approval, we may terminate the offering and promptly return, with interest at ESSA Bank & Trust s passbook savings rate, all funds previously delivered to us to purchase shares of common stock and cancel deposit account withdrawal authorizations, and, after consulting with the Office of Thrift Supervision, we may terminate the plan of conversion. Alternatively, we may establish a new offering range and extend the offering period and commence a resolicitation of subscribers or take other actions as permitted by the Office of Thrift Supervision in order to complete the conversion and the offering. In the event that a resolicitation is commenced, we will notify subscribers of the extension of time and of the rights of subscribers to confirm, change or cancel their stock orders for a specified resolicitation period. If a subscriber does not respond, we will cancel the stock order and return funds, as described above. Any resolicitation following the conclusion of the subscription and community offerings would not exceed 45 days.

An increase in the number of shares to be issued in the offering would decrease both a subscriber s ownership interest and ESSA Bancorp, Inc. s pro forma earnings and stockholders equity on a per share basis while increasing pro forma earnings and stockholders equity on an aggregate basis. A decrease in the number of shares to be issued in the offering would increase both a subscriber s ownership interest and ESSA Bancorp, Inc. s pro forma earnings and stockholders equity on a per share basis, while decreasing pro forma earnings and stockholders equity on an aggregate basis. For a presentation of the effects of these changes, see Pro Forma Data.

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Copies of the independent valuation appraisal report of RP Financial, LC. and the detailed memorandum setting forth the method and assumptions used in the appraisal report are available for inspection at the main office of ESSA Bank & Trust and as specified under Where You Can Find Additional Information.

Subscription Offering and Subscription Rights

In accordance with the plan of conversion, rights to subscribe for shares of common stock in the subscription offering have been granted in the following descending order of priority. The filling of all subscriptions that we receive will depend on the availability of common stock after satisfaction of all subscriptions of all persons having prior rights in the subscription offering and to the maximum, minimum and overall purchase limitations set forth in the plan of conversion and as described below under Limitations on Common Stock Purchases.

Priority 1: Eligible Account Holders. Each ESSA Bank & Trust depositor with aggregate deposit account balances of $50.00 or more (a Qualifying Deposit) as of the close of business on April 30, 2005 (an Eligible Account Holder) will receive, without payment therefor, nontransferable subscription rights to purchase, subject to the overall purchase limitations, up to $350,000 or 35,000 shares of our common stock or, if greater, 15 times the number of subscription shares offered multiplied by a fraction of which the numerator is the aggregate Qualifying Deposit account balances of the Eligible Account Holder and the denominator is the aggregate Qualifying Deposit account balances of all Eligible Account Holders, subject to the overall purchase limitations. See Limitations on Common Stock Purchases. If there are not sufficient shares available to satisfy all subscriptions, shares will first be allocated so as to permit each Eligible Account Holder to purchase a number of shares sufficient to make his or her total allocation equal to the lesser of 100 shares or the number of shares for which he or she subscribed. Thereafter, unallocated shares will be allocated to each Eligible Account Holder whose subscription remains unfilled in the proportion that the amount of his or her Qualifying Deposit bears to the total amount of Qualifying Deposits of all subscribing Eligible Account Holders whose subscriptions remain unfilled. If an amount so allocated exceeds the amount subscribed for by any one or more Eligible Account Holders, the excess shall be reallocated among those Eligible Account Holders whose subscriptions are not fully satisfied until all available shares have been allocated.

To ensure proper allocation of shares of our common stock, each Eligible Account Holder must list on his or her stock order form all deposit accounts in which he or she has an ownership interest on April 30, 2005. In the event of oversubscription, failure to list an account could result in fewer shares being allocated than if all accounts had been disclosed. In the event of an oversubscription, the subscription rights of Eligible Account Holders who are also directors or executive officers of ESSA Bancorp, Inc. or their associates will be subordinated to the subscription rights of other Eligible Account Holders to the extent attributable to increased deposits in the twelve months preceding April 30, 2005.

Priority 2: Tax-Qualified Plans. Our tax-qualified employee benefit plans, including our employee stock ownership plan and 401(k) plan, will receive, without payment therefor, nontransferable subscription rights to purchase in the aggregate up to 10% of the shares of common stock sold in the offering.

Priority 3: Supplemental Eligible Account Holders. To the extent that there are sufficient shares of common stock remaining after satisfaction of subscriptions by Eligible Account Holders and our tax-qualified employee benefit plans, each ESSA Bank & Trust depositor with a Qualifying Deposit as of the close of business on ____________________ who is not an Eligible Account Holder (Supplemental Eligible Account Holder) will receive, without payment therefor, nontransferable subscription rights to purchase up to $350,000 or 35,000 shares of common stock or, if greater, 15 times the number of subscription shares offered multiplied by a fraction of which the numerator is the aggregate Qualifying Deposit account balances of the Supplemental Eligible Account Holder and the denominator is the aggregate Qualifying Deposit account balances of all Supplemental Eligible Account Holders, subject to the overall purchase limitations. See Limitations on Common Stock Purchases. If there are not sufficient shares available to satisfy all subscriptions, shares will be allocated so as to permit each Supplemental Eligible Account Holder to purchase a number of shares sufficient to make his or her total allocation equal to the lesser of 100 shares of common stock or the number of shares for which he or she subscribed. Thereafter, unallocated shares will be allocated to each Supplemental Eligible Account Holder whose subscription remains unfilled in the proportion that the amount of his or her Qualifying Deposit bears to the total amount of Qualifying Deposits of all Supplemental Eligible Account Holders whose subscriptions remain unfilled. If an amount so allocated exceeds the amount subscribed for by any one or more Supplemental Eligible Account Holders, the excess shall be reallocated among those Supplemental Eligible Account Holders whose subscriptions are not fully satisfied until all available shares have been allocated.

To ensure proper allocation of common stock, each Supplemental Eligible Account Holder must list on the stock order form all deposit accounts or loan accounts in which he or she has an ownership interest at ____________________. In the event of oversubscription, failure to list an account could result in fewer shares being allocated than if all accounts had been disclosed.

Priority 4: Other Members. To the extent that there are shares of common stock remaining after satisfaction of subscriptions by Eligible Account Holders, our tax-qualified employee benefit plans and Supplemental Eligible Account Holders, each depositor of ESSA Bank & Trust on the voting record date of ____________________ and each borrower as of ___________ who is not an Eligible Account Holder or Supplemental Eligible Account Holder (Other Members) will receive, without payment therefor, nontransferable subscription rights to purchase up to $350,000 or 35,000 shares of common stock, subject to the overall purchase limitations. See Limitations on Common Stock Purchases. If there are not sufficient shares available to satisfy all subscriptions, available shares will be allocated on a pro rata basis based on the size of the order of each Other Member whose order remains unfilled.

To ensure proper allocation of common stock, each Other Member must list on the stock order form all deposit accounts or loan accounts in which he or she has an ownership interest at ____________________. In the event of oversubscription, failure to list an account could result in fewer shares being allocated than if all accounts had been disclosed.

Expiration Date. The Subscription Offering will expire at 12:00 Noon, Eastern time, on ____________, unless extended by us for up to 45 days or such additional periods with the approval of the Office of Thrift Supervision, if necessary. Subscription rights will expire whether

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or not each eligible depositor or borrower can be located. We may decide to extend the expiration date of the subscription offering for any reason, whether or not subscriptions have been received for shares at the minimum, midpoint or maximum of the offering range. Subscription rights which have not been exercised prior to the expiration date will become void. We may extend the offering, without notice, until __________, 2007.

We will not execute orders until we have received orders to purchase at least the minimum number of shares of common stock. If we have not received orders to purchase at least 9,350,000 shares by ________, 2007, and the Office of Thrift Supervision has not consented to an extension, all funds delivered to us to purchase shares of common stock in the offering will be returned promptly to the subscribers with interest calculated at ESSA Bank & Trust s passbook savings rate and all deposit account withdrawal authorizations will be canceled. If an extension beyond the 45-day period following the expiration date is granted by the Office of Thrift Supervision, for any reason, we will notify all subscribers in the stock offering of the extension of time and of the rights of subscribers to confirm, change or cancel their stock order during a specified resolicitation period. Aggregate extensions may not go beyond _________, which is two years after the special meeting of voting members of ESSA Bank & Trust to vote on the plan of conversion.

Community Offering

To the extent that shares of common stock remain available for purchase after satisfaction of all subscriptions of the Eligible Account Holders, our tax-qualified employee benefit plans, Supplemental Eligible Account Holders and Other Members, we may offer shares pursuant to the plan of conversion to members of the general public in a community offering. Shares may be offered with a preference to natural persons residing in the Pennsylvania Counties of Monroe and Northampton.

Subscribers in the community offering may purchase up to 35,000 shares of common stock, subject to the overall purchase limitations. See Limitations on Common Stock Purchases. **The opportunity to purchase shares of common stock in the community offering category is subject to our right, in our sole discretion, to accept or reject any such orders in whole or in part either at the time of receipt of an order or as soon as practicable following the expiration date of the offering.**

If we do not have sufficient shares of common stock available to fill the orders of natural persons residing in the Pennsylvania Counties of Monroe and Northampton, we will allocate the available shares among those persons in a manner that permits each of them, to the extent possible, to purchase the lesser of 100 shares, or the number of shares subscribed for by such person. Thereafter, unallocated shares will be allocated among natural persons residing in the Pennsylvania Counties of Monroe and Northampton whose orders remain unsatisfied on an equal number of shares basis per order.

The term residing or resident as used in this prospectus means any person who occupies a dwelling within the Pennsylvania Counties of Monroe and Northampton, has a present intent to remain within this community for a period of time and manifests the genuineness of that intent by establishing an ongoing physical presence within the community,

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together with an indication that this presence within the community is something other than merely transitory in nature. We may utilize deposit or loan records or other evidence provided to us to decide whether a person is a resident. In all cases, however, the determination shall be in our sole discretion.

Expiration Date. The community offering may begin with, during or after the subscription offering, and is currently expected to terminate at the same time as the subscription offering, and must terminate no more than 45 days following the subscription offering.

Syndicated Community Offering

The plan of conversion provides that, if necessary, shares of common stock not purchased in the subscription offering and community offering may be offered for sale to the general public in a syndicated community offering to be managed by Ryan Beck & Co., Inc., acting as our agent. In such capacity, Ryan Beck & Co., Inc. may form a syndicate of other broker-dealers. Neither Ryan Beck & Co., Inc. nor any registered broker-dealer will have any obligation to take or purchase any shares of the common stock in the syndicated community offering; however, Ryan Beck & Co., Inc. has agreed to use its best efforts in the sale of shares in any syndicated community offering. The syndicated community offering would terminate no later than 45 days after the expiration of the subscription offering, unless extended by us, with approval of the Off