November 20, 2006

Dear Shareholders:

This letter will comment on our performance through the 2006 third quarter and discuss expected future opportunities and challenges for your Corporation. We have made a steady advance toward achieving our goals for growth and profit through the first nine months of 2006. Our expectations are high and challenging for the fourth quarter of 2006 and future periods. We are closing out 2006 with a slowing Michigan economy and a market bias for declining interest rates, both of which could lead to shrinking interest margins. This environment will result in a need for an even greater focus on quality loan growth, core deposit growth and expense management.

<u>Third Quarter 2006 in-Review</u>

The third quarter marked the following successes:

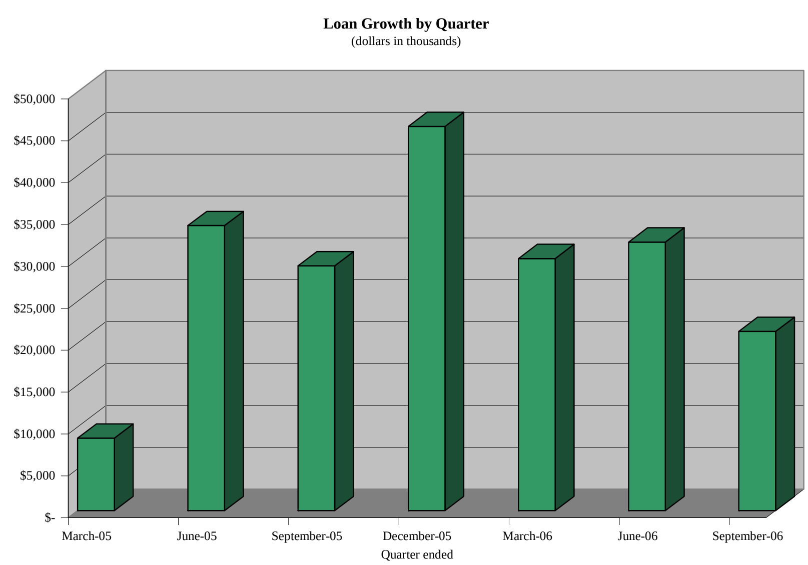
- Continued, yet slower loan growth with production of $21.4 million,
- Core deposit growth of $10 million in balances,
- On going Credit Quality:
  - Nonaccrual loans at .71% of total loans
  - Nonperforming assets at .58% of total assets.

In the third quarter our results included some unplanned items:

- Legal expenses related to lawsuit against former accountants; $160,000 for the quarter and $400,000 year to date,
- On the positive side the increased profitability of your Corporation allowed us to recognize a small portion, $500,000, of the deferred tax benefit related to the NOL carry-forward.

<u>Loan Production</u>

The third quarter provided continued, yet slower loan growth in all markets. We are beginning to experience the effects of a slowdown of the Michigan economy; however, our pipeline of $21.1 million of approved but unclosed loans ($15.0 million in Oakland County) at the end of the third quarter was encouraging and our expectations are that the fourth quarter will be a good one. The loan growth that we have achieved marks one of our successes for 2006. Production of $83.548 million in loans through September 30 is slightly behind our aggressive growth Plan for 2006 but is $11.651 million ahead of 2005 production for the same period. In the third quarter we continued our recent success in consumer loan growth throughout our northern branch network. So far in 2006, the Bank has grown consumer loan outstandings by $7.2 million, or 15.3%. Commercial loan growth is still the primary focus but we expect continued success in consumer loan growth due from increased mBank brand recognition in our banking markets coupled with the increased efforts and service of



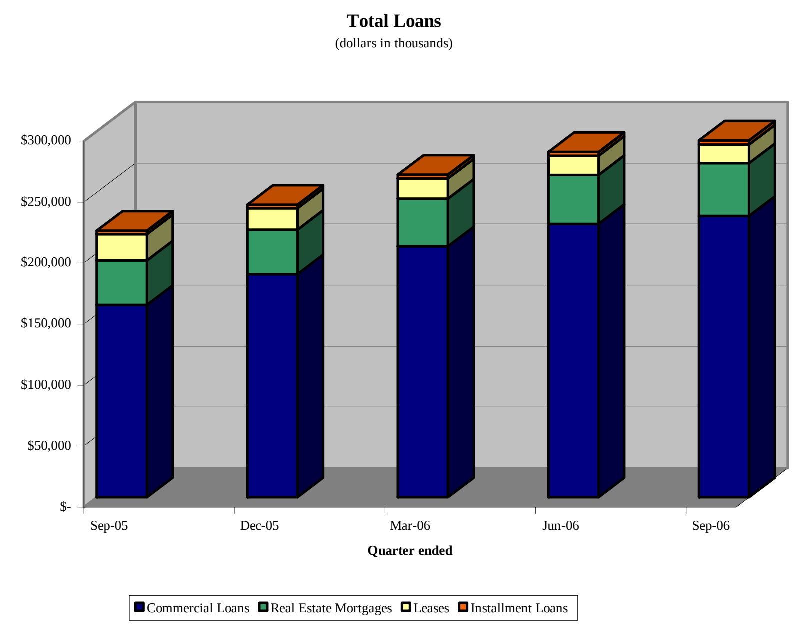
branch managers and support staff. The table and chart below illustrate the success we have experienced in generating loans for the seven quarters following recapitalization.

NEW LOAN PRODUCTION

(dollars in thousands)	2005 First Quarter	2005 Second Quarter	2005 Third Quarter	2005 YTD 09/30/05	2005 Fourth Quarter	**2005 Total**
REGION						
Upper Peninsula	$ 6,861	$ 9,099	$ 9,090	$ 25,050	$ 19,263	$ 44,313
Northern Lower Peninsula	686	12,449	9,698	22,833	13,786	36,619
Oakland County	1,100	12,480	10,434	24,014	12,813	36,827
TOTAL	$ 8,647	$ 34,028	$ 29,222	$ 71,897	$ 45,862	$ 117,759

	2006 First Quarter	2006 Second Quarter	2006 Third Quarter	2006 YTD 09/30/06
REGION				
Upper Peninsula	$ 7,592	$ 14,082	$ 10,356	$ 32,030
Northern Lower Peninsula	7,621	7,655	5,537	20,813
Oakland County	14,884	10,320	5,501	30,705
TOTAL	$ 30,097	$ 32,057	$ 21,394	$ 83,548

The chart below illustrates the portfolio mix of loans for each period end:



Credit Quality

We are pleased that the significant loan growth for 2005 and the first nine months of 2006 was accomplished without compromising credit quality. As of September 30, 2006, the Corporation's nonaccrual loans and total nonperforming assets remained at levels considered below peer. The reserve for loan losses was reduced by $600,000 in the first quarter in recognition of our excellent credit quality. The reserve at September 30, 2006 stood at $5.316 million 1.82% of loans outstanding.

Core Deposit Growth

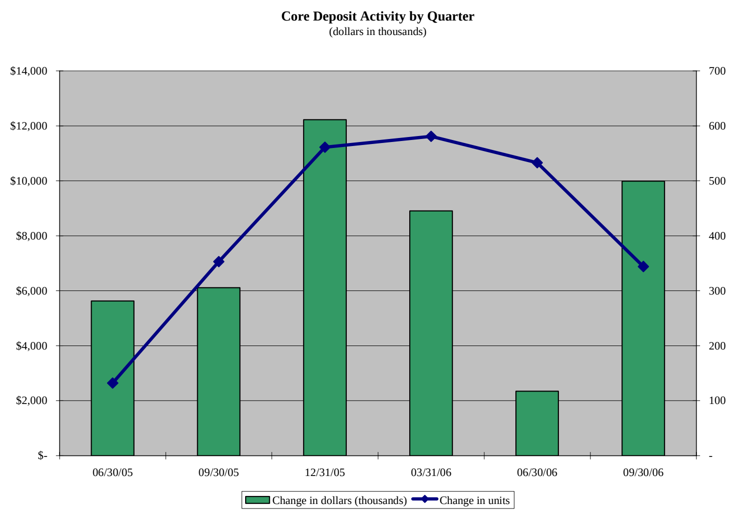
The growth of core deposits, which we define as demand deposits, interest bearing checking accounts, money market and savings accounts, and certificates of deposits that are generated by our branch system, continued during the third quarter of 2006. Growth of core deposits is a vital element of increased profitability and the notable increase in demand account balances in the third quarter provides an early indication of success in low cost deposit growth. We are pleased with the growth overall and continue to experience new account openings which we believe will lead to greater core balances in future periods.

The table and chart below show changes in dollars and number of accounts lost and added by quarter.

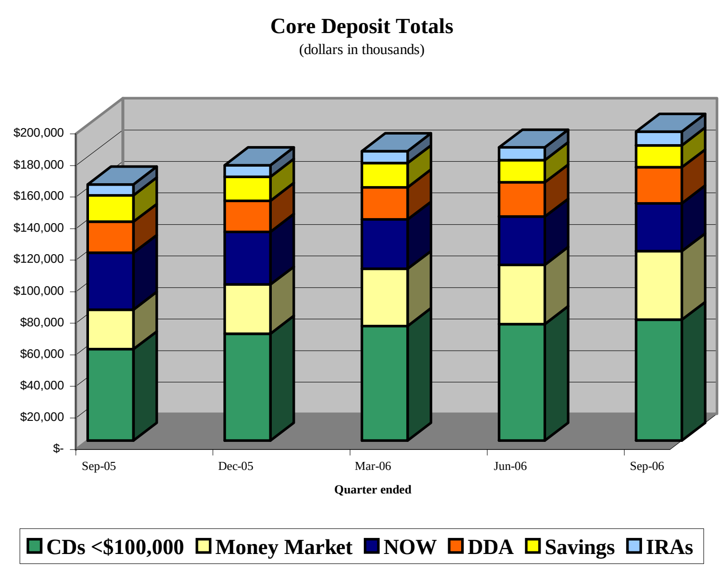
DEPOSIT ACCOUNT ACTIVITY

(dollars in thousands)	2005 First Quarter	2005 Second Quarter	2005 Third Quarter	2005 YTD 09/30/05	2005 Fourth Quarter
Core deposit balances	$ 150,567	$ 156,195	$ 162,303		$ 174,530
Deposit balance, change	$ (2,282)	$ 5,628	$ (33,472)	$ (30,126)	$ 12,227
Accounts opened	272	880	956	2,108	1,428
Accounts closed	461	748	603	1,812	867
Net change	(189)	132	353	296	561
Total accounts	15,837	15,922	18,415		18,415
Average balance, per account (in whole dollars)	$ 9,507	$ 9,810	$ 8,814		$ 9,477

	2006 First Quarter	2006 Second Quarter	2006 Third Quarter	2006 YTD 09/30/06
Core deposit balances	$ 183,438	$ 185,784	$ 195,775	
Deposit balance, change	$ 8,908	$ 2,346	$ 9,991	$ 21,245
Accounts opened	1,236	1,605	1,327	4,168
Accounts closed	655	1,052	983	2,690
Net change	581	553	344	1,478
Total accounts	19,063	19,616	19,960	
Average balance, per account (in whole dollars)	$ 9,622	$ 9,471	$ 9,808	



Growth in core deposits is important since this less expensive loan funding source will provide the benefits of higher levels of profitability. Core deposit growth is the primary reason for maintaining a branch banking system. We are pleased with our progress in growing core deposits but recognize that maintaining future growth at our recent pace will be challenging. The initial benefits of the "mBank' brand image and reintroduction into our historical branch markets provided core growth momentum late in 2005 and early in 2006. Our challenge for future core growth will be dependent upon competitive products and pricing promoted by an active sales culture and supported by service.



Noninterest Income

Noninterest income amounted to $251,000 during the second quarter, well below our planned level of $356,000. The 2006 Plan included aggressive noninterest income contribution from secondary mortgage market activity. We fell significantly short of our Plan goals due primarily to the downturn in Michigan's economy, primarily Southeast Michigan, where we had high expectations for mortgage originations.

Generating significant increases in noninterest income for future periods will be difficult since we have a limited platform for growth. Our expectations for future period increases are modest and include increased fee income from our newly introduced overdraft protection program. We are also in the process of reviewing other financial services that we intend to introduce in the near future which will contribute to noninterest income.

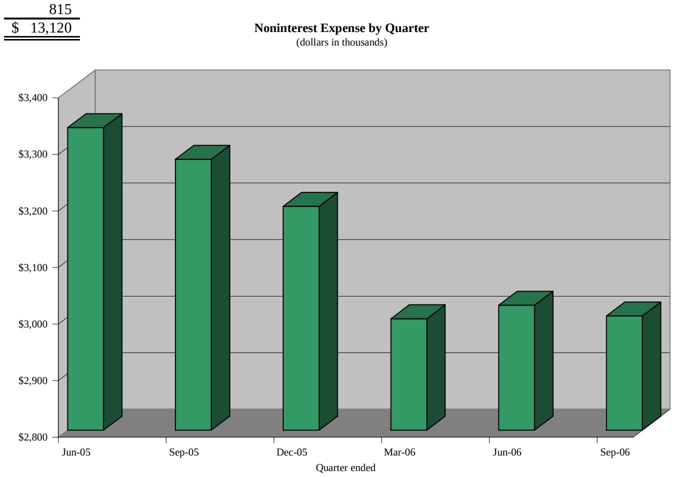
Noninterest Expense

In the third quarter of 2006 noninterest expense was modestly lower than second quarter expenses. We continued to incur higher than normal legal fees due to the ongoing costs of our legal action against the former accountants of the Corporation. Controlling noninterest expense is a distinct challenge when our primary Corporate objective for increased profitability hinges on growth. We accept this challenge yet recognize that certain operational costs will increase in future periods; however, we have in fact continued our plan for reduction of noninterest expense in most other categories as illustrated in the table below.

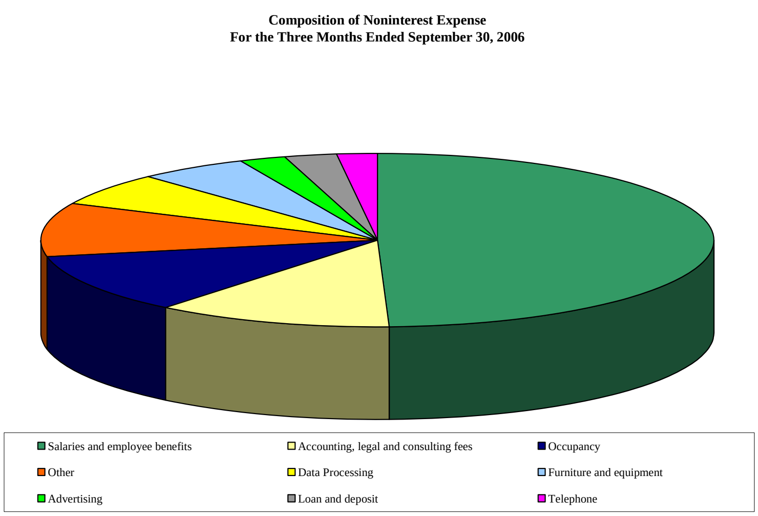
NONINTEREST EXPENSE

(dollars in thousands)	2005					
	First Quarter	Second Quarter	Third Quarter	YTD 09/30/05	Fourth Quarter	**2005 Total**
Salaries and employee benefits	$ 1,504	$ 1,606	$ 1,555	$ 4,665	$ 1,425	$ 6,090
Occupancy	226	247	275	748	305	1,053
Furniture and equipment	159	138	133	430	130	560
Data processing	246	246	234	726	994	1,720
Accounting, legal and consulting fees	318	228	204	750	136	886
Loan and deposit	293	250	153	696	156	852
Telephone	60	77	66	203	68	271
Advertising	139	243	314	696	118	814
Other	4,685	300	345	5,330	679	6,009
Total noninterest expense	7,630	3,335	3,279	14,244	4,011	18,255
Less:						
Penalty - prepayment of FHLB borrowings	4,320	-	-	4,320	-	4,320
Data processing conversion costs	-	-	-	-	815	815
Noninterest expense, as adjusted	$ 3,310	$ 3,335	$ 3,279	$ 9,924	$ 3,196	$ 13,120

	2006			
	First Quarter	Second Quarter	Third Quarter	YTD 09/30/06
Salaries and employee benefits	$ 1,594	$ 1,496	$ 1,487	$ 4,577
Occupancy	317	293	333	943
Furniture and equipment	156	155	158	469
Data processing	154	182	176	512
Accounting, legal and consulting fees	200	414	341	955
Loan and deposit	129	98	79	306
Telephone	49	51	56	156
Advertising	70	107	70	247
Other	328	225	302	855
Total noninterest expense	$ 2,997	$ 3,021	$ 3,002	$ 9,020



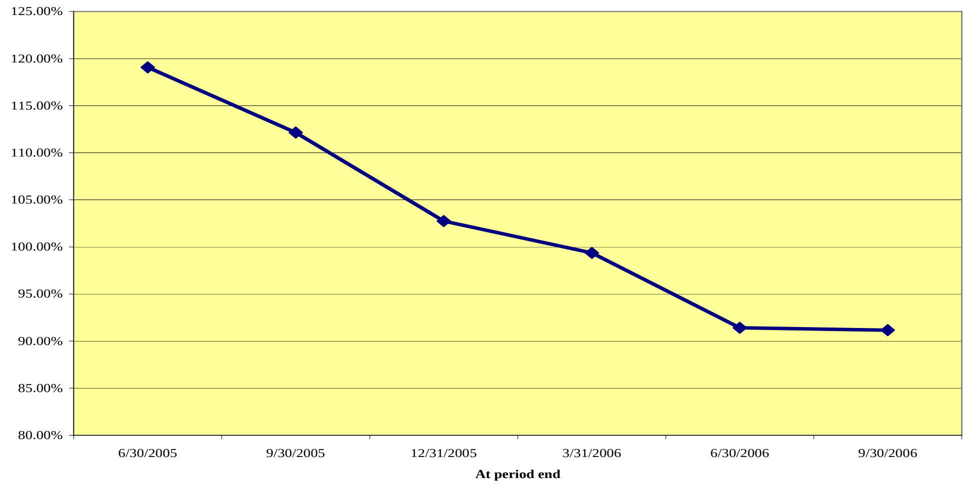
The table above illustrates the progress we have made in controlling noninterest expense. Excluding the one-time extraordinary costs referred to above, noninterest expenses have declined in each successive quarter. We have reduced total noninterest expense more than 10% in the last year. The increases for 2006 include the one time costs associated with the legal action against our former accountants which totaled $400,000 through the end of the third quarter. We expect additional costs in this matter of $250,000 which will bring the case to resolution and/or trial. The increase in occupancy costs over the last few quarters is due to the opening of the full service branch location in Birmingham in January and the relocation of our Gaylord branch office in June of this year. We do not expect any other significant changes to occupancy expense in



future periods and are exploring opportunities for rental of excess office space at our branch locations.

The chart below illustrates the impact of controlling expenses and expanding our net interest margin has on our efficiency ratio.

EFFICIENCY RATIO*



COMPONENTS OF THE EFFICIENCY RATIO*

	Quarter ended,					
(dollars in thousands)	06/30/05	09/30/05	12/31/05	03/31/06	06/30/06	09/30/06
Net interest income (FTE basis)	$ 2,528	$ 2,643	$ 2,822	$ 2,800	$ 3,055	$ 3,052
Noninterest income, excluding securities gain/loss	272	254	303	216	250	241
Total operating income (FTE basis)	2,800	2,897	3,125	3,016	3,305	3,293
Noninterest expense	$ 3,335	$ 3,279	$ 3,246	$ 2,997	$ 3,021	$ 3,002
Efficiency ratio	**119.10** %	**113.19** %	**103.85** %	**99.37** %	**91.41** %	**91.16** %

The efficiency ratio calculation excludes the FHLB prepayment penalty and the data processing conversion costs.

Capital

As of September 30, 2006, your Corporation was well capitalized. The strong growth of the Corporation has presented us with challenges to maintain the regulatory capital ratios of the bank. In the second quarter the Corporation established a $6 million line of credit at a correspondent bank to provide the necessary funding for additional capital infusions into the Bank. As of September 30, we have drawn $1.950 million for capital infusion to the bank. High growth requires capital and the Corporation will be exploring different short-term and long-term capital solutions to sustain our growth and profitability objectives.

Looking Forward

We are looking forward to a strong closing quarter in 2006. In the fourth quarter we will be finalizing our 2007 goals and objectives. We will develop this 2007 Plan conscious of our responsibility to you, our shareholders, to increase franchise value by expanding our customer base, growing loans, and controlling costs, all leading to increased profitability.

Sincerely,

Paul D. Tobias
Chairman and CEO

Mackinac Financial Corporation Selected Financial Highlights

(Dollars in thousands, except per share data) *	For The Period Ended		
	September 30, 2006	December 31, 2005	September 30, 2005
	(Unaudited)		(Unaudited)
Selected Financial Condition Data (*at end of period*):			
Total assets	$ 363,191	$ 298,722	$ 280,590
Total loans	292,614	239,771	218,462
Total deposits	293,494	232,632	213,268
Borrowings and subordinated debentures	38,307	36,417	36,417
Total shareholders' equity	28,226	26,588	27,900
Selected Statements of Income Data *nine months and year ended):*			
Net interest income	$ 8,566	$ 9,780	$ 7,100
Income (loss) before taxes	853	(7,364)	(6,336)
Net income (loss)	1,378	(7,364)	(6,336)
Income (loss) per common share - Basic	.40	(2.15)	(1.85)
Income (loss) per common share - Diluted	.40	(2.15)	(1.85)
Three Months Ended			
Net interest income	$ 2,952	$ 2,680	$ 2,507
Income (loss) before taxes	190	(1,028)	(518)
Net income (loss)	690	(1,028)	(518)
Income (loss) per common share - Basic	.20	(.30)	(.15)
Income (loss) per common share - Diluted	.20	(.30)	(.15)
Selected Financial Ratios and Other Data *(nine months and year ended*):			
Performance Ratios:			
Net interest margin	3.53 %	3.64 %	3.79 %
Efficiency ratio	93.12	160.43	112.11
Return on average assets	.54	(2.58)	(2.97)
Return on average equity	6.71	(25.63)	(28.99)
Average total assets	$ 341,646	$ 285,896	$ 284,978
Average total shareholders' equity	$ 27,440	$ 28,732	$ 29,218
Average loans to average deposits ratio	98.86 %	98.17 %	99.33 %
Common Share Data (at end of period):			
Market price per common share	$ 10.56	$ 9.10	$ 10.99
Book value per common share	$ 8.23	$ 7.76	$ 8.14
Common shares outstanding	3,428,695	3,428,695	3,428,695
Other Data (at end of period):			
Allowance for loan losses	$ 5,316	$ 6,108	$ 6,589
Non-performing assets	$ 2,091	$ 1,059	$ 3,905
Allowance for loan losses to total loans	1.82 %	2.55 %	3.02 %
Non-performing assets to total assets	.58 %	.35 %	1.39 %
Number of:			
Employees (FTE basis)	96	102	98
Branch locations	13	12	12

QUARTERLY FINANCIAL SUMMARY

*(Dollars in thousands, except per share data)

Quarter Ended	Average Assets	Average Loans	Average Deposits	Average Shareholders' Equity	Return on Average Assets	Return on Average Equity	Net Interest Margin	Efficiency Ratio	Net Income Per Share	Book Value Per Share
September 30, 2006	**$ 362,632**	**$ 289,210**	**$ 296,608**	**$ 28,041**	**.75 %**	**9.76 %**	**3.36 %**	**91.17 %**	**$ .20**	**$ 8.23**
June 30, 2006	342,820	273,686	274,591	27,213	.22	2.82	3.62	91.41	.05	7.93
March 31, 2006	319,007	250,735	254,720	27,055	.63	7.47	3.62	99.37	.15	7.93
December 31, 2005	288,619	224,386	219,967	27,288	(1.41)	(14.95)	3.96	128.37	(.30)	7.76
September 30, 2005	280,506	209,785	211,197	28,112	(.73)	(7.39)	3.79	112.11	(.15)	8.14
June 30, 2005	277,754	197,545	206,875	28,879	(.83)	(8.01)	3.67	119.07	(.17)	8.32
March 31, 2005	296,856	199,703	209,035	30,692	(7.16)	(69.25)	3.21	300.96	(1.53)	8.42
December 31, 2004	327,543	218,962	211,685	8,455	2.95	114.17	2.48	71.83	8.25	10.13
September 30, 2004	346,078	226,951	236,418	6,096	(.87)	(49.53)	2.25	120.66	(2.17)	18.44

* Historical per share data has been adjusted for the 20:1 reverse stock split distributed in December 2004.