



To our Shareholders:

Growth at Highlands State Bank has continued to be strong for the first quarter of 2008. This past year, total assets increased by 57% to \$51.3 million as of March 31, 2008, compared to \$32.6 million in total assets on March 31, 2007. Total assets also increased by 20% compared to \$42.9 million in total assets on December 31, 2007.

Net loans outstanding as of March 31, 2008 were \$37.2 million, showing an increase of 195% when compared to \$12.6 million on that date in 2007. Net loans outstanding increased 20% over the balance of \$31 million on December 31, 2007. Comparative balance sheets are shown on the back of this letter.

The current year brings a number of challenges with it. Although the banking environment is currently in a state of flux, we are encouraged with the results we are seeing from our mortgage department. We have been able to generate a good volume of residential mortgage business while maintaining high credit quality standards. However, the atmosphere for developing new business is still quite difficult.

Highlands has engaged an additional lender to continue building our loan portfolio and has dedicated a full-time person to develop new business in our market area. We also continue to seek additional sources of deposits. While the Federal Reserve has lowered their rates, the cost of deposit generation has not adjusted accordingly. We offer very competitive rates on our deposit accounts and ask that you consider Highlands State Bank for some of your banking needs.

Our earnings trend is very positive and while Highlands is still not profitable, I am confident that we will be showing profits by the fourth quarter of this year. I would welcome the opportunity to talk with you about any questions or comments you may have regarding your investment in Highlands State Bank.

Sincerely,

George E. Irwin,
President & CEO

HIGHLANDS STATE BANK BALANCE SHEET

(in dollars)

	March 31 2008 (unaudited)	December 31 2007 (audited)	March 31 2007 (unaudited)
ASSETS			
Cash and due from banks	\$1,079,937	\$1,161,515	\$514,858
Interest bearing deposits in other banks	198,000	-	298,000
Time deposits in other banks	1,488,000	2,481,000	4,164,000
Securities available for sale	10,478,548	7,364,599	9,420,317
Restricted investment in bank stock	113,100	50,000	50,000
Federal funds sold	-	-	4,822,000
Loans	\$37,533,238	\$31,327,016	\$12,759,650
less: Allowance for loan loss	(377,870)	(304,144)	(127,830)
Net loans	\$37,155,368	\$31,022,872	\$12,631,820
Bank premises and equipment, net	448,604	468,443	503,688
Other assets	333,950	329,195	218,970
Total Assets	\$51,295,507	\$42,877,624	\$32,623,653
LIABILITIES AND STOCKHOLDERS' EQUITY			
LIABILITIES			
Deposits:			
Non-interest bearing	\$7,724,911	\$6,693,759	\$7,711,934
Interest-bearing	29,561,924	26,518,735	16,563,531
Total Deposits	\$37,286,835	\$33,212,494	\$24,275,465
Borrowings	5,248,000	759,000	-
Other liabilities	181,110	204,554	102,385
Total Liabilities	\$42,715,945	\$34,176,048	\$24,377,850
STOCKHOLDERS EQUITY			
Common stock, \$5 par value; authorized 5,000,000 shares; issued and outstanding 1,095,159 shares 3/31/2008 and 12/31/2007; 3/31/2007 1,000,000 shares	\$5,475,795	\$5,475,795	\$5,000,000
Surplus	5,740,982	5,730,086	5,178,844
Accumulated deficit	(2,783,722)	(2,566,089)	(1,935,429)
Accumulated other comprehensive loss	146,507	61,784	2,388
Total Stockholders' Equity	\$8,579,562	\$8,701,576	\$8,245,803
Total Liabilities and Stockholders' Equity	\$51,295,507	\$42,877,624	\$32,623,653