



Highlands State Bank

To our shareholders:

Growth continues to be strong at Highlands State Bank. As of June 30, 2007, total assets were \$35.3 million, an increase of \$2.7 million compared to March 31, 2007 total assets of \$32.6 million. This is an increase of \$10.1 million compared to June 30, 2006 assets of \$25.2 million. Net Loans outstanding as of June 30, 2007 were \$20.8 million reflecting a substantial increase of 65% over the \$12.6 million outstanding at the end of the first quarter of 2007. Deposits have grown to \$27.2 million as of the most recent quarter-end compared to \$22.6 million at year-end 2006 and \$16.2 million at the end of June the previous year. For your convenience, we have printed comparative balance sheet information on the back of this letter.

Highlands State Bank continues to offer some the most competitive rates available on checking accounts and money market accounts. In our last letter we wrote about the PIMMA (Prime Interest Money Market Account). This is a money market account that pays an interest rate equal to 60% of the Prime Rate, currently 5.07% APY, and requires a minimum balance of \$50,000. The bank has also introduced a regular money market account that pays a rate equal to 50% of the Prime Rate, currently 4.21% APY, and a minimum balance requirement of \$1,000. We now pay 3.78% APY on personal checking accounts. The rate on this account is indexed at 45% of the Prime Rate. The annual percentage yields will increase or decrease if the prime rate is raised or lowered.

In the middle of July we sent a letter advising you that the warrants you hold will be expiring on October 11, 2007. The letter also advised of the action taken by your board of directors regarding those warrants. A separate flier is included with this letter explaining more about the options available to you regarding the exercise of the warrants.

Your investment in Highlands State Bank is very much appreciated and we take our responsibility to you very seriously. Thank you for supporting our growth and sharing in our continued success.

Sincerely,



George E. Irwin
President & CEO

HIGHLANDS STATE BANK BALANCE SHEET

(in dollars)

	June 30 2007 (unaudited)	December 31 2006 (audited)	June 30 2006 (unaudited)
ASSETS			
Cash and due from banks	\$667,273	\$568,607	\$552,688
Interest bearing deposits in other banks	0	199,000	398,000
Time deposits in other banks	3,965,000	2,676,000	1,881,000
Securities available for sale	8,917,471	9,324,030	4,831,663
Federal funds sold	103,000	9,944,000	13,833,000
Loans	\$20,979,292	\$7,847,281	\$3,074,542
less: Allowance for loan loss	(205,400)	(78,513)	(38,358)
Net loans	\$20,773,892	\$7,768,768	\$3,036,184
Bank premises and equipment, net	498,681	466,721	477,128
Other assets	341,998	228,700	181,060
Total Assets	\$35,267,315	\$31,175,826	\$25,190,723
LIABILITIES AND STOCKHOLDERS' EQUITY			
LIABILITIES			
Deposits:			
Non-interest bearing	\$5,928,401	\$7,217,122	\$6,423,715
Interest-bearing	21,279,727	15,335,554	9,782,575
Total Deposits	\$27,208,128	\$22,552,676	\$16,206,290
Other Liabilities	158,477	129,844	93,227
Total Liabilities	\$27,366,605	\$22,682,520	\$16,299,517
STOCKHOLDERS EQUITY			
Common stock, \$5 par value authorized 5,000,000 shares; issued and outstanding 1,000,625 shares as of June 30, 2007; issued and outstanding 1,000,000 shares as of December 31 & June 30, 2006	\$5,003,125	\$5,000,000	\$5,000,000
Surplus	5,207,118	5,153,695	5,003,347
Accumulated deficit	(2,213,901)	(1,660,939)	(1,079,634)
Accumulated other comprehensive loss	(95,632)	550	(32,507)
Total Stockholders' Equity	\$7,900,710	\$8,493,306	\$8,891,206
Total Liabilities and Stockholders' Equity	\$35,267,315	\$31,175,826	\$25,190,723