

SECOND QUARTER 2008

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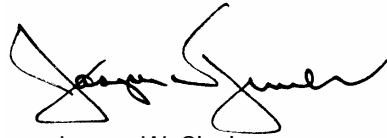
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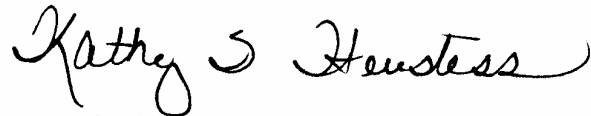
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Jasper W. Shuler
Chief Executive Officer



Kathy S. Heustess
Chief Operating and Financial Officer



James M. Ward
Chairman of the Board

August 4, 2008

Management's Discussion and Analysis of Financial Condition and Results of Operations

(dollars in thousands)

The following commentary reviews the financial condition and results of operations of **ArborOne, ACA**, (Association) for the period ended June 30, 2008. These comments should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements and the 2007 Annual Report of the Association. The accompanying consolidated financial statements were prepared under the oversight of the Audit Committee of the Board of Directors.

LOAN PORTFOLIO

The Association provides funds to farmers, rural homeowners and farm-related businesses for financing of short and intermediate-term loans and long-term real estate mortgage loans. The Association's loan portfolio is diversified over a range of agricultural commodities in our region, including tobacco, poultry, swine and forestry. Farm size varies and many of the borrowers in the region have diversified farming operations. These factors, along with the numerous opportunities for non-farm income in the area, somewhat impact the level of dependency on a given commodity. Approximately twenty-eight percent of the portfolio has significant outside income to diversify dependence on agriculture, consisting of lifestyle loans and loans to less than full-time farmers with retirement income, salaried income and non-agricultural business income. Further, approximately fourteen percent of the assets carry federal guarantees as a risk management tool.

The gross loan volume of the Association as of June 30, 2008, was \$316,733, a decrease of \$28,653 as compared to \$345,386 at December 31, 2007. Net loans outstanding at June 30, 2008, were \$316,049 as compared to \$345,333 at December 31, 2007. During the six months ended June 30, 2008, the Association's sold participations to **AgFirst Farm Credit Bank** (the Bank) increased by \$44,249. As of June 30, 2008, the Association had \$100,500 of such participations outstanding. The Association has investment securities that are classified as available for sale in the amount of \$31,505 at June 30, 2008 compared to \$32,500 at December 31, 2007. The Association entered into commitments to acquire Successor-in-Interest Contracts (SIIC), beginning in the fourth quarter of 2005. As of June 30, 2008, the Association had \$107,298 in other investments for SIIC, compared to \$121,693 at December 31, 2007. Net loans and investments accounted for 94.31 percent of total assets at June 30, 2008, as compared to 94.59 percent of total assets at December 31, 2007.

Net loans and investments decreased by \$44,676 during the reporting period. The decrease in loan volume is primarily due to an increase in participations sold to the Bank. Investment securities available for sale decreased by \$995 due to normal payments and a decrease in fair value. The other investments

for SIIC decreased by \$14,395, which was due to the annual payments on the contracts. The Association continues to review and engage in investment and participation opportunities, while serving customers within the territory.

There is an inherent risk in the extension of any type of credit. However, portfolio credit quality continues to be maintained at an acceptable level, and credit administration remains satisfactory. Nonaccrual loans increased from \$2,673 at December 31, 2007, to \$5,093 at June 30, 2008. This was due to one large participation loan that was moved to non-accrual during the second quarter of 2008.

Association management maintains an allowance for loan losses in an amount considered sufficient to absorb possible losses in the loan portfolio based on historical losses, current conditions, and expected future conditions. The allowance for loan losses at June 30, 2008, was \$684, compared to \$53 at December 31, 2007. This increase was due to the Association recording a specific reserve of \$636 on the participation loan that was moved to non-accrual this quarter. The increase is considered by management to be adequate to cover possible losses. There were recoveries of \$4 and charge-offs of \$21 for the three months ended June 30, 2008.

RESULTS OF OPERATIONS

For the three months ended June 30, 2008

Net income for the three months ended June 30, 2008, totaled \$959, as compared to \$2,696 for the same period in 2007. Net interest income decreased \$673, for the three months ended June 30, 2008, as compared to the same period in 2007 due to decreased loan volume coupled with lower interest rates. This decrease is a result of interest income on loan volume and other investments (SIIC) decreasing by \$2,242, while the interest income on investment securities increased by \$220. Interest expense also decreased by \$1,349.

At June 30, 2008, interest income on accruing loans decreased by \$2,088 compared to \$6,817 at June 30, 2007. Nonaccrual income was \$38 for the three months ended June 30, 2008, as compared to \$85 for the same period in 2007. Interest income on investment securities was \$246 compared to \$26 for the same period in 2007. Interest income on other investments (SIIC) was \$1,473 for the three months ended June 30, 2008, and \$1,627 for the same period in 2007. Interest expense decreased \$1,349 for the three months ended June 30, 2008, as compared to the comparable period of 2007. This was a result of decreased loan volume and lower interest rates which were partially offset by the increase of investment securities volume. The Association recorded a provision for loan loss of \$636 as a result of setting up a specific reserve for the participation loan moved to nonaccrual.

Noninterest income for the three months ended June 30, 2008, totaled \$2,081, as compared to \$1,926 for the same period of 2007, an increase of \$155. The increase is primarily the result of increased patronage income for loans sold to the Bank. Noninterest expense for the three months ended June 30, 2008, increased \$376 compared to the same period of 2007. Increases in salaries and employee benefits, occupancy and equipment, and other operating expenses were the primary drivers of the increase. The Association recorded a provision for income taxes of \$9 for the three months ended June 30, 2008, as compared to \$2 for the three months ended June 30, 2007.

For the six months ended June 30, 2008

Net income for the six months ended June 30, 2008, totaled \$3,026, as compared to \$4,747 for the same period in 2007. For the six months ended June 30, 2008, net interest income decreased by \$704 or 16.26 percent compared to June 30, 2007. Interest income on loans and other investments (SIIC) decreased by \$2,599 which was partially offset by an increase of \$546 in investment securities. Interest expense decreased by \$1,349 compared to the same period of 2007. This change in net interest income is the result of both decreased loan volume and lower interest rates.

Nonaccrual income was \$65 for the six months ended June 30, 2008, as compared to \$90 for the same period in 2007. The Association recorded a provision for loan loss of \$636 for the six months ended June 30, 2008, but recorded a reversal of provision for loan loss of \$200 for the same period in 2007.

Noninterest income for the six months ended June 30, 2008, totaled \$4,090, as compared to \$3,564 for the same period of 2007, an increase of \$526. The increase is primarily the result of increases in patronage income by \$924. The increase was primarily offset by a decrease in financially related services income of \$46 and loan fees by \$21. Noninterest expense for the six months ended June 30, 2008, increased \$690 compared to the same period of 2007. This increase is attributable to a rise in salaries and employee benefits of \$197, occupancy and equipment expenses of \$255, and other operating expenses of \$269. The Association recorded a provision for income taxes of \$19 for the six months ended June 30, 2008, a decrease of \$17 as compared to the same period in 2007.

FUNDING SOURCES

The principal source of funds for the Association is the borrowing relationship established with the Bank through a General Financing Agreement. The General Financing Agreement utilizes the Association's credit and fiscal performance as criteria for establishing a line of credit on which the Association may draw funds. The funds are advanced by the Bank to the Association in the form of notes payable. The notes payable are segmented into variable rate and fixed rate sections. The variable rate note is utilized by the Association to fund variable rate loan advances and operating funds requirements. The fixed rate note is used specifically to fund fixed rate loan advances made by the Association. The total notes payable to the Bank at June 30, 2008, was \$426,504 as compared to \$466,846 at December 31, 2007. The decrease during the period is primarily attributable to decreased loan volume and lower interest rates.

CAPITAL RESOURCES

Total members' equity at June 30, 2008, increased to \$50,687 from the December 31, 2007, total of \$48,414. The increase is primarily attributable to the increase in retained earnings in excess of the reduction of protected stock and revolved equities.

Total capital stock and participation certificates were \$1,576 on June 30, 2008, compared to \$1,608 on December 31, 2007. This decrease is attributed to the retirement of protected stock and participation certificates on loans liquidated in the normal course of business and the annual retirement of B stock.

The Association reports other comprehensive income (loss) (OCI) in its Consolidated Statements of Changes in Members' Equity. The Association recognized OCI of \$(382) as of June 30, 2008, as compared to \$(45) in 2007 for FAS 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans." The Association also recognized OCI of \$(692) as of June 30, 2008, as compared to \$(44) in 2007 for unrealized gains (losses) on investments available for sale.

Farm Credit Administration (FCA) regulations require all Farm Credit institutions to maintain minimum permanent capital, total surplus and core surplus ratios. These ratios are calculated by dividing the Association's permanent capital, total surplus and core surplus as defined in FCA regulations, by a risk-adjusted asset base. As of June 30, 2008, the Association's total surplus ratio and core surplus ratio were 11.78 percent and 8.73 percent, respectively, and the permanent capital ratio was 12.23 percent. All three ratios were well above the minimum regulatory ratios of 7.00 percent for permanent capital and total surplus ratios and 3.50 percent for the core surplus ratio.

ACCOUNTING FOR DEFINED BENEFIT PENSION AND OTHER POSTRETIREMENT PLANS

On September 29, 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans". Please refer to Note 3, "Employee Benefit Plans", in the Notes to the Financial Statements, and the 2007 Annual Report of ArborOne, ACA for recently issued accounting pronouncements.

NOTE: Shareholder investment in the Association could be affected by the financial condition and results of operations of AgFirst Farm Credit Bank. Copies of AgFirst's Annual and Quarterly reports are available upon request free of charge by calling 1-800-845-1745, ext. 378, or writing Stephen Gilbert, AgFirst Farm Credit Bank, P.O. Box 1499, Columbia, SC 29202. Information concerning AgFirst Farm Credit Bank can also be obtained at their website, www.agfirst.com. Copies of the Association's Annual and Quarterly reports are also available upon request free of charge by calling 1-800-741-7332, writing Joan Boice, Corporate Secretary, ArborOne, ACA, P.O. Box 3699, Florence, SC 29502, or accessing the website, www.arborone.com. The Association prepares a quarterly report within 40 days after the end of each fiscal quarter, except that no report need be prepared for the fiscal quarter that coincides with the end of the fiscal year of the institution.

ArborOne, ACA

Notes to the Consolidated Financial Statements

(dollars in thousands, except as noted)
(unaudited)

NOTE 1 – ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements include the accounts of ArborOne, ACA (the Association). A description of the organization and operations of the Association, the significant accounting policies followed, and the financial condition and results of operations as of and for the year ended December 31, 2007, are contained in the 2007 Annual Report to Shareholders. These unaudited second quarter 2008 consolidated financial statements should be read in conjunction with the 2007 Annual Report to Shareholders.

The accompanying consolidated financial statements contain all adjustments necessary for a fair presentation of the interim financial condition and results of operations and conform with generally accepted accounting principles (GAAP) and prevailing practices within the banking industry. The results for the six months ended June 30, 2008, are not necessarily indicative of the results to be expected for the year ending December 31, 2008.

Certain amounts in the prior period's consolidated financial statements may have been reclassified to conform to the current period's consolidated financial statement presentation. Such reclassifications had no effect on the prior period net income or total capital as previously reported.

The Association maintains an allowance for loan losses in accordance with GAAP. The loan portfolio is reviewed quarterly to determine the adequacy of the allowance for losses. As of June 30, 2008, the allowance for losses is adequate in management's opinion to provide for possible losses on existing loans.

In December 2007, the Financial Accounting Standards Board issued Statements of Financial Accounting Standards No. 141R, "Business Combinations" (SFAS 141R). SFAS 141R requires business combinations to be accounted for under the acquisition method of accounting (previously called the purchase method). The acquisition method requires (a) identifying the acquirer, (b) determining the acquisition date, (c) recognizing and measuring the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree, at their acquisition date fair values, and (d) recognizing and measuring goodwill or a gain from a bargain purchase. SFAS 141R should be applied prospectively to business combinations for which the

acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. Early application is prohibited. The Association is still evaluating the provisions of SFAS 141R, but believes that its adoption will significantly impact its accounting for combinations/acquisitions that may occur in 2009 and beyond.

NOTE 2 – ALLOWANCE FOR LOAN LOSSES

An analysis of the allowance for loan losses follows:

| | For the six months ended June 30, | |
|---|-----------------------------------|--------------|
| | 2008 | 2007 |
| Balance at beginning of period | \$ 53 | \$ 243 |
| Provision for (reversal of) loan losses | 636 | (200) |
| Loans (charged off), net of recoveries | (5) | 11 |
| Balance at end of period | <u>\$ 684</u> | <u>\$ 54</u> |

NOTE 3 – EMPLOYEE BENEFIT PLANS

The following is a table of retirement and other postretirement benefit expenses for the Association:

| | For the six months ended June 30, | |
|-------------------------------|-----------------------------------|---------------|
| | 2008 | 2007 |
| Pension | \$ 203 | \$ 188 |
| 401(k) | 56 | 54 |
| Other postretirement benefits | 114 | 127 |
| Total | <u>\$ 373</u> | <u>\$ 369</u> |

The following is a table of retirement and other postretirement benefit contributions for the Association:

| | Actual YTD Through 6/30/08 | Projected Contributions For Remainder of 2008 | Projected Total Contributions 2008 |
|-------------------------------|----------------------------|---|------------------------------------|
| Pension | \$ - | \$ - | \$ - |
| Other postretirement benefits | 101 | 102 | 203 |
| Total | <u>\$ 101</u> | <u>\$ 102</u> | <u>\$ 203</u> |

Market conditions could impact discount rates and return on plan assets which could change the above contribution projections by making additional contributions necessary before the next plan measurement date.

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 158, *"Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans"* (SFAS 158), which required the recognition of the overfunded or underfunded status of pension and other postretirement benefit plans on the balance sheet. The balance sheet recognition provisions of SFAS 158 were adopted at December 31, 2007 by the Association.

SFAS 158 also requires that employers measure the benefit obligation and plan assets as of the fiscal year end for fiscal years ending after December 15, 2008. In fiscal 2007 and earlier, a September 30 measurement date was used for pension and other postretirement benefit plans. The Standard provides two approaches for an employer to transition to a fiscal year end measurement date. The approach applied by the Association allows for the use of the measurements determined for the prior year end. Under this alternative, pension and other postretirement benefit expense measured for the three-month period October 1, 2007 to December 31, 2007 (determined using the September 30, 2007 measurement date) is reflected as an adjustment to beginning 2008 unallocated retained earnings. As a result, the Association decreased unallocated retained earnings and increased the pension liability by \$45 thousand.

Upon adoption, SFAS 158 further required the determination of the fair value of plan assets and recognition of actuarial gains and losses, prior service costs or credits, and transition assets or obligations as a component of accumulated other comprehensive income (AOCI). These amounts are subsequently recognized as components of net periodic benefit costs. For the first six months of 2008, \$67 thousand has been recognized as a credit to accumulated other comprehensive income and a debit to pension expense to reflect the amortization of the components previously recognized in AOCI.

Further details regarding employee benefit plans and adoption of SFAS 158 are contained in the 2007 Annual Report to Shareholders.