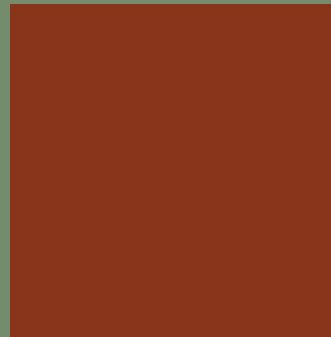
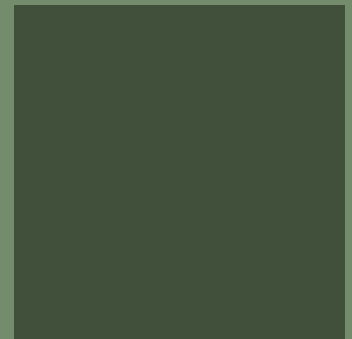




Financial Group

2005 Financial Report





Building a Family

In 1964, when Bill Ashley became CEO of Ashe Savings & Loan, all of the institution's customers suddenly became family.

Bill didn't just use numbers to decide if he would grant a loan. He got to know the individuals.

"Many people wouldn't qualify for a loan, and we did quite a bit on faith," said Ashley. "We believed in Ashe County and the people did not disappoint us."

Ashley goes on to say that today, more stringent regulations prevent us from giving loans on faith, but his philosophy lives on in the way that AF Financial Group continues to create services and programs that make life easier for our customers.



In 1939 Ashe Building & Loan granted the very first loan to add masonry to the home pictured above.

Our History

Realizing the growing need for a building and loan association in Ashe County, Glenn B. Graybeal took the first steps toward creating such an institution and submitted an application to the North Carolina Insurance Commission in 1938.

In January 1939 Ashe Building and Loan Association received its charter from the NC Insurance Commission and set up shop in the Parker Tie building in downtown West Jefferson. The shareholders met and elected ten directors, including Graybeal who also acted as Secretary-Treasurer and managed the day-to-day affairs of the building and loan. Twelve years later the Association expanded beyond its initial scope of lending and became Ashe Savings and Loan Association.

The year 1964 brought two major changes to the Association. Following Graybeal's death in July, the directors turned to Ashe County native William O. "Bill" Ashley, Jr. and he accepted the role of managing officer and later director, continuing the tradition of compassion, respect, and service that Graybeal had practiced for 25 years. That same year, Ashe Savings and Loan moved to 205 South Jefferson Avenue, which continues to serve as a branch office today.

In 1982 a federal charter was obtained and the company became Ashe Federal Savings and Loan and would later change its name again to Ashe Federal Bank. Bill Ashley retired in 1994 after 30 years of service, however he remained as a director until the year 2000. That same year Ashe Federal opened a second branch in Jefferson.

The years following Ashley's retirement saw rapid growth and expansion, as Ashe Federal became AF Bank and opened five additional branch locations in Ashe, Watauga, and Alleghany Counties. A mutual holding company, AsheCo, MHC, was established in 1996. A mid-tier holding company, AF Bankshares, Inc. was created in 1998 and in 2002 the company's shareholders voted to change its name to AF Financial Group.

Realizing that its customers' financial needs include more than banking, the Company expanded once again to offer insurance and investment services. AF Insurance Services, Inc. is home to six agencies in Ashe, Alleghany, Watauga, Surry, Wilkes, and Caldwell Counties and AF Investments provides services through office locations in West Jefferson and Boone and by appointment in other AF locations. Many things have changed over the past 66 years, but one thing about AF has remained the same – taking care of our customers with the friendly hometown service they deserve.

A Proud Heritage

Dreams Realized

AF Financial Group is in the business of making dreams come true. Whether it is a new home, the freedom of retirement, a new business, a college education, insuring your assets, or even a dream vacation, AF Financial Group equips its customers with the tools they need to enjoy their lives to the fullest.



Your Golden Years



Your Dream Home



Your Own Business



Your Child's Future



Dear Shareholder,

Fiscal year 2005 has been an exciting year for AF Financial Group with numerous changes and positive earnings growth. I joined the Company as President and Chief Executive Officer on November 1, 2004. I'm truly excited to be part of this Company that has been serving local communities' needs since 1939. During my first year, I have learned that our Company has a dedicated group of employees and a committed Board which exhibits strong ethical values and a desire to provide the highest quality financial services in the markets we serve.

We can see the results of this dedication in the financial results during the most recent fiscal year. Net income for the year ended June 30, 2005 was \$648,777 compared to a net loss of \$308,254 during the fiscal year ended June 30, 2004. Total assets on June 30, 2005 were \$214,101,115, a 1.2% increase over the June 30, 2004 total of \$211,619,177. At June 30, 2005, stockholders' equity totaled \$13,038,969 which was a 4.5% increase over the June 30, 2004 total of \$12,473,996. During the coming year you will find your Company focusing on improving the quality of every service we offer. We are interested in continuing our growth in the markets we serve; however, our primary focus will be enhancing the customer experience. This should produce moderate growth in the coming fiscal year. For detailed financial results and comparisons, please see the 10-KSB filed for the year ended June 30, 2005 enclosed with this annual report and proxy statement.

In addition to the financial results mentioned above, your Company made significant progress in a number of other areas in the year just ended.

- We opened our new Boone Financial Center on October 4, 2004. This Center brings together the services of AF Bank, AF Investments and AF Insurance under one roof in Boone.
- We have improved our deposit product line for both personal and business customers.
- We have created a Non-Profit Interest Checking account to serve the needs of those community organizations that serve all of us.
- To reduce cost and create a better referral network AF Brokerage has been disbanded as a separate entity and now operates as AF Investments, a unit of AF Bank.

This year's annual report highlights our past, present and future. Highlighted in the report is Bill Ashley, a former Director and President of AF and one reason for our success today. During my first week on the job Mr. Ashley came to see me to lend his support to the Company. It was a welcome that was very much appreciated. Another example of an important leader featured in the report is John D. Weaver. Mr. Weaver has been on the board since 1990 and has recently announced that he will retire in November 2005. Mr. Ashley's and Mr. Weaver's leadership and high ethical standards have had an enduring impact on our past success. In addition, both leaders have helped establish the foundation for a rewarding present and a continued future of serving our community needs and remaining a local community financial services company.

Thank you for your support during my first year at AF Financial Group. I believe that our continuing dedication to providing the highest quality financial services in the markets we serve will result in increased profitability and growth in the 2006 fiscal year and beyond. If you have any questions about the Company or how we may better serve you, your family, or your business, please let me know.

For AF Financial Group,



Robert E. Washburn
President and Chief Executive Officer



Our Team of Outstars

AF Financial Group is made up of individuals who believe in what they do. Their goal is not only to become a and secure about your financial situation. We value our team members and want to give you a glimpse into who they

Jennifer Adams

Gregory Ashley

Ann Ashman

Gayle Atkinson

E. Helen Bare

Joanna Barelski

Pamela Barker

Vance Bell, III

Shelley Bentley

James Blair

Lindsay Blevins

Peggy Blinson

Lori Brooks

Joseph Brown, III

Teresa Buchanan

Heather Burgess

Mary Ann Byrd

Jennifer Calhoun

John Carini

Jennifer Carrier

Robin Carter

Angelia Church

M. Diane Cochran

Scott Coe

David Cottrell

Michelle Cox

Thomas Crabtree

Bhupendra Dave

Tempie Davis

Vicki Davis

M. Denise Deitz

Pamela DeVall

Karen Durham

Andrea Eastridge

Donna Edwards

M. Drew Eldreth

Crystal Eller

Joseph Eller

Barbara Ezell

Pamela Fisher

Heather Graham

Thomas Graybeal

Marsha Greene

Marta Greene

Audrey Greene

Reba Grogan

Michael Grubb

Sandra Grubb

Mabel Hamm

Crystal Hardin

Melissa Harmon

Tracy Harris

Christine Hart

Dustin Hayes

William Hendricks

Christopher Hill

H. Christian Hilliard, II

Mary Horn

Jesse Horner

Brianna Houck

Dennis Houck

Nancy Houck

Gary Howell

Kimberly Isaacs

Stacey Jenkins

Michael Johnson

Gary Joines

Ann Jones

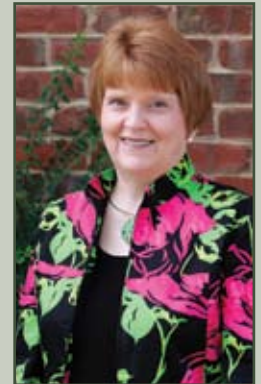
Margo Levi

Carolyn Lineberry

Martin Little

Shannon Marsh

“AF Bank is truly committed to its customers and employees. I enjoy getting to know the people I serve personally and seeing them leave happy.”



-Sandy Grubb



“One of the best feelings you can have is seeing the excitement on someone’s face when they are buying their home for the first time!”

-Mike Johnson

Leading Individuals

trusted friend, but to empower you to make decisions, realize your goals, and feel safe are and how they believe in you.



"The people of AF share a commitment to do what is best for the customer and try to see things from the customer's perspective."

-Scott Coe

"AF's greatest assets are its employees. We care about the customers and go out of our way to meet their complete financial needs."



-Alice Thompson

Conard Mash	Jane Roark
Dana Mastrangelo	Miranda Roark
Julie Maye	Patricia Severt
Margaret McGlamery	Belinda Sheets
Candida Miller	Jessica Sheets
Cathy Miller	Jennifer Shelton
Christopher Miller	D. Shane Simmons
Debra Miller	Mary Ellen Studstrup
Elizabeth Miller	Beverly Talley
Heather Miller	Alice Thompson
Melanie Miller	Michael Todd-Stone
Vicky Moody	Mark Trivette
Kristen Olinger	Mack Vannoy
Lori Osborn	Sheryl Waddell
Kathy Pell	Barbara Walters
Barbara Pim	Lisa Ward
Sandra Poe	Robert Washburn
Sommer Poe	Donna Watson
Andrea Potter	C. Gregory Westbrook
Mae Potter	Kimberly Wheeler
Conla Rainey	Eddie Wiles
Donna Rash	Allison Williams
Jennifer Richardson	Teresa Winebarger
Malinda Richardson	James Young

At Your Service



Front row, left to right:

Robert E. Washburn, President and Chief Executive Officer of AF Financial Group and AF Bank; Donald R. Moore, Restaurant Owner; Claudia L. Kelley, Ph.D, Associate Professor of Accounting at Appalachian State University; Jerry L. Roten, Clerk of Superior Court of Ashe County; Wayne R. Burgess, Vice President and Manager of Burgess Furniture; Kenneth R. Greene, Owner of Builders Mart of Ashe, Inc.

Back row, left to right:

Jimmy D. Reeves, Chairman of AF Financial Group and Partner in the law firm of Vannoy & Reeves, PLLC; Michael M. Sherman, President and Chief Executive of Zibra, LLC; John D. Weaver, Vice President of Weaver Tree Farm; Jan R. Caddell, Vice Chairman of AF Financial Group and President and General Manager of Caddell Broadcasting, Inc.

Report of Independent Registered Public Accounting Firm

To the Stockholders and Board of Directors
AF Financial Group and Subsidiaries
West Jefferson, North Carolina

We have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated statements of financial condition of AF Financial Group and subsidiaries (the "Company") as of June 30, 2005 and 2004, and the related consolidated statements of income (loss), stockholders' equity, and cash flows for the years then ended (not presented herein); and in our report dated September 6, 2005, we expressed an unqualified opinion on those consolidated financial statements. The accompanying condensed consolidated financials statements as of June 30, 2005 and for the year then ended are the responsibility of the Company's management. Our responsibility is to express an opinion on such condensed consolidated financial statements in relation to the completed consolidated financial statements.

In our opinion, the information set forth in the accompanying condensed consolidated statement of financial condition as of June 30, 2005 and 2004 and the related condensed consolidated statement of income (loss) for the years then ended, is fairly stated, in all material respects, in relation to the consolidated financial statements from which it has been derived.

A handwritten signature in cursive script that reads "Dixon Hughes PLLC".

Charlotte, North Carolina
September 6, 2005



What Tomorrow Brings



A Promising Future



John D. Weaver owns a Christmas Tree Farm in Ashe County and serves on the Board of Directors at AF Financial Group. He is pictured here with his grandson, Will.

“I’m proud of the way AF Financial Group has worked to keep in touch with its heritage--its roots--but is still constantly looking forward to what they can do in the future to better serve their customers. The Board has worked hard to install management that help us develop and grow. We’ve created new programs, and are currently doing research to get to know what our customers expect.”

“Our goals in the future are all about relationships. We’re the only community bank left around here and we’re proud of it. We want to strengthen the community through our continued contributions through scholarships, donations to charitable organizations and volunteer work. And we want to build even more relationships with individuals, business people, and other organizations, to help our mountains to prosper.”

-John D. Weaver
Board Member



Financial Group

BANKS

Boone

1675 Blowing Rock Road
828-265-2580

Jefferson

840 East Main Street
336-246-4344

Sparta

381 South Main Street
336-372-7990

Warrensville

4951 NC Hwy. 88 W
336-384-4900

West Jefferson

205 South Jefferson Ave.
1441 Mt. Jefferson Road
1489 Mt. Jefferson Road
(in Wal-Mart)
336-246-4344

INVESTMENTS

Boone

1675 Blowing Rock Road
828-265-2580

West Jefferson

206 South Jefferson Ave.
1441 Mt. Jefferson Road
336-246-4345

INSURANCE

Boone

1675 Blowing Rock Road
828-265-2580

Elkin

948 Johnson Ridge Road
336-835-4060

Jefferson

840 East Main Street
336-246-4344

Lenoir

324 Morganton Blvd. SW
828-758-4453

North Wilkesboro

315 Main Street
336-838-3100

Sparta

381 South Main Street
336-372-7990

West Jefferson

206 South Jefferson Avenue
1441 Mt. Jefferson Road
336-246-4344

www.afgrp.com