

November 2008

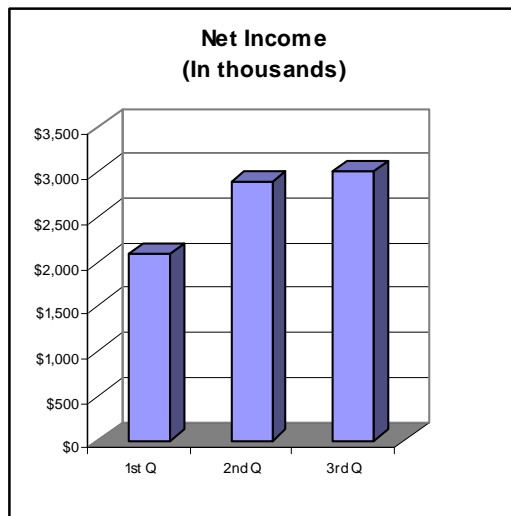
A Message to our Community, Customers, and Stockholders:

“Different is Good.”

That was the theme of Alliance Financial Corporation’s 2007 Annual Report, in which we sought to differentiate ourselves from those in our industry who were experiencing difficulties with sub-prime mortgage lending. Since we released that report in March 2008, changes to the financial services industry have been nothing less than historic. The financial industry is in the midst of its greatest challenges, and its greatest change, in seventy years. Deteriorating credit quality and losses on investment securities are affecting many financial institutions, large and small, on Wall Street and on Main Street, in every region of the country, including our own. **At Alliance, however, things truly are different.**

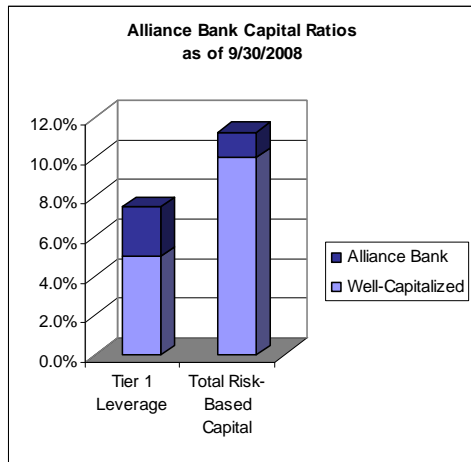
With challenges and change, comes opportunity. As we said in our 2007 Annual Report, “The last thing we’d ever want to be is just another bank.”

We’re proud to be different in the way we continue to conduct our business and serve the financial needs of our markets. Our exceptional performance in what is an extremely difficult environment for financial institutions is the result of the disciplined approach to banking by the employees of Alliance. We have consistently maintained a prudent credit culture and employed conservative balance sheet management strategies irrespective of economic and interest rate cycles, and these practices have clearly differentiated us from those in the financial services industry who are now experiencing difficulties.



Our **profitability** is at its highest levels in our history. In fact, Alliance achieved record levels of net income in both the second and third quarters of 2008. Net income was \$3.0 million in the third quarter, which was 24.9% higher than the third quarter of 2007. Diluted earnings per share increased 27.5% to \$0.65 in the third quarter, compared with \$0.51 per share in the year-ago quarter.

Net income for the nine months ended September 30, 2008 was \$8.0 million or \$1.73 per diluted share, an increase of 13.3% compared with \$7.0 million or \$1.47 per diluted share in the year-ago period.



Our **capital ratios** remain strong, and continue to comfortably exceed the Federal Deposit Insurance Corporation's thresholds for classification as "well-capitalized." Alliance Bank, the banking subsidiary of Alliance Financial Corporation, had Tier 1 leverage and total risk-based capital ratios of 7.25% and 11.27%, respectively at September 30, 2008. The minimum levels required for classification as a well-capitalized institution are 5.0% and 10.0%, respectively.

Our **asset quality** is fundamentally sound, with delinquent and non-performing loans decreasing in 2008 from already manageable levels at the end of 2007. Commercial banks nationwide with assets between \$1 billion and \$3 billion have experienced a near doubling in nonperforming loan ratios, with the average nonperforming loan ratio to total loans for these banks equaling 1.80% at September 30. Alliance's total non-performing loan ratio, however, has dropped by nearly a third since the end of 2007, and was equal to 0.52% of total loans at September 30, 2008. This improvement is especially noteworthy in the difficult economic and credit environments in which we are operating, and is in clear contrast to the national average for banks our size.

Our primary business of **taking in deposits** and **making loans** continues as it always has. Total deposits increased \$16.9 million in the third quarter of 2008, while total loans and leases increased \$13.5 million. Most of the increase in loans was in residential mortgages, which reached an all-time high of \$305.3 million at September 30. Our residential mortgage origination volume increased 32% in the third quarter compared with the year-ago period, and was up 53% for the first nine months of 2008 compared with the same period in 2007. Through the end of October, we are on a pace to originate \$100 million of residential mortgage loans in 2008.

We continue to support the financing needs of small and medium-size businesses in Central New York. During the third quarter, we originated commercial loans totaling \$18 million, and for the first nine months of 2008, our commercial loan originations totaled \$45 million. On top of this, Alliance stands ready to provide our commercial customers additional financing for the day-to-day operations of their businesses through commercial credit facilities. At September 30, 2008, Alliance's commercial line-of-credit customers had access to additional credit of \$61 million on their credit lines.

We're Alliance Bank and Central New York is right where we want to be.

On behalf of the Board of Directors of Alliance Financial Corporation,

Jack H. Webb
Chairman, President and Chief Executive Officer

Alliance Financial Corporation Board of Directors:

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