NORTHEAST BANCORP /ME/
Form 10-Q
November 14, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10 Q

X Quarterly report pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934

For the quarterly period ended September 30, 2007

Or

___ Transition report pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934

For the transition period for _______________ to _______________

Commission File Number 1-14588

Northeast Bancorp

(Exact name of registrant as specified in its charter)

Maine	01-0425066
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
500 Canal Street, Lewiston, Maine	04240
(Address of Principal executive offices)	(Zip Code)

(207) 786-3245
Registrant's telephone number, including area code

Not Applicable
Former name, former address and former fiscal year, if changed since last report.

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subjected to such filing requirements for the past 90 days. Yes _X_ No ___

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (check one):
Large accelerated filer __ Accelerated filer __ Non-accelerated filer X

Indicate by check mark whether the registrant is a shell company (as defined by Rule 12b-2 of the Exchange Act). Yes_ No X

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. As of November 1, 2007, the registrant had outstanding 2,368,982 shares of common stock, $1.00 stated value per share.

Part I. Financial Information

Item 1.	Consolidated Financial Statements
	Consolidated Balance Sheets September 30, 2007 (Unaudited) and June 30, 2007
	Consolidated Statements of Income (Unaudited) Three Months Ended September 30, 2007 and 2006
	Consolidated Statements of Changes in Stockholders' Equity (Unaudited) Three Months Ended September 30, 2007 and 2006
	Consolidated Statements of Cash Flows (Unaudited) Three Months ended September 30, 2007 and 2006
	Notes to Consolidated Financial Statements (Unaudited)
Item 2.	Management's Discussion and Analysis of Results of Operations and Financial Condition
Item 3.	Quantitative and Qualitative Disclosure about Market Risk
Item 4.	Controls and Procedures

Part II. Other Information

Item 1.	Legal Proceedings
Item 1.a.	Risk Factors
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds
Item 3.	Defaults Upon Senior Securities
Item 4.	Submission of Matters to a Vote of Security Holders
Item 5.	Other Information
Item 6.	Exhibits

PART 1 - FINANCIAL INFORMATION

Item 1. Financial Statements

NORTHEAST BANCORP AND SUBSIDIARY
Consolidated Balance Sheets

	September 30, 2007 (Unaudited)	June 30, 2007
Assets		
Cash and due from banks	$ 7,353,302	$ 9,065,330
Interest-bearing deposits	1,562,126	1,676,391
Total cash and cash equivalents	8,915,428	10,741,721
Available-for-sale securities, at fair value	109,525,834	86,348,070
Loans held-for-sale	829,610	1,636,485
Loans receivable	421,289,576	425,571,418
Less allowance for loan losses	5,756,000	5,756,000
Net loans	415,533,576	419,815,418
Premises and equipment, net	7,388,998	7,545,430
Accrued interest receivable	2,590,134	2,586,720
Federal Home Loan Bank stock, at cost	4,825,700	4,825,700
Federal Reserve Bank stock, at cost	471,500	471,500
Goodwill	3,467,993	2,880,803
Intangible assets, net of accumulated amortization of $2,784,685 at 09/30/07 and $2,681,148 at 6/30/07	4,785,544	4,110,081
Bank owned life insurance (BOLI)	9,946,784	9,844,584
Other assets	5,398,590	5,994,468
Total assets	$ 573,679,691	$ 556,800,980
Liabilities and Stockholders' Equity		
Liabilities:		
Deposits		
Demand	$ 34,557,846	$ 36,332,604
NOW	55,167,710	53,405,241
Money market	8,429,069	8,053,552
Regular savings	21,518,956	21,145,567
Brokered time deposits	18,860,960	22,546,163
Certificates of deposit	222,478,254	223,070,650
Total deposits	361,012,795	364,553,777
Federal Home Loan Bank advances	85,240,181	93,016,698
Structured repurchase agreements	30,000,000	-
Short-term borrowings	31,685,285	33,105,377
Junior subordinated debentures issued to affiliated trusts	16,496,000	16,496,000
Capital lease obligation	2,620,886	2,653,511

Other borrowings		3,200,057		2,292,163
Other liabilities		2,783,353		3,833,576
Total liabilities		533,038,557		515,951,102
Commitments and contingent liabilities				
Stockholders' equity				
Preferred stock, $1.00 par value, 1,000,000 shares authorized; none issued		-		-
Common stock, at stated value, 15,000,000 shares authorized; 2,371,332 and 2,448,832 shares outstanding at September 30, 2007 and June 30, 2007, respectively		2,371,332		2,448,832
Additional paid-in capital		3,409,539		4,715,164
Retained earnings		35,810,257		35,600,428
Accumulated other comprehensive loss		(949,994)		(1,914,546)
Total stockholders' equity		40,641,134		40,849,878
Total liabilities and stockholders' equity	$	573,679,691	$	556,800,980

NORTHEAST BANCORP AND SUBSIDIARY

Consolidated Statements of Income

(Unaudited)

	Three Months Ended September	
	2007	2006
Interest and dividend income:		
Interest on loans	$ 7,723,178	$ 7,942,105
Interest on Federal Home Loan Bank overnight deposits	10,909	19,494
Taxable interest on available-for-sale securities	973,414	803,909
Tax-exempt interest on available-for-sale securities	111,123	110,381
Dividends on available-for-sale securities	32,779	33,661
Dividends on Federal Home Loan Bank and Federal Reserve Bank stock	85,283	100,429
Other interest and dividend income	20,201	12,010
Total interest and dividend income	8,956,887	9,021,989
Interest expense:		
Deposits	3,414,576	3,350,654
Federal Home Loan Bank advances	1,102,051	934,636
Short-term borrowings	372,425	307,829
Junior subordinated debentures issued to affiliated trusts	273,480	277,991
Structured repurchase agreements	125,989	-
Obligation under capital lease agreements	33,441	35,061
Other borrowings	42,078	441
Total interest expense	5,364,040	4,906,612
Net interest and dividend income before provision for loan losses	3,592,847	4,115,377
Provision for loan losses	190,283	300,786

Net interest and dividend income after provision for loan losses	3,402,564	3,814,591
Noninterest income:		
Fees for other services to customers	273,613	266,808
Net securities (losses) gains	(5,937)	4,386
Gain on sales of loans	152,956	95,785
Investment commissions	398,010	371,608
Insurance commissions	866,042	428,465
BOLI income	111,766	97,044
Other income	192,924	198,332
Total noninterest income	1,989,374	1,462,428
Noninterest expense:		
Salaries and employee benefits	2,861,145	2,773,924
Occupancy expense	411,007	411,349
Equipment expense	379,380	398,369
Intangible assets amortization	103,537	66,762
Other	1,086,535	1,019,274
Total noninterest expense	4,841,604	4,669,678
Income before income tax expense	550,334	607,341
Income tax expense	119,769	152,674
Net income	$ 430,565	$ 454,667
Earnings per common share:		
Basic	$ 0.18	$ 0.19
Diluted	$ 0.18	$ 0.18
Net interest margin (tax equivalent basis)	2.75%	3.05%
Net interest spread (tax equivalent basis)	2.42%	2.77%
Return on average assets (annualized)	0.31%	0.32%
Return on average equity (annualized)	4.17%	4.52%
Efficiency ratio	87%	84%

NORTHEAST BANCORP AND SUBSIDIARY

Consolidated Statements of Changes in Stockholders' Equity

Three Months Ended September 30, 2007 and 2006

(Unaudited)

	Preferred Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total
Balance at June 30, 2006	$ -	$ 2,447,132	$ 4,675,258	$ 34,596,204	$ (2,622,469)	$ 39,096,125
Net income for three months ended 9/30/06				454,667		454,667

Other comprehensive income net of tax:						
Net unrealized losses on investments available for sale, net of reclassification adjustment					1,170,126	1,170,126
Total comprehensive income						1,624,793
Dividends on common stock at $0.09 per share				(220,242)		(220,242)
Common stock issued in connection with the purchase of branch real estate		5,000	98,000			103,000
Balance at September 30, 2006	$ -	$ 2,452,132	$ 4,773,258	$ 34,830,629	$ (1,452,343)	$ 40,603,676
Balance at June 30, 2007	$ -	$ 2,448,832	$ 4,715,164	$ 35,600,428	$ (1,914,546)	$ 40,849,878
Net income for three months ended 9/30/07				430,565		430,565
Other comprehensive income net of tax:						
Net unrealized losses on investments available for sale, net of reclassification adjustment					964,552	964,552
Total comprehensive income						1,395,117
Dividends on common stock at $0.09 per share				(220,736)		(220,736)
Common stock re-purchased		(77,500)	(1,305,625)			(1,383,125)
Balance at September 30, 2007	$ -	$ 2,371,332	$ 3,409,539	$ 35,810,257	$ (949,994)	$ 40,641,134

NORTHEAST BANCORP AND SUBSIDIARY

Consolidated Statements of Cash Flows

(Unaudited)

	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006
Cash (used) provided by operating activities:	$ (485,207)	$ 266,586
Cash flows from investing activities:		
Available-for-sale securities purchased	(25,540,529)	(3,133,932)
Available-for-sale securities matured	3,440,048	2,566,629
Available-for-sale securities sold	395,695	266,573
Net change in loans	4,366,136	(4,352,246)
Net capital expenditures	(111,003)	(46,681)
Cash paid in connection with purchase of branch real estate	-	(297,000)
Cash paid in connection with acquisition of insurance agency	(425,250)	-
Net cash used by investing activities	(17,874,903)	(4,996,657)
Cash flows from financing activities:		
Net change in deposits	(3,540,982)	(5,006,450)
Net change in short-term borrowings	(1,420,092)	9,301,032
Dividends paid	(220,736)	(220,242)
Company stock repurchased	(1,383,125)	-
Advances from the Federal Home Loan Bank	-	19,000,000
Repayment of advances from the Federal Home Loan Bank	(8,211,517)	(17,205,734)
Net advances on Federal Home Loan Bank overnight advances	435,000	-
Structured repurchase agreements	30,000,000	-
Debt from purchase of insurance agency	933,000	-
Repayment on debt from insurance agencies acquisitions	(25,106)	-
Repayment on capital lease obligation	(32,625)	(31,004)
Net cash provided by financing activities	16,533,817	5,837,602
Net (decrease) increase in cash and cash equivalents	(1,826,293)	1,107,531
Cash and cash equivalents, beginning of period	10,741,721	12,103,721
Cash and cash equivalents, end of period	$ 8,915,428	$ 13,211,252

Cash and cash equivalents include cash on hand, amounts due from banks, and interest-bearing deposits.

	2007	2006
Supplemental schedule of noncash activities:		
Net change in valuation for unrealized gains/losses, net of income tax, on available-for-sale securities	$ 964,552	$ 1,170,126
Common stock issued in connection with purchase of branch real estate	-	103,000
Supplemental disclosures of cash paid during the period for:		
Income taxes paid, net of refunds	$ 220,000	$ 664,500
Interest paid	5,306,321	4,927,132
Insurance Agency acquisitions - see Note 10		

NORTHEAST BANCORP AND SUBSIDIARY
Notes to Consolidated Financial Statements
September 30, 2007
(Unaudited)

1. Basis of Presentation

The accompanying unaudited condensed and consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, the accompanying consolidated financial statements contain all adjustments (consisting principally of normal recurring accruals) considered necessary for a fair presentation of the Company's financial position at September 30, 2007, the results of operations for the three month periods ended September 30, 2007 and 2006, the changes in stockholders' equity for the three month periods ended September 30, 2007 and 2006, and the cash flows for the three month periods ended September 30, 2007 and 2006. Operating results for the three month period ended September 30, 2007 are not necessarily indicative of the results that may be expected for the fiscal year ending June 30, 2008. For further information, refer to the audited consolidated financial statements and footnotes thereto for the fiscal year ended June 30, 2007 included in the Company's Annual Report on Form 10-K. Certain June 30, 2007 amounts have been reclassified to be consistent with the September 30, 2007 financial statements.

2. Junior Subordinated Debentures

NBN Capital Trust II and NBN Capital Trust III were created in December 2003. NBN Capital Trust IV was created in December 2004. Each trust is a Delaware statutory trust (together, the "Private Trusts"). The exclusive purpose of the Private Trusts was (i) issuing and selling Common Securities and Preferred Securities (the “Trust Preferred Securities”) in a private placement offering, (ii) using the proceeds of the sale of the Trust Preferred Securities to acquire Junior Subordinated Deferrable Interest Notes of the Company ("Junior Subordinated Debentures"); and (iii) engaging only in those other activities necessary, convenient, or incidental thereto. Accordingly the Junior Subordinated Debentures are the sole assets of each of the Private Trusts.

The following table summarizes the Junior Subordinated Debentures issued by the Company to each Private Trust and the Trust Preferred securities issued by each Trust at September 30, 2007 and June 20, 2007. Amounts include the Junior Subordinated Debentures acquired by the Private Trusts from the Company with the capital contributed by the Company in exchange for the common securities of such trust. The Trust Preferred Securities were sold in two separate private placement offerings. The Company has the right to redeem the Junior Subordinated Debentures, in whole or in part, on or after March 30, 2009, for NBN Capital Trust II and III, and on or after February 23, 2010, for NBN Capital Trust IV, at the redemption price specified in the Indenture plus accrued but unpaid interest to the redemption date.

Affiliated Trusts	Trust Preferred Securities	Common Securities	Junior Subordinated Debentures	Interest Rate	Maturity Date
NBN Capital Trust II	$ 3,000,000	$ 93,000	$ 3,093,000	8.03%	March 30, 2034
NBN Capital Trust III	3,000,000	93,000	3,093,000	6.50%	March 30, 2034
NBN Capital Trust IV	10,000,000	310,000	10,310,000	5.88%	February 23, 2035
Total	$ 16,000,000	$ 496,000	$ 16,496,000	6.40%	

NBN Capital Trust II pays a variable rate based on three month LIBOR plus 2.80%, NBN Capital Trust III pays a 6.50% fixed rate until March 30, 2009 when the rate changes to a variable rate based on three month LIBOR plus 2.80%, and NBN Capital Trust IV pays a 5.88% fixed rate until February 23, 2010 when the rate changes to a variable rate based on three month LIBOR plus 1.89%. Accordingly, the Trust Preferred Securities of the Private Trusts currently pay quarterly distributions at an annual rate of 8.03% for the stated liquidation amount of $1,000 per Trust Preferred Security for NBN Capital Trust II, an annual rate of 6.50% for the stated liquidation amount of $1,000 per Trust Preferred Security for NBN Capital Trust III and an annual rate of 5.88% for the stated liquidation amount of $1,000 per Trust Preferred Security for NBN Capital Trust IV. The Company has fully and unconditionally guaranteed all of the obligations of each trust. The guaranty covers the quarterly distributions and payments on liquidation or redemption of the Private Trust Preferred Securities, but only to the extent of funds held by the trusts. Based on the current rates, the annual interest expense is approximately $1,056,000.

3. Loans

The following is a summary of the composition of loans at:

	September 30, 2007	June 30, 2007
Residential real estate	$ 142,354,415	$ 145,184,733
Commercial real estate	108,864,523	112,534,812
Construction	6,254,224	5,450,826
Commercial	38,917,994	40,783,958
Consumer & Other	122,077,760	118,880,723
Total	418,468,916	422,835,052
Net Deferred Costs	2,820,660	2,736,366
Total Loans	$ 421,289,576	$ 425,571,418

4. Allowance for Loan Losses

The following is an analysis of transactions in the allowance for loan losses:

	Three months Ended September 30, 2007	2006
Balance at beginning of period	$ 5,756,000	$ 5,496,000
Add provision charged to operations	190,283	300,786
Recoveries on loans previously charged off	17,788	40,998
	5,964,071	5,837,784
Less loans charged off	208,071	231,784
Balance at end of period	$ 5,756,000	$ 5,606,000

5. Securities

Securities available-for-sale at cost and approximate fair values and maturities are summarized below:

	September 30, 2007		June 30, 2007	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Debt securities issued by U. S. Government-sponsored enterprises	$ 20,765,448	$ 20,437,642	$ 21,765,732	$ 21,158,409
Mortgage-backed securities	76,365,301	75,504,323	53,987,824	52,138,732
Municipal Bonds	11,280,609	11,182,258	11,067,197	10,709,069

Corporate bonds	500,000	493,285	500,000	484,625
Equity securities	2,031,348	1,908,326	1,928,144	1,857,235
	$ 110,942,706	$ 109,525,834	$ 89,248,897	$ 86,348,070

	September 30, 2007		June 30, 2007	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	$ 13,194,898	$ 13,026,854	$ 6,505,701	$ 6,410,365
Due after one year through five years	5,680,304	5,630,635	13,370,205	12,989,363
Due after five years through ten years	997,048	983,290	996,925	972,840
Due after ten years	12,673,807	12,472,406	12,460,098	11,979,535
Mortgage-backed securities (including securities with interest rates ranging from 4.0% to 6.4% maturing November 2007 to March 2037)	76,365,301	75,504,323	53,987,824	52,138,732
Equity securities	2,031,348	1,908,326	1,928,144	1,857,235
	$ 110,942,706	$ 109,525,834	$ 89,248,897	$ 86,348,070

6. Advances from the Federal Home Loan Bank

A summary of borrowings from the Federal Home Loan Bank is as follows:

September 30, 2007

Principal Amounts	Interest Rates	Maturity Dates For Periods Ending September 30,
$ 52,240,181	2.68% - 5.83%	2008
20,000,000	4.86 – 5.11	2009
3,000,000	4.99	2011
10,000,000	4.26	2017
$ 85,240,181		

June 30, 2007

Principal Amounts	Interest Rates	Maturity Dates For Periods Ending June 30,
$ 50,016,698	2.68% - 5.69%	2008
30,000,000	4.86 - 5.21	2009
3,000,000	4.99	2011
10,000,000	4.26	2017
$ 93,016,698		

The Federal Home Loan Bank has the option to call $21,000,000 of the outstanding advances at September 30, 2007. The options are continuously callable quarterly until maturity.

7. Structured Repurchase Agreements

In a leveraging strategy, during the three months ended September 30, 2007, the Company borrowed $30,000,000. The borrowed funds, along with available funds, were used to acquire $32,100,895 of mortgage-backed securities. The funding was implemented in two parts and had imbedded purchased interest rate caps and sold interest rate floors, as summarized below. The interest rate caps eliminated the balance sheet risk to rising interest rates. Interest is payable quarterly, and the interest rates are fixed for the first two years during which the issuer of the debt may not terminate the transaction. Following the two years ending August 28, 2009, the interest rates will reset quarterly based on three month LIBOR and the issuer of the debt can terminate the transaction on any quarterly payment date. The final maturity is August 28, 2012.

Amount	Interest Rate	Cap/Floor	Amount of Cap/Floor	Strike Rate
$20,000,000	4.68%	Purchased Caps	$40,000,000	5.50%
$10,000,000	3.98%	Sold Floors	$20,000,000	4.86%

8. Stock-Based Compensation

The Company has stock-based employee compensation plans, which are described more fully in Note 1 of the June 30, 2007 audited consolidated financial statements. The Company adopted Statement of Financial Accounting Standard No. 123 (revised 2004), *Shared-Based Payment* ("SFAS 123-R"), effective for the fiscal year beginning July 1, 2005, superseding APB Opinion 25 and replacing FASB Statement No. 123. Prior to July 1, 2005, the Company utilized the intrinsic value methodology allowed by APB Opinion 25. SFAS 123-R requires companies to measure and record compensation expense for stock options and other share-based payments based on the instruments' fair value reduced by expected forfeitures. Under the modified prospective approach adopted by the Company, the Company recognizes expense for new options awarded and to awards modified, repurchased or canceled after the effective date. Since there were no new options granted (or modifications of existing options) during the three months ended September 30, 2007, and since all previously granted options were fully vested at the grant date, adoption of the SFAS 123-R had no impact on the September 30, 2007 financial statements.

9. Capital Lease

The principal executive and administrative offices of the Company and the Bank were relocated to 500 Canal Street, Lewiston, Maine ("Headquarters Building") from 158 Court Street, Auburn, Maine in August, 2005. The Bank entered into a fifteen year lease with respect to the Headquarters Building. Our principal executive and administrative offices, along with our operations, loan processing and underwriting, loan servicing, accounting, human resources, and commercial lending departments, were consolidated to this four story building located in downtown Lewiston. We lease the entire building, a total of 27,000 square feet. Since the present value of the lease payments over the fifteen year term ($264,262 per year for each of the initial ten years of the lease term and $305,987 per year for each of the last five years) exceeded 90% of the fair value of the property, we recorded a capital lease of $2,892,702 in Premises and Equipment and an Obligation under Capital Lease Agreement. The Obligation under Capital Lease was $2,620,886 and $2,653,511 at September 30, 2007 and June 30, 2007, respectively. The capital lease asset is being amortized over the lease term.

10. Insurance Agency Acquisitions

On August 30, 2007, Northeast Bank Insurance Group, Inc., a wholly-owned subsidiary of Northeast Bank, acquired substantially all of the assets of the Hartford Insurance Agency (Hartford) located in Lewiston, Maine for cash and debt. The Hartford acquisition purchase price was $1,358,000, of which $425,000 was paid in cash and $833,000 is payable to the seller over a term of seven years and bearing an interest rate of 6.50% and $100,000 was payable over the same seven year period but bears no interest. The goodwill and customer list intangibles recorded as a result of this acquisition have been estimated and are subject to change.

All acquisitions were accounted for using the purchase method and resulted in increases in customer list intangibles and goodwill on the balance sheet. All agreements also call for a reduction of the purchase price should the stipulated minimum income levels not be attained. The customer list intangibles will be amortized over twelve years. The non-compete agreements will be amortized over the individual's expected years of employment plus three years. The results of operations of Hartford have been included in the consolidated financial statements of the Company since the acquisition date. There is no pro-forma disclosure included because Hartford was not considered a significant acquisition. The details of the purchase appear below.

Purchase Price:	Hartford
Cash	$ 425,250
Debt	933,000
Acquisition Costs	5,181
Total	$ 1,363,431
Allocation:	
Customer List	$ 679,000
Non-compete Agreement	100,000
Goodwill	584,431
Total	$ 1,363,431

Item 2. Management's Discussion and Analysis of Results of Operations and Financial Condition

This Management's Discussion and Analysis of Results of Operations and Financial Condition presents a review of the results of operations for the three months ended September 30, 2007 and 2006 and the financial condition at September 30, 2007 and June 30, 2007. This discussion and analysis is intended to assist in understanding the results of operations and financial condition of Northeast Bancorp and its wholly-owned subsidiary, Northeast Bank. Accordingly, this section should be read in conjunction with the consolidated financial statements and the related notes and other statistical information contained herein. See our annual report on Form 10-K, for the fiscal year ended June 30, 2007, for discussion of the critical accounting policies of the Company. Certain amounts in the prior year have been reclassified to conform to the current-year presentation.

A Note about Forward Looking Statements

This report contains certain "forward-looking statements" within the meaning of federal securities law Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, such as statements relating to our financial condition, prospective results of operations, future performance or expectations, plans, objectives, prospects, loan loss allowance adequacy, simulation of changes in interest rates, capital spending and finance sources, and revenue sources. These statements relate to expectations concerning matters that are not historical facts. Accordingly, statements that are based on management's projections, estimates, assumptions, and judgments constitute forward-looking statements. These forward-looking statements, which are based on various assumptions (some of which are beyond the Company's control), may be identified by reference to a future period or periods, or by the use of forward-looking terminology such as "believe", "expect", "estimate", "anticipate", "continue", "plan", "approximately", "intend", "objective", "goal", "project", or other similar terms or variations on those terms, or the future or conditional verbs such as "will", "may", "should", "could", and "would". In addition, the Company may from time to time make such oral or written "forward-looking statements" in future filings with the Securities and Exchange Commission (including exhibits thereto), in its reports to shareholders, and in other communications made by or with the approval of the Company.

Such forward-looking statements reflect our current views and expectations based largely on information currently available to our management, and on our current expectations, assumptions, plans, estimates, judgments, and projections about our business and our industry, and they involve inherent risks and uncertainties. Although we believe that these forward-looking statements are based on reasonable estimates and assumptions, they are not guarantees of future performance and are subject to known and unknown risks, uncertainties, contingencies, and other factors. Accordingly, we cannot give you any assurance that our expectations will, in fact, occur or that our estimates or assumptions will be correct. We caution you that actual results could differ materially from those expressed or implied by such forward-looking statements due to a variety of factors, including, but not limited to, those related to the economic environment, particularly in the market areas in which the Company operates, competitive products and pricing, fiscal and monetary policies of the U.S. Government, changes in government regulations affecting financial institutions, including regulatory fees and capital requirements, changes in prevailing interest rates, acquisitions and the integration of acquired businesses, credit risk management, asset/liability management, changes in technology, changes in the securities markets, and the availability of and the costs associated with sources of liquidity. Accordingly, investors and others are cautioned not to place undue reliance on such forward-looking statements. For a more complete discussion of certain risks and uncertainties affecting the Company, please see "Item 1. Business - Forward-Looking Statements and Risk Factors" set forth in our Form 10-K for the fiscal year ended June 30, 2007. These forward-looking statements speak only as of the date of this report and we do not undertake any obligation to update or revise any of these forward-looking statements to reflect events or circumstances occurring after the date of this report or to reflect the occurrence of unanticipated events.

Overview of Operations

This Overview is intended to provide a context for the following Management's Discussion and Analysis of the Results of Operations and Financial Condition, and should be read in conjunction with our unaudited consolidated financial statements, including the notes thereto, in this quarterly report on Form 10-Q, as well as our audited consolidated financial statements for the year ended June 30, 2007 as filed on Form 10-K with the Securities and Exchange Commission (“SEC”). We have attempted to identify the most important matters on which our management focuses in evaluating our financial condition and operating performance and the short-term and long-term opportunities, challenges, and risks (including material trends and uncertainties) which we face. We also discuss the action we are taking to address these opportunities, challenges, and risks. The Overview is not intended as a summary of, or a substitute for review of, Management's Discussion and Analysis of the Results of Operations and Financial Condition.

Northeast Bank is faced with three challenges: growing loans, improving net interest margins, and improving the efficiency ratio.

Loans have decreased compared to June 30, 2007, due principally to decreases in residential real estate, commercial real estate, and commercial loans. While competition for commercial real estate and small commercial loans is intense, we are not competing for relationships where we believe transactions do not reflect pricing or structure for risk.

To improve net interest income, during the quarter ended September 30, 2007, we purchased $30 million of mortgage-backed securities funded through a repurchase agreement. This leveraging of our balance sheet increased overall earning assets.

Net interest margins are expected to continue to decline. The competition for deposits and the relatively high cost of attracting new deposits is expected to maintain the overall cost of funds. By lowering the federal funds rate in September, the Federal Reserve Bank caused loans with interest rates tied to prime rate and subject to change immediately to decline by 50 basis points. In contrast, any decline in interest rates on interest-bearing deposits will occur over an extended number of months. Our certificates of deposits, which reprice over the next twelve months, are expected to reprice to interest rates slightly lower than one year ago. We believe that the prospect of additional decreases in prime rate in the immediate future is likely. Thus, any improvement in net interest income would result from an increased volume of new loan originations or investment purchases, as opposed to rate increases. As of June 30, 2007, the balance sheet was slightly liability sensitive based on a twelve month repricing period. A liability sensitive position indicates that more liabilities than assets repriced during the repricing period and would generally be expected to result in a decrease in net interest income during a period of rising interest rates.

Management believes that the allowance for loan losses as of September 30, 2007 was adequate, under present conditions, for credit risk known in the loan portfolio. Non-accrual loans decreased slightly compared to June 30, 2007.

We expect to continue to increase non-interest income through the continued expansion of Northeast Bank Insurance Agency, Inc. into southern Maine through the acquisition of existing insurance agencies, the expansion of the wealth management division of our trust department, resulting in increased trust fees, continuing increase of the investment brokerage division, thereby increasing commission revenue, the continued increase in commercial and personal property and casualty insurance policies through the cross-sale to existing bank customers and the sale to new customers increasing insurance commission revenue. Non-interest expense is expected to increase to support the expansion of each division.

Description of Operations

Northeast Bancorp (the "Company") is a Maine corporation and a bank holding company registered with the Federal Reserve Bank of Boston ("FRB") under the Bank Holding Company Act of 1956. The FRB is the primary regulator of the Company, and it supervises and examines our activities. The Company also is a registered Maine financial institution holding company under Maine law and is subject to regulation and examination by the Superintendent of Maine Bureau of Financial Institutions. We conduct business from our headquarters in Lewiston, Maine and, as of September 30, 2007, we had twelve banking offices and twelve insurance offices, all located in western and south-central Maine. At September 30, 2007, we had consolidated assets of $573.7 million and consolidated stockholders' equity of $40.6 million.

The Company's principal asset is all the capital stock of Northeast Bank (the "Bank"), a Maine state-chartered universal bank. Accordingly, the Company's results of operations are primarily dependent on the results of the operations of the Bank. The Bank's 12 offices are located in Auburn, Augusta, Bethel, Brunswick, Buckfield, Falmouth, Harrison, Lewiston (2), Mechanic Falls, Portland, and South Paris, Maine. The Bank's investment brokerage division offers investment, insurance and financial planning products and services from its office in Falmouth, Maine.

The Bank's wholly owned subsidiary, Northeast Bank Insurance Group Inc., is our insurance agency. There are twelve insurance agency offices, an increase of one since the quarter ended June 30, 2007. Five agencies have been acquired since June 28, 2006: Hartford Insurance Agency of Lewiston, Maine was acquired on August 30, 2007; Russell Agency of Madison, Maine was acquired on June 28, 2007; Southern Maine Insurance Agency of Scarborough, Maine was acquired on March 30, 2007; Sturtevant and Ham, Inc. of Livermore, Maine was acquired on December 1, 2006; and Palmer Insurance of Turner, Maine was acquired on November 28, 2006. The Russell Agency was moved to our existing location in Anson, Maine following the acquisition. Our insurance agency offices are located in Anson, Auburn, Augusta, Bethel, Jackman, Lewiston, Livermore Falls, Mexico, Rangeley (its headquarters), Turner, Scarborough, and South Paris, Maine. All of our insurance agencies offer personal and commercial property and casualty insurance products. See Note 6 in our June 30, 2007 audited consolidated financial statements for more information.

Bank Strategy

The principal business of the Bank consists of attracting deposits from the general public and applying those funds to originate or acquire residential mortgage loans, commercial loans, commercial real estate loans, and a variety of consumer, indirect auto and indirect recreational vehicle loans. The Bank sells, from time to time, fixed rate residential mortgage loans into the secondary market. The Bank also invests in mortgage-backed securities, securities issued by United States government sponsored enterprises, corporate and municipal securities. The Bank's profitability depends primarily on net interest income and is affected by the level of interest rates, changes in interest rates, and by changes in the amount and composition of interest-earning assets(i.e. loans and investments) and interest-bearing liabilities(i.e. customer deposits and borrowed funds). The Bank also emphasizes the growth of non-interest sources of income from investment and insurance brokerage, trust management, and financial planning to reduce its dependency on net interest income.

Our goal is to continue modest, but profitable, growth by increasing our loan and deposit market share in our existing markets in western and south-central Maine, closely managing the yields on interest-earning assets and rates on interest-bearing liabilities, introducing new financial products and services, increasing the number of bank services sold to each household, increasing non-interest income from expanded trust services, investment and insurance brokerage services, and controlling the growth of non-interest expenses. It also is part of our business strategy to make targeted acquisitions in our current market areas from time to time when opportunities present themselves.

Results of Operations

Comparison of the three months ended September 30, 2007 and 2006

General

The Company reported consolidated net income of $430,565, or $0.18 per diluted share, for the three months ended September 30, 2007 compared with $454,667, or $0.18 per diluted share, for the three months ended September 30, 2006, a decrease of $24,102, or 5%. Net interest and dividend income decreased $522,530, or 13%, as a result of a lower net interest margin, and a decrease in earning assets. Non interest income increased $526,946, or 36%, primarily from increased gain on sale of loans, increased investment brokerage commissions, and increased insurance commissions. Noninterest expense increased $171,926, or 4%, primarily due to increased salaries and employee benefits and other noninterest expenses.

Annualized return on average equity ("ROE") and return on average assets ("ROA") were 4.17% and 0.31%, respectively, for the quarter ended September 30, 2007 as compared to 4.52% and 0.32%, respectively, for the quarter ended September 30, 2006. The decrease in the returns on average equity and average assets was primarily due to lower net income for the most recent quarter.

Net Interest and Dividend Income

Net interest and dividend income for the three months ended September 30, 2007 decreased to $3,592,847, as compared to $4,115,377 for the same period in 2006. The decrease in net interest and dividend income of $522,530, or 13%, was primarily due to a 30 basis point decrease in net interest margin, on a tax equivalent basis, and a decrease in average earning assets of $7,223,912, or 1%, for the quarter ended September 30, 2007 as compared to the quarter ended September 30, 2006. The decrease in average earning assets was primarily due to a decrease in average loans of $13,968,891, or 3%, and a decrease in average interest-bearing deposits and regulatory stock of $946,886, or 11%, partially offset by an increase in average investment securities of $7,673,865, or 9%, from the purchase of mortgage-backed securities. Average loans as a percentage of average earning assets was 81% and 82% for quarters ended September 30, 2007 and 2006, respectively. Our net interest margin, on a tax equivalent basis, was 2.75% and 3.05% for the quarters ended September 30, 2007 and 2006, respectively. Our net interest spread, on a tax equivalent basis, for the three months ended September 30, 2007 was 2.42%, a decrease of 35 basis points from 2.77% for the same period a year ago. Comparing the three months ended September 30, 2007 and 2006, the yields on earning assets increased 4 basis points compared to a 39 basis point increase in the cost of interest-bearing liabilities. The increases in our yield on earning assets and in the cost of interest-bearing liabilities reflect the competitive pressure on interest rates to attract new customers and retain existing customer relationships and a generally rising interest rate environment. We were not able to increase our net interest spread due to the volume of interest-bearing liabilities (primarily certificates of deposits) that repriced to higher rates, our slightly liability sensitive balance sheet, resulting in the cost of interest-bearing liabilities repricing more quickly then the yield of interest bearing assets, and a decreased prime rate during the quarter ended September 30, 2007 resulting in an immediate decline in the rates earned on loans with an interest rate tied to the prime rate.

The changes in net interest and dividend income, on a tax equivalent basis, are presented in the schedule below, which compares the three months ended September 30, 2007 and 2006.

	Difference Due to		
	Volume	Rate	Total
Investments	$ 80,762	$ 73,785	$ 154,547
Loans, net	(254,546)	35,619	(218,927)
FHLB & Other Deposits	(3,208)	2,814	(394)
Total Interest-earnings Assets	(176,992)	112,218	(64,774)
Deposits	(258,386)	322,308	63,922
Securities sold under repurchase Agreements	28,932	35,664	64,596
Borrowings	280,407	48,503	328,910
Total Interest-bearing Liabilities	50,953	406,475	457,428
Net Interest and Dividend Income	$ (227,945)	$ (294,257)	$ (522,202)

Rate/volume amounts which are partly attributable to rate and volume are spread proportionately between volume and rate based on the direct change attributable to rate and volume. Borrowings in the table include junior subordinated notes, FHLB borrowings, structured repurchase agreement, capital lease obligation and other borrowings. The adjustment to interest income and yield on a fully tax equivalent basis was $49,577 and $49,249 for the three months ended September 30, 2007 and 2006, respectively.

The Company's business primarily consists of the commercial banking activities of the Bank. The success of the Company is largely dependent on its ability to manage interest rate risk and, as a result, changes in interest rates, as well as fluctuations in the level of assets and liabilities, affect net interest and dividend income. This risk arises from our core banking activities: lending and deposit gathering. In addition to directly impacting net interest and dividend income, changes in interest rates can also affect the amount of loans originated and sold by the Bank, the ability of borrowers to repay adjustable or variable rate loans, the average maturity of loans, the rate of amortization of premiums and discounts paid on securities, the amount of unrealized gains and losses on securities available-for-sale and the fair value of our saleable assets and the resultant ability to realize gains. The interest sensitivity of the Bank's balance sheet has shifted to a liability sensitive position, where more liabilities than assets reprice within a twelve month repricing period, from an asset sensitive position. As a result, the Bank is generally expected to experience a decrease in its net interest margins during a period of increasing interest rates.

As of September 30, 2007 and 2006, 43% and 46%, respectively, of the Bank's loan portfolio was composed of adjustable rate loans based on a prime rate index or short-term rate indices such as the one-year U.S. Treasury bill. Interest income on these existing loans would increase if short-term interest rates increase. An increase in short-term interest rates would also increase deposit and FHLB advance rates, increasing the Company's interest expense. The impact on future net interest and dividend income from changes in market interest rates will depend on, among other things, actual rates charged on the Bank's loan portfolio, deposit and advance rates paid by the Bank and loan volume.

Provision for Loan Losses

The provision for loan losses for the three months ended September 30, 2007 was $190,283, a decrease of $110,503, or 37%, from $300,786 for the three months ended September 30, 2006. The provision was decreased due to our internal analysis of the adequacy of the allowance for loan losses. We considered: the decrease in net charge-offs of $190,283 for the three months ended September 30, 2007 compared to $190,786 for the same period in 2006; an increase in loan delinquency to 2.82% at September 30, 2007 compared to 2.42% at June 30, 2007 and 2.59% at September 30, 2006 due to the amount of loan balances past due; a decrease in non-performing loans (more than 90 days past due) at September 30, 2007 compared to June 30, 2007; and internally classified and criticized loans at September 30, 2007 that increased slightly compared to June 30, 2007. Management deemed the allowance for loan losses adequate for the risk in the loan portfolio. See Financial Condition for a discussion of the Allowance for Loan Losses and the factors impacting the provision for loan losses. The allowance as a percentage of outstanding loans increased to 1.37% at September 30, 2007 compared to 1.35% at June 30, 2007 and 1.27% at September 30, 2006.

Noninterest Income

Total noninterest income was $1,989,374 for the three months ended September 30, 2007, an increase of $526,946, or 36%, from $1,462,428 for the three months ended September 30, 2006. This increase was the combined impact of a $57,171 increase in gains on the sales of loans due to an increase in the volume of residential real estate sold, a $26,402 increase in investment commissions resulting from an increase in sales, and a $437,577 increase in insurance commission revenue due to the additional revenue contributed by insurance agency acquisitions.

Noninterest Expense

Total noninterest expense for the three months ended September 30, 2007 was $4,841,604, an increase of $171,926, or 4%, from $4,669,678 for the three months ended September 30, 2006. This increase was primarily due an $87,221, or 3%, increase in salaries and employee benefits from an increase in full-time staff for our insurance agency acquisitions, and lower deferrals of salary and benefit expenses due to a decrease in the number of loans closed partially offset by lower deferred compensation expenses and lower medical benefits costs. Occupancy expense was virtually unchanged compared to the prior year. Equipment expense decreased $18,989, or 5%, due to lower depreciation and storage expenses. Intangible amortization increased from the intangibles added from the five insurance agency acquisitions. Other noninterest expense increased $67,261, or 7%, primarily from increased professional fees for outsourcing public relations and information security, increased advertising expenses primarily from the timing of television commercials, increased provisions for off-balance sheet credit risk, increased debit card processing expenses and losses on deposit accounts and increased travel and entertainments expenses. These increases in noninterest expense were partially offset by a decrease in non-marketable securities impairment expense compared to September 30, 2006.

For the three months ended September 30, 2007, the decrease in income tax expense was primarily due to the decrease in income before income taxes as compared to the same period in 2006.

Our efficiency ratio, total non interest expense as a percentage of the sum of net interest and dividend income and non-interest income, was 87% and 84% for the three months ended September 30, 2007 and 2006, respectively. The increase in the efficiency ratio was due, in part, to the decrease in net interest and dividend income compared to the three months ended September 30, 2006, and, in part, to the increase in operating expenses during the three months ended September 30, 2007 from acquired insurance agencies.

Financial Condition

Our consolidated assets were $573,679,691 and $556,800,980 as of September 30, 2007 and June 30, 2007, respectively, an increase of $16,878,711, or 3%. This increase was primarily due to an increase of $23,177,764, or 27%, in available-for-sale investment securities, partially offset by a decrease of $4,281,842 in loans, primarily commercial loans, a decrease in loans held-for-sale of $806,875, and a decrease in cash and due from banks of $1,712,028. For the three months ended September 30, 2007, average total assets were $559,679,376, a decrease of $2,758,042, or less than 1%, from $562,437,418 for the same period in 2006. This average asset decrease was primarily attributable to a decrease in net loans.

Total stockholders' equity was $40,641,134 and $40,849,878 at September 30, 2007 and June 30, 2007, respectively, a decrease of $208,744, or less than 1%, due to dividends paid and stock repurchased partially offset by net income for the three months ended September 30, 2007 and a decrease in accumulated other comprehensive loss. Book value per outstanding share was $17.14 at September 30, 2007 and $16.68 at June 30, 2007.

Investment Activities

The available-for-sale investment portfolio was $109,525,834 as of September 30, 2007, an increase of $23,177,764, or 27%, from $86,348,070 as of June 30, 2007. This increase was due to a leveraging transaction in August, 2007 to increase net interest income by acquiring $32 million of mortgage-backed securities which were funded through a structured repurchase agreement of $30 million with an average rate of 4.45% and a spread of approximately 1.36%. To reduce the balance sheet exposure to rising interest rates, $40 million of interest rate caps were imbedded in this transaction with an at the money strike rate of 5.50% based on three month LIBOR. See note 7 for additional information.

The investment portfolio as of September 30, 2007 consisted of debt securities issued by U.S. government-sponsored enterprises and corporations, mortgage-backed securities, municipal securities and equity securities. Generally, funds retained by the Bank as a result of increases in deposits or decreases in loans, which are not immediately used by the Bank, are invested in securities held in its investment portfolio. The investment portfolio is used as a source of liquidity for the Bank. The investment portfolio is structured so that it provides for an ongoing source of funds for meeting loan and deposit demands and for reinvestment opportunities to take advantage of changes in the interest rate environment. The investment portfolio averaged $94,665,715 for the three months ended September 30, 2007 as compared to $86,991,850 for the three months ended September 30, 2006, an increase of $7,673,865, or 9%. This increase was due primarily to the leveraging transaction described above.

Our entire investment portfolio is classified as available-for-sale at September 30, 2007 and June 30, 2007, and is carried at fair value. Changes in fair value, net of applicable income taxes, are reported as a separate component of stockholders' equity. Gains and losses on the sale of securities are recognized at the time of the sale using the specific identification method. The amortized cost and fair value of availab