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 quarter ended December 31,1998

or

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

For the transition period from __________ 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.) |
| 232 Center Street, Auburn, Maine | 04210 |
| (Address of principal executive offices) | (Zip Code) |

(207) 777 - 6411

Registrant's telephone number, including area code

Not Applicable

1

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 subject to such filing requirements for the past 90 days. Yes _X_ No ___

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Shares outstanding as of February 10, 1999: 2,765,576 of common stock, $1.00 par value per share.

NORTHEAST BANCORP
Table of Contents

Item 1. Legal Proceedings

Item 2. Changes in Securities

Item 3. Defaults Upon Senior Securities

Item 4. Submission of Matters to a Vote of Security Holders

Item 5. Other Information

Item 6. Exhibits and Reports on Form 8-K

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

NORTHEAST BANCORP AND SUBSIDIARY
Consolidated Balance Sheets
(Unaudited)

| | December 31, 1998 | June 30, 1998 |
|---|---|---|
| Assets | | |
| Cash and due from bank | $ 5,092,834 | $ 6,821,574 |
| Interest bearing deposits in other banks | 593,064 | 421,392 |
| Federal Home Loan Bank overnight deposits | 13,172,000 | 4,909,000 |
| Trading account securities at market | -- | 50,000 |
| Available for sale securities | 17,372,783 | 13,608,823 |
| Federal Home Loan Bank stock | 5,680,500 | 5,680,500 |
| Loans held for sale | 949,601 | 369,500 |
| Loans | 284,313,294 | 282,030,950 |
| Less allowance for loan losses | 2,869,000 | 2,978,000 |
| Net loans | 281,444,294 | 279,052,950 |
| Bank premises and equipment, net | 4,794,612 | 4,473,885 |
| Assets acquired through foreclosure | 273,515 | 381,288 |
| Goodwill (net of accumulated amortization of $1,680,995 at 12/31/98 and $1,532,808 at 6/30/98) | 1,775,728 | 1,923,915 |
| Other assets | 5,046,060 | 4,839,767 |
| Total Assets | 336,194,991 | 322,532,594 |
| Liabilities and Shareholders' Equity | | |
| Liabilities | | |
| Deposits | $ 201,930,962 | $ 184,024,097 |
| Repurchase Agreements | 9,278,719 | 5,205,594 |
| Advances from Federal Home Loan Bank | 92,109,544 | 104,439,952 |
| Notes payable | 840,278 | 993,055 |
| Other Liabilities | 5,836,232 | 2,730,369 |
| Total Liabilities | 309,995,735 | 297,393,067 |
| Shareholders' Equity | | |
| Preferred stock, Series A | 0 | 999,988 |
| Common stock, par value $1, 2,755,076 and 2,614,285 shares issued and outstanding at 12/31/98 and 6/30/98, respectively | 2,755,076 | 2,614,285 |
| Additional paid in capital | 10,156,814 | 9,258,107 |

| | | |
|---|---|---|
| Retained earnings | 13,365,169 | 12,331,595 |
| | 26,277,059 | 25,203,975 |
| Accumulated other comprehensive income (loss) | (77,803) | (64,448) |
| Total Shareholders' Equity | 26,199,256 | 25,139,527 |
| Total Liabilities and Shareholders' Equity | $ 336,194,991 | $ 322,532,594 |

NORTHEAST BANCORP AND SUBSIDIARY
Consolidated Statements of Income
(Unaudited)

| | Three Months Ended December 31, 1998 | 1997 |
|---|---|---|
| Interest and Dividend Income | | |
| Interest on FHLB overnight deposits | $ 73,860 | $ 121,584 |
| Interest on loans & loans held for sale | 6,179,727 | 5,256,343 |
| Interest on available for sale securities | 177,051 | 437,952 |
| Dividends on Federal Home Loan Bank stock | 91,635 | 71,904 |
| Other Interest Income | 5,443 | 4,596 |
| Total Interest Income | 6,527,716 | 5,892,379 |
| Interest Expense | | |
| Deposits | 2,157,908 | 1,901,610 |
| Repurchase agreements | 86,531 | 54,618 |
| Other borrowings | 1,379,940 | 1,128,589 |
| Total Interest Expense | 3,624,379 | 3,084,817 |
| Net Interest Income | 2,903,337 | 2,807,562 |
| Provision for loan losses | 164,491 | 227,663 |
| Net Interest Income after Provision for Loan Losses | 2,738,846 | 2,579,899 |
| Other Income | | |
| Service charges | 269,536 | 237,235 |
| Net securities gains | 47,699 | 99,696 |
| Net gain on trading securities | 5,120 | 0 |
| Other | 519,115 | 405,177 |
| Total Other Income | 841,470 | 742,108 |
| Other Expenses | | |
| Salaries and employee benefits | 1,191,497 | 1,272,952 |
| Net occupancy expense | 219,399 | 221,148 |
| Equipment expense | 210,958 | 234,410 |
| Goodwill amortization | 74,094 | 74,094 |

| | | |
|---|---|---|
| Other | 789,131 | 963,019 |
| Total Other Expenses | 2,485,079 | 2,765,623 |
| Income Before Income Taxes | 1,095,237 | 556,384 |
| Income tax expense | 394,669 | 200,318 |
| Net Income | $ 700,568 | $ 356,066 |
| Earnings Per Share | | |
| Basic | $ 0.26 | $ 0.14 |
| Diluted | $ 0.25 | $ 0.13 |

NORTHEAST BANCORP AND SUBSIDIARY
Consolidated Statements of Income
(Unaudited)

| | Six Months Ended December 31, 1998 | 1997 |
|---|---|---|
| Interest and Dividend Income | | |
| Interest on FHLB overnight deposits | $ 190,094 | $ 263,677 |
| Interest on loans & loans held for sale | 12,488,988 | 10,428,625 |
| Interest on available for sale securities | 371,438 | 926,435 |
| Dividends on Federal Home Loan Bank stock | 181,838 | 141,741 |
| Other Interest Income | 10,515 | 9,377 |
| Total Interest Income | 13,242,873 | 11,769,855 |
| Interest Expense | | |
| Deposits | 4,287,652 | 3,785,093 |
| Repurchase agreements | 139,276 | 103,056 |
| Other borrowings | 2,817,018 | 2,308,883 |
| Total Interest Expense | 7,243,946 | 6,197,032 |
| Net Interest Income | 5,998,927 | 5,572,823 |
| Provision for loan losses | 369,421 | 390,163 |
| Net Interest Income after Provision for Loan Losses | 5,629,506 | 5,182,660 |
| Other Income | | |
| Service charges | 522,921 | 513,640 |
| Net securities gains | 58,490 | 207,692 |
| Net gain on trading securities | 10,732 | 1,797 |
| Other | 670,997 | 573,420 |

| | | |
|---|---|---|
| Total Other Income | 1,263,140 | 1,296,549 |
| Other Expenses | | |
| Salaries and employee benefits | 2,388,228 | 2,436,566 |
| Net occupancy expense | 354,309 | 442,534 |
| Equipment expense | 392,963 | 454,096 |
| Goodwill amortization | 148,187 | 148,187 |
| Other | 1,519,199 | 1,560,839 |
| Total Other Expenses | 4,802,886 | 5,042,222 |
| Income Before Income Taxes | 2,089,760 | 1,436,987 |
| Income tax expense | 753,155 | 510,356 |
| Net Income | $ 1,336,605 | $ 926,631 |
| Earnings Per Share | | |
| Basic | $ 0.49 | $ 0.39 |
| Diluted | $ 0.48 | $ 0.35 |

NORTHEAST BANCORP AND SUBSIDIARY
Consolidated Statements of Changes in Shareholders' Equity
Six Months Ended December 31, 1998 and 1997
(Unaudited)

| | Preferred Stock | Common Stock at $1.00 Par | Additional Paid in Capital | Retained Earnings | Accumulated Other Comprehensive Income (Loss) | Treasury Stock | Total |
|---|---|---|---|---|---|---|---|
| Balance at June 30, 1997 | $ 1,999,980 | $1,462,909 | $7,699,883 | $ 11,266,984 | $ (334,175) | $ -- | $22,095,581 |
| Net income for six months ended December 31, 1997 | -- | -- | -- | 926,631 | -- | -- | 926,631 |
| Other comprehensive income, net of tax: Adjustment of valuation reserve for securities available for sale | -- | -- | -- | -- | 195,948 | -- | 195,948 |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Comprehensive income | -- | -- | -- | -- | -- | -- | 1,122,579 |
| Cash dividends declared on common stock | -- | -- | -- | (206,875) | -- | -- | (206,875) |
| Cash dividends declared on preferred stock | -- | -- | -- | (69,999) | -- | -- | (69,999) |
| Stock Split in the form of a dividend | -- | 740,807 | -- | (741,902) | -- | -- | (1,095) |
| Common stock issued in connection with employee benefit and stock option plans | -- | 18,975 | 74,513 | -- | -- | (44,988) | 48,500 |
| Treasury Stock Purchased | -- | -- | -- | -- | -- | 44,988 | 44,988 |
| Balance December 31, 1997 | $ 1,999,980 | $2,222,691 | $7,774,396 | $ 11,174,839 | $ (138,227) | $ 0 | $23,033,679 |
| Balance at June 30, 1998 | 999,988 | 2,614,285 | 9,258,107 | 12,331,595 | (64,448) | -- | 25,139,527 |
| Net income for six months ended December 31, 1998 | -- | -- | -- | 1,336,605 | -- | -- | 1,336,605 |
| Other comprehensive income, net of tax: Adjustment of valuation reserve for securities available for sale | -- | -- | -- | -- | (13,355) | -- | (13,355) |
| Comprehensive income | -- | -- | -- | -- | -- | -- | 1,323,250 |
| Cash dividends declared on common stock | -- | -- | -- | (277,364) | -- | -- | (277,364) |
| Cash dividends declared on preferred stock | -- | -- | -- | (25,667) | -- | -- | (25,667) |
| Preferred Stock Converted to Common Stock | (999,988) | 136,362 | 863,626 | -- | -- | -- | 0 |
| Common stock issued in connection with employee benefit and stock option plans | -- | 4,429 | 35,081 | -- | -- | -- | 39,510 |
| Balance December 31, 1998 | $ 0 | $2,755,076 | $10,156,814 | $ 13,365,169 | $ (77,803) | $ 0 | $26,199,256 |

NORTHEAST BANCORP AND SUBSIDIARY
Consolidated Statements of Cash Flow
(Unaudited)

| | Six Months Ended December 31, 1998 | 1997 |
|---|---|---|
| Cash used in (provided by) operating activities | $ (338,406) | $ 654,801 |
| Cash flows from investing activities: | | |
| FHLB stock purchased | -- | (243,000) |
| Available for sale securities purchased | (8,699,888) | (14,775,583) |
| Available for sale securities matured | 2,387,746 | 1,499,614 |
| Available for sale securities sold | 6,537,024 | 23,662,251 |
| New loans, net of repayments & charge offs | (2,090,976) | (5,759,169) |
| Net capital expenditures | (672,016) | (141,207) |
| Assets acquired through foreclosure sold | 299,163 | 87,038 |
| Real estate held for investment sold | 50,000 | 68,743 |
| Net cash used in (provided by) investing activities | (2,188,947) | 4,398,687 |
| Cash flows from financing activities: | | |
| Net change in deposits | 17,906,866 | 1,439,952 |
| Net change in repurchase agreements | 4,073,125 | 638,499 |
| Dividends paid | (303,031) | (276,874) |
| Proceeds from stock issuance | 39,510 | 93,488 |
| Net decrease in advances from Federal Home Loan Bank of Boston | (12,330,408) | (7,930,746) |
| Net change in notes payable | (152,778) | (152,778) |
| Net cash provided by (used in) financing activities | 9,233,284 | (6,188,459) |
| Net increase (decrease) in cash and cash equivalents | 6,705,931 | (1,134,971) |
| Cash and cash equivalents, beginning of period | 12,151,966 | 18,774,344 |
| Cash and cash equivalents, end of period | $ 18,857,897 | $ 17,639,373 |

Cash and cash equivalents include cash on hand, amounts due from banks, interest bearing deposits and federal funds sold

Supplemental schedule of noncash investing activities:

| | | |
|---|---|---|
| Net change in valuation for unrealized market value adjustments on available for sale securities | (13,355) | 195,948 |
| Net transfer (to) from Loans to Other Real Estate Owned | 153,657 | 56,325 |
| Supplemental disclosure of cash paid during the period for: | | |
| Income taxes paid, net of refunds | 856,000 | 366,000 |
| Interest paid | 7,298,563 | 6,229,407 |

NORTHEAST BANCORP AND SUBSIDIARY
Notes to Consolidated Financial Statements
December 31, 1998

1. Basis of Presentation

The accompanying unaudited condensed and consolidated financial statements have been prepared in accordance with generally accepted accounting principles 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 generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the six month period ended December 31, 1998 are not necessarily indicative of the results that may be expected for the fiscal year ending June 30, 1999. For further information, refer to the audited consolidated financial statements and footnotes thereto for the fiscal year ended June 30, 1998 included in the Company's Annual Report on Form 10-K.

2. Reporting Comprehensive Income

In June 1997, the FASB issued SFAS No. 130, "Reporting Comprehensive Income." SFAS No. 130 establishes standards for reporting and displaying comprehensive income, which is defined as all changes to equity except investments by and distributions to stockholders. Net income is a component of comprehensive income, with all other components referred to in the aggregate as other comprehensive income. Such components of total comprehensive income for the Company are net income and net unrealized gains (losses) on securities available for sale, net of tax. The Company has adopted SFAS No. 130 effective for the quarter ended September 30, 1998.

3. Securities

Securities available for sale at cost and approximate market values are summarized below.

| | December 31, 1998 | June 30, 1998 |
|---|---|---|

| | Cost | Market Value | Cost | Market Value |
|---|---|---|---|---|
| Debt securities issued by the U.S. Treasury and other U.S. Government corporations and agencies | $ 348,167 | $ 350,730 | $ 4,696,659 | $ 4,698,266 |
| Corporate bonds | 202,429 | 205,336 | 202,952 | 203,484 |
| Mortgage-backed securities | 15,608,884 | 15,619,847 | 7,723,843 | 7,714,332 |
| Equity securities | 1,331,187 | 1,196,870 | 1,083,018 | 992,741 |
| | $17,490,667 | $17,372,783 | $13,706,472 | $13,608,823 |

| | December 31, 1998 | | June 30, 1998 | |
|---|---|---|---|---|
| | Cost | Market Value | Cost | Market Value |
| Due in one year or less | $ 248,167 | $ 248,167 | $ 347,253 | $ 347,253 |
| Due after one year through five years | 202,429 | 205,336 | 452,952 | 450,984 |
| Due after five years through ten years | 100,000 | 102,563 | 1,100,000 | 1,103,200 |
| Due after ten years | -- | -- | 2,999,406 | 3,000,313 |
| Mortgage-backed securities (including securities with interest rates ranging from 5.15% to 9.0% maturing September 2003 to December 2028) | 15,608,884 | 15,619,847 | 7,723,843 | 7,714,332 |
| Equity securities | 1,331,187 | 1,196,870 | 1,083,018 | 992,741 |
| | $17,490,667 | $17,372,783 | $13,706,472 | $13,608,823 |

## 4. Allowance for Loan Losses

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

| | Six Months Ended December 31, 1998 | 1997 |
|---|---|---|
| Balance at beginning of year | $ 2,978,000 | $ 2,741,809 |
| Add provision charged to operations | 369,421 | 390,163 |
| Recoveries on loans previously charged off | 63,954 | 90,350 |

| | | |
|---|---|---|
| | 3,411,375 | 3,222,322 |
| Less loans charged off | 542,375 | 449,322 |
| Balance at end of period | $ 2,869,000 | $ 2,773,000 |

5. Advances from Federal Home Loan Bank

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

December 31, 1998

| Principal Amounts | Interest Rates | Maturity Dates |
|---|---|---|
| $ 28,800,000 | 4.64% - 5.96% | 1999 |
| 5,000,000 | 4.85% - 6.27% | 2000 |
| 4,160,873 | 5.38% - 6.49% | 2001 |
| 5,000,000 | 5.71% | 2002 |
| 6,148,671 | 5.69% - 6.67% | 2003 |
| 9,000,000 | 5.25% - 6.65% | 2005 |
| 34,000,000 | 4.89% - 5.68% | 2008 |
| $ 92,109,544 | | |

June 30, 1998

| Principal Amounts | Interest Rates | Maturity Dates |
|---|---|---|
| $ 43,745,440 | 5.55% - 6.00% | 1999 |
| 4,000,000 | 5.88% - 6.27% | 2000 |
| 1,212,676 | 5.56% - 6.40% | 2001 |
| 1,138,627 | 6.21% - 6.49% | 2002 |
| 9,631,854 | 5.69% - 6.64% | 2003 |
| 1,711,355 | 6.36% - 6.67% | 2004 |
| 9,000,000 | 5.25% - 6.65% | 2005 |
| 34,000,000 | 4.89% - 5.68% | 2008 |
| $ 104,439,952 | | |

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

## General

This Management's Discussion and Analysis of Financial Condition and Results of Operations presents a review of the material changes in the financial condition of the Company from June 30, 1998 to December 31,1998, and the results of operations for the three and six months period ended December 31, 1998 and 1997. This discussion and analysis is intended to assist in understanding the financial condition and results of operations of the Company. Accordingly, this section should be read in conjunction with the condensed consolidated financial statements and the related notes contained herein.

Certain statements contained herein are not based on historical facts and are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, such as statements relating to financial condition and future prospects, loan loss reserve adequacy, year 2000 readiness, simulation of changes in interest rates, prospective results of operations, capital spending and financing sources, and revenue sources. 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 "may", "will", "believe", "expect", "estimate", "anticipate", "continue", or similar terms or variations on those terms, or the negative of those terms. Such forward-looking statements reflect the current view of management and are based on information currently available to them, and upon current expectations, estimates, and projections regarding the Company and its industry, management's belief with respect there to, and certain assumptions made by management. These forward-looking statements are not guarantees of future performance and are subject to risks, uncertainties, and other factors. Accordingly, actual results could differ materially from those set forth in 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.

## Description of Operations

Northeast Bancorp (the "Company"), is a unitary savings and loan holding company and is primarily regulated by the Office of Thrift Supervision ("OTS"). The Company has one wholly-owned subsidiary, Northeast Bank, FSB (the "Bank"), which has branches located in Auburn, Augusta, Bethel, Harrison, South Paris, Buckfield, Mechanic Falls, Brunswick, Richmond and Lisbon Falls, Maine.

## Financial Condition

Total consolidated assets were $336,194,991 on December 31, 1998, which represents an increase of $13,662,397 from June 30, 1998. Total net loans increased by $2,391,344, from June 30, 1998 to December 31, 1998. Cash equivalents and securities increased by $6,705,931 and $3,713,960, respectively, during the same period. Total deposits and repurchase agreements increased by $21,979,990, while Federal Home Loan Bank ("FHLB") borrowings decreased by $12,330,408 from June 30, 1998 to December 31, 1998.

The increase in cash equivalents and the decrease in total net loans from June 30, 1998 was due, in part, to the sale of approximately $6,700,000 of indirect auto loans during the December 31, 1998 quarter. The increase in deposits and repurchase agreements were utilized to support the increase in securities and to repay FHLB borrowings from June 30, 1998 to December 31, 1998.

At December 31, 1998, the carrying value of securities available for sale by the Company was $17,372,783, which is $117,883 less than the cost of the underlying securities. The difference between the carrying value and the cost of the securities was primarily attributable to the decline in the market value of equity securities from the prices at the time of purchase. Management attributes the reduction in the market value of equity securities to the decline of the stock market, which had a greater affect on the market value of the Company's investments in small cap technology stocks. Management reviews the portfolio of investments on an ongoing basis to determine if there has been an other-than-temporary decline in value. Some of the considerations management makes in the determination are market valuations of particular securities and economic analysis of the securities' sustainable market values based on the underlying companies' profitability.

Total loans increased by $2,282,344 for the six months ended December 31, 1998. The loan portfolio growth was in consumer installment and commercial loans. In the December 1998 quarter, the Bank sold approximately $6,700,000 of indirect auto loans. The Bank anticipates holding approximately $15,000,000 to $20,000,000 of indirect auto loans in its portfolio and currently holds approximately $13,000,000 as of December 31, 1998. As the Bank continues to grow the indirect auto portfolio, it is the Bank's intent to build relationships with other institutions for future sales of indirect auto loans. In the September 1998 quarter, the Bank purchased approximately $5,900,000 of 1-4 family mortgages. The purchase consisted of 1-4 family fixed rate mortgages secured by property located primarily in the State of New York. The continued expansion into new markets diversifies the credit risk and the potential economic risks of the credits held in the Bank's purchased loan portfolio, such that the portfolio is not effected solely by the local State of Maine economy. The Bank's local market, as well as the secondary market, continues to be very competitive for loan origination volume. The local competitive environment and customer response to favorable secondary market rates have affected the Bank's ability to increase the loan portfolio. In an effort to increase loan volume, the Bank's offering rates for its loan products have been reduced to compete in the various markets. The Bank will experience some margin compression due to decreased loan rates.

The loan portfolio contains elements of credit and interest rate risk. The Bank primarily lends within its local market areas, which management believes helps them to better evaluate credit risk. As the Bank expands its purchase of loans in other states, management researches the strength of the economy in the respective state and underwrites every loan before purchase. These steps are taken to better evaluate and minimize the credit risk of out-of-state purchases. The Bank also maintains a well collateralized position in real estate mortgages.

At December 31, 1998, residential real estate mortgages made up 60% of the total loan portfolio, of which 48% of the residential loans are variable rate products, as compared to 62% and 59%, respectively, at December 31, 1997. Although the Bank has purchased fixed rate loans, it is management's intent, where market opportunities arise, to increase the volume in variable rate residential loans to reduce the interest rate risk in this area.

At December 31, 1998, 18% of the Bank's total loan portfolio balance is commercial real estate mortgages. Commercial real estate loans have minimal interest rate risk as 88% of the portfolio consists of variable rate products. At December 31, 1997, commercial real estate mortgages made up 21% of the total loan portfolio, of which 89% of the commercial real estate loans were variable rate products. The Bank tries to mitigate credit risk by lending in its local market area as well as maintaining a well collateralized position in real estate.

Commercial loans make up 10% of the total loan portfolio, of which 53% are variable rate instruments at December 31, 1998. At December 31, 1997 commercial loans made up 10% of the total loan portfolio, of which 70% were variable rate instruments The credit loss exposure on commercial loans is highly dependent on the cash flow of the customer's business. The Bank mitigates losses by strictly adhering to the Company's underwriting and credit policies.

Consumer and other loans make up 12% of the loan portfolio as of December 31, 1998 as compared to 7% at December 31, 1997. Since these loans are primarily fixed rate products, they have interest rate risk when market rates increase. These loans also have credit risk with minimal security. The increase in consumer loans was primarily due to the volume generated from the automobile dealer finance department. This department underwrites all the automobile dealer finance loans to protect credit quality. The Bank primarily pays a nominal one time origination fee on the loans. The fees are deferred and amortized over the life of the loans as a yield adjustment. Management attempts to mitigate credit and interest rate risk by keeping the products offered short-term, receiving a rate of return commensurate with the risk, and lending to individuals in the Bank's known market areas.

The Bank's allowance for loan losses was $2,869,000 as of December 31, 1998 versus $2,978,000 as of June 30, 1998, representing 1.01% and 1.06% of total loans, respectively. The Bank had non-performing loans totaling $1,594,000 at December 30, 1998 compared to $2,248,000 at June 30, 1998. Non-performing loans represented 0.47% and 0.70% of total assets at December 31, 1998 and June 30, 1998, respectively. The Bank's allowance for loan losses was equal to 180% and 132% of the total non-performing loans at December 31, 1998 and June 30, 1998, respectively. At December 31, 1998, the Bank had approximately $614,000 of loans classified substandard, exclusive of the non-performing loans stated above, that could potentially become non-performing due to delinquencies or marginal cash flows. These substandard loans increased by $514,000 when compared to the $100,000 at June 30, 1998. The increase was attributed to management downgrading certain loans during its internal review process.

The following table represents the Bank's non-performing loans as of December 31, 1998 and June 30, 1998, respectively:

| Description | December 31, 1998 | June 30, 1998 |
| --- | --- | --- |

| | | |
|---|---|---|
| 1-4 Family Mortgages | $ 972,000 | $ 783,000 |
| Commercial Mortgages | 478,000 | 956,000 |
| Commercial Loans | 22,000 | 509,000 |
| Consumer Installment | 122,000 | 0 |
| Total non-performing | $ 1,594,000 | $ 2,248,000 |

The following table reflects the quarterly trend of total delinquencies 30 days or more past due, including non-performing loans, for the Bank as a percentage of total loans:

| 03-31-98 | 06-30-98 | 09-30-98 | 12-31-98 |
|---|---|---|---|
| 1.44% | 1.09% | 0.89% | 1.27% |

At December 31, 1998, loans classified as non-performing included approximately $375,000 of loan balances that are current and paying as agreed, but which the Bank maintains as non-performing until the borrower has demonstrated a sustainable period of performance. Excluding these loans, the Bank's total delinquencies 30 days or more past due, as a percentage of total loans, would be 1.14% as of December 31, 1998. Based on reviewing the credit risk and collateral of delinquent, non-performing and classified loans, management considers the allowance for loan losses to be adequate.

On a regular and ongoing basis, management evaluates the adequacy of the allowance for loan losses. The process to evaluate the allowance involves a high degree of management judgement. The methods employed to evaluate the allowance for loan losses are quantitative in nature and consider such factors as the loan mix, the level of non-performing loans, delinquency trends, past charge-off history, loan reviews and classifications, collateral, and the current economic climate.

While management uses its best judgement in recognizing loan losses in light of available information, there can be no assurance that the Company will not have to increase its provision for loan losses in the future as a result of changing economic conditions, adverse markets for real estate or other factors. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Bank's allowance for loan losses. Such agencies may require the Bank to recognize additions to the allowance for loan losses based on their judgements about information available to them at the time of their examination. The Bank's most recent examination by the OTS was on November 30, 1998. At the time of the exam the regulators proposed no additions to the allowance for loan losses.

The bank's premises and equipment increased by $320,727 from June 30, 1998 to December 31, 1998. The increase was due to the purchase and replacement of the Bank's mainframe and software.

The Bank's other liabilities was $5,836,232 as of December 31, 1998, which was an increase of $3,105,863 when compared to June 30, 1998. The increase was due to an amount due to the broker for the purchase of available for sale securities.

## Capital Resources and Liquidity

Cash provided by operating activities in the consolidated statements of cash flow decreased by $993,207 from December 31, 1997 to December 31, 1998 as a result of reduction in other liabilities due to transaction timing differences.

The Bank continues to attract new local deposit relationships. The Bank utilizes, as alternative sources of funds, brokered certificate of deposits ("C.D.s") when national deposit interest rates are less than the interest rates on local market deposits. Brokered C.D.s are also used to supplement the growth in earning assets. Brokered C.D.s carry the same risk as local deposit C.D.s, in that both are interest rate sensitive with respect to the Bank's ability to retain the funds. The Bank also utilizes FHLB advances, as alternative sources of funds, when the interest rates of the advances are less than market deposit interest rates. FHLB advances are also used to fund short-term liquidity demands.

Total deposits were $201,930,962 and securities sold under repurchase agreements were $9,278,719 as of December 31, 1998. These amounts represent an increase of $17,906,866 and $4,073,125, respectively, compared to June 30, 1998. The increase in deposits was primarily due to the $10,000,000 increase in NOW demand deposits and a $9,000,000 increase in time deposits. The increase in NOW deposits was attributable to the development of a demand account where the interest rate increases as deposit balances increase. Brokered deposits represented $8,804,744 of the total deposits at December 31, 1998, which increased by $1,230,034 compared to the $7,574,710 balance as of June 30, 1998. Cross selling strategies are employed by the Bank to develop deposit growth. Even though deposit interest rates have remained competitive, the rates of return are much higher with other financial instruments such as mutual funds and annuities. Like other companies in the banking industry, the Bank will be challenged to maintain and or increase its core deposits.

Total advances from the FHLB were $92,109,544 as of December 31, 1998, a decrease of $12,330,408 compared to June 30, 1998. The cash received from the increase in the Bank's deposits was utilized to repay FHLB advances. The Bank has unused borrowing capacity from the FHLB through its advances program. The Bank's current advance availability, subject to the satisfaction of certain conditions, is approximately $35,000,000 over and above the December 31, 1998 advances. Mortgages, free of liens, pledges and encumbrances are required to be pledged to secure FHLB advances. The Bank's ability to access principal sources of funds is immediate and with the borrowing capacity at the Federal Home Loan Bank, the normal growth in bank deposits and repurchase agreements and the immediate availability of the Bank's cash equivalents as well as securities available for sale, management believes that the Company's available liquidity resources are sufficient to support the Company's needs.

Total equity of the Company was $26,199,256 as of December 31, 1998 versus $25,139,527 at June 30, 1998. Book value per common share was $9.51 as of December 31, 1998 versus $9.23 at June 30, 1998. The total equity to total assets ratio of the Company was 7.79% as of December 31, and June 30, 1998.

In November of 1998 Square Lake Holding Corporation converted its Series A preferred stock into 136,362 shares of common stock. Square Lake Holding Corporation is a Maine corporation and a subsidiary of a Canadian corporation of which Ronald Goguen is a 95% shareholder and director. Mr. Goguen, also is a director, and, through the ownership of his affiliates, a principal shareholder of the Company.

The Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA"), contains various provisions intended to capitalize the Bank Insurance Fund ("BIF") and also affects a number of regulatory reforms that impact all insured depository institutions, regardless of the insurance fund in which they participate. Among other things, FDICIA grants the OTS broader regulatory authority to take prompt corrective action against insured institutions that do not meet capital requirements, including placing undercapitalized institutions into conservatorship or receivership. FDICIA also grants the OTS broader regulatory authority to take corrective action against insured institutions that are otherwise operating in an unsafe and unsound manner.

FDICIA defines specific capital categories based on an institution's capital ratios. The OTS has issued regulations requiring a minimum regulatory tangible capital equal to 1.5% of adjusted total assets, core capital of 3.0%, leverage capital of 4.0% and a risk-based capital standard of 8.0%. The prompt corrective action regulations define specific capital categories based on an institution's capital ratios. The capital categories, in declining order, are "well capitalized", "adequately capitalized", "undercapitalized", "significantly undercapitalized", and "critically undercapitalized". As of December 31,1998, the most recent notification from the OTS categorized the Bank as well capitalized. There are no conditions or events since that notification that management believes has changed the institution's category.

At December 31, 1998, the Bank's regulatory capital was in compliance with regulatory capital requirements as follows:

| | Actual | | For Capital Adequacy Purposes | | To Be "Well Capitalized" Under Prompt Corrective Action Provisions | |
|---|---|---|---|---|---|---|
| | Amount | Ratio | Amount | Ratio | Amount | Ratio |
| (Dollars in Thousands) | | | | | | |
| As of December 31, 1998: | | | | | | |
| Tier 1 (Core) capital (to risk weighted assets) | $ 24,213 | 10.91% | $ 8,880 | 4.00% | $ 13,320 | 6.00% |
| Tier 1 (Core) capital (to total assets) | $ 24,213 | 7.24% | $ 13,373 | 4.00% | $ 16,716 | 5.00% |
| Total Capital (to risk weighted assets) | $ 25,791 | 11.62% | $ 17,760 | 8.00% | $ 22,220 | 10.00% |

Results of Operations

Net income for the quarter ended December 31, 1998 was $700,568 or basic earnings per share of $0.26 and diluted earnings per share of $0.25. This compares to earnings of $356,066 or basic earnings per share of $0.14 and diluted earnings per share of $0.13 for the quarter ended December 31, 1997. Net income for the six months ended December 31, 1998 was $1,336,605 versus $926,631 for the period ended December 31, 1997. Basic earnings per share were $.49 and diluted earnings per share were $.48 for the six months ended December 31, 1998 versus basic earnings per share of $.39 and diluted earnings per share of $.35 for the period ended December 31, 1997.

The Company completed the acquisition of Cushnoc in the quarter ended December 31, 1997. The one-time costs associated with the acquisition totaled approximately $283,000 after tax of which $276,000 after tax was recognized in the quarter ended December 31, 1997. The Company's net operating income, before the aforementioned one-time charge, was $631,665, basic earnings per share were $.27 and diluted earnings per share were $.23 for the three months ended December 31, 1997, and $1,209,390, basic earnings per share were $.51 and diluted earnings per share were $.45, for the six months ended December 31, 1997.

On September 30, 1998, the Company adopted FASB Statement No. 130, "Reporting Comprehensive Income". Comparative financial information in the Statements of Changes in Shareholders' Equity for earlier periods have been reclassified in accordance with the requirement of Statement No. 130.

The Company's net interest income was $5,998,927 for the six months ended December 30, 1998, versus $5,572,823 for the six months ended December 31, 1997, an increase of $426,104. Total interest income increased $1,473,018 during the six months ended December 31, 1998 compared to the six months ended December 31, 1997, resulting primarily from an increase in the volume of loans offset in part by a decrease in rates. The increase in total interest expense of $1,046,914 for the six months ended December 31, 1998 resulted primarily from the increased volume of deposits and borrowings.

The changes in net interest income are presented in the schedule below.

Northeast Bancorp
Rate/Volume Analysis for the six months ended
December 31, 1998 versus December 31, 1997

| | Difference Due to | | |
|---|---|---|---|
| | Volume | Rate | Total |
| Investments | $ (459,709) | $ (54,705) | $ (514,414) |
| Loans | 2,762,863 | (702,500) | 2,060,363 |
| FHLB & Other Deposits | (70,498) | (2,433) | (72,931) |
| Total | 2,232,656 | (759,638) | 1,473,018 |
| Deposits | 378,836 | 123,723 | 502,559 |
| Repurchase Agreements | 35,604 | 616 | 36,220 |

| | | | |
|---|---|---|---|
| Borrowings | 597,075 | (88,940) | 508,135 |
| Total | 1,011,515 | 35,399 | 1,046,914 |
| Net Interest Income | $1,221,141 | $ (795,037) | $ 426,104 |

Rate/Volume amounts spread proportionately between volume and rate.

The majority of the Company's income is generated from the Bank. Management believes that the Bank is slightly asset sensitive based on its own internal analysis which categorizes its core deposits as long term liabilities which are then matched to long term assets. As a result, the Bank will generally experience a contraction in its net interest margins during a period of falling rates. Management believes that the maintenance of a slight asset sensitive position is appropriate since historically interest rates tend to rise faster than they decline.

Approximately 21% of the Bank's loan portfolio is comprised of floating rate loans based on a prime rate index. Interest income on these existing loans will increase as the prime rate increases, as well as on approximately 29% of other loans in the Bank's portfolio that are based on short-term rate indices such as the one-year treasury bill. An increase in short-term interest rates will also increase deposit and FHLB advance rates, increasing the Bank's interest expense. Although the Bank has experienced some net interest margin compression, the impact on net interest income 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. The net interest margin compression at the Bank has been primarily due to the decrease in loan rates. Loan yields have decreased due to the effect of the Federal Reserve easing the prime lending rate in September and October of 1998 as well as loans within the Bank refinancing to lower current market rates. As of December 31, 1998 the Bank's net loan yields have decreased by 11 basis points when compared to net loan yields at September 30,1998.

Total non-interest income was $841,470 and $1,263,140 for the three and six months ended December 31, 1998 versus $742,108 and $1,296,549 for the three and six months ended December 31, 1997. Service fee income was $269,536 and $522,921 for the three and six months ended December 31, 1998 versus $237,235 and $513,640 for the three and six months ended December 31, 1997. The $32,301 and $9,281 service fee increase for the three and six months ended December 31, 1998, respectively, was primarily due to an increase in loan servicing and deposit fee income. Gains from available for sale securities were $47,699 and $58,490 for the three and six months ended December 31, 1998 versus $99,696 and $207,692 for the three and six months ended December 31, 1997. The Company sold a larger volume of its available for sale securities during the three and six month period ended December 31, 1997, taking advantage of the fluctuation in market prices in the mortgage-backed security portfolio.

Other income was $519,115 and $670,997 for the three and six months ended December 31, 1998, which was an increase of $113,938 and $97,577 when compared to other income of $405,177 and $573,420 for the three and six months ended December 31, 1997, respectively. The increase in other income in the three and six months ended December 31,1998, was primarily due to gains from 1-4 family mortgage and indirect auto loan sales.

Total non-interest expense for the Company was $2,485,079 and $4,802,886 for the three and six months ended December 31, 1998, which was a decrease of $280,544 and $239,336, respectively, when compared to total non-interest expense of $2,765,623 and $5,042,222 for the three and six months ended December 31, 1997. Total non-interest expense for the Company was higher for the three and six month period ended December 31, 1997 primarily due to acquisition costs associated with Cushnoc Bank.

## Impact of Inflation

The consolidated financial statements and related notes herein have been presented in terms of historic dollars without considering changes in the relative purchasing power of money over time due to inflation. Unlike industrial companies, substantially all of the assets and virtually all of the liabilities of the Company are monetary in nature. As a result, interest rates have a more significant impact on the Company's performance than the general level of inflation. Over short periods of time, interest rates may not necessarily move in the same direction or in the same magnitude as inflation.

## Year 2000

The Company is currently addressing the Year 2000 issue. Many existing computer programs and hardware configurations use only two digits to identify a year in the date field. Since these programs did not take into consideration the upcoming change in the century, many computer applications could create erroneous results by the year 2000 if not corrected. The Year 2000 issue will affect this Company and it will affect virtually all companies and organizations, including the Company's borrowers. The Company has organized a Year 2000 committee to research, develop and implement a plan that will correct this issue before the year 2000. The OTS, which primarily regulates thrifts, savings and loan associations, and savings and loan holding companies, has issued a formal regulation and comprehensive plan concerning the Year 2000 issue for such financial institutions. The Company has adopted the regulatory comprehensive plan which has the following phases:

### Awareness Phase

This phase consists of defining the Year 2000 problem; developing the resources necessary to perform compliance work, establishing a Year 2000 program committee and developing an overall strategy that encompasses in-house systems, service bureaus for systems that are outsourced, vendors, auditors, customers, and suppliers (including correspondents). This phase has been completed by the Company's committee.

### Assessment Phase

This phase consists of assessing the size and complexity of the problem and detailing the magnitude of the effort necessary to address the Year 2000 issue. This phase must identify all hardware, software, networks, automated teller machines, other various processing platforms, and customer and vendor interdependencies affected by the Year 2000 date change. The assessment must go beyond information systems and include environmental systems that are dependent on embedded microchips, such as security systems, elevators and vaults. During this phase management also must evaluate the Year 2000 effect on other strategic business initiatives. The assessment should consider the potential effect that mergers and acquisitions, major system development, corporate alliances, and system interdependencies will have on existing systems and/or the potential Year 2000 issues that may arise from acquired systems. The financial institution or vendor should also identify resource needs, establish time frames and sequencing of Year 2000 efforts. Resource needs include appropriately skilled personnel, contractors, vendor support, budget allocations, and hardware capacity. This phase should clearly identify corporate accountability throughout the project, and policies should define reporting, monitoring, and notification requirements. Finally, contingency plans should be developed to cover unforeseen obstacles during the renovation and validation phases and include plans to deal with lesser priority systems that would be fixed later in the renovation phase.

The assessment phase has been materially completed, but is considered an ongoing phase for the Company. The Company is in the process of developing its contingency plan and anticipates its completion by June 30, 1999. The Company has instituted a comprehensive plan to communicate with all its borrowers that the Company considers to be at risk concerning the Year 2000 issue. The Company considers this plan necessary to mitigate the risk associated with borrowers not having the ability to make loan payments due to a Year 2000 issue. The company has currently estimated the following costs associated with the Year 2000 issue, (i) computer hardware replacement $130,000, (ii) software replacement $72,000, (iii) testing and administrative costs $84,000, and (iv) potential contingency costs $60,000. As of December 31, 1998, the Company has incurred approximately $37,333 of capitalized purchases and $84,600 of cumulative Year 2000 expenses. These costs are under continuous review and will be revised as needed. There can be no assurance that actual costs will not exceed the Company's estimates. During the quarter ended December 31, 1998, the Company replaced its computer mainframe and software as planned to accommodate the growth of the Company through merger and acquisitions. The previous mainframe and software had been fully depreciated through the normal course of its depreciable life and the costs associated with the replacement of these items was in the Company's general business plan for fiscal 1999. The anticipated Year 2000 hardware and software costs indicated above are in addition to the Company's costs associated with the replacement of the mainframe and software.

Renovation Phase

This phase includes code enhancements, hardware and software upgrades, system replacements, vendor certification, and other associated changes. Work should be prioritized based on information gathered during the assessment phase. For institutions relying on outside services or third-party software providers, ongoing discussions and monitoring of vendor progress are necessary. The Company has limited out-side services and vendors. Each servicer and vendor has been contacted and has or will provide information to the Company concerning their efforts to comply with the Year 2000 issue. The Company has materially completed this phase and is in the process of converting the data communications network. The Company anticipates completion of this phase by March 31, 1999. However, there can be no assurance that these services or vendors will become Year 2000 compliant in a timely manner.

Validation Phase

Testing is a multifaceted process that is critical to the Year 2000 project and inherent in each phase of the project management plan. This process includes the testing of incremental changes to hardware and software components. In addition to testing upgraded components, connections with other systems must be verified, and all changes should be accepted by internal and external users. Management will establish controls to assure the effective and timely completion of all hardware and software testing prior to final implementation. As with the renovation phase, the Company will be in ongoing discussions with their vendors on the success of their validation efforts. The Company has completed the testing all of its critical systems and will implement the data communications testing after conversion. The Company anticipates completion of this phase by March 31, 1999.

Implementation Phase

In this phase, systems should be certified as Year 2000 compliant and be accepted by the business users. For any system failing certification, the business effect must be assessed clearly and the organization's Year 2000 contingency plans should be implemented. Any potentially non-compliant mission-critical system should be brought to the attention of executive management immediately for resolution. In addition, this phase must ensure that any new systems or subsequent changes to verified systems are compliant with Year 2000 requirements. The Company anticipates completion of this phase by June 30, 1999.

In summary, the Company recognizes the Year 2000 as a global issue with potentially catastrophic results if not addressed. The Company has and will continue to undertake all the necessary steps to protect itself and its customers concerning the Year 2000 issue. Management is confident that all the instituted phases will be completed and in place prior to the year 2000. However, failure to meet the Year 2000 deadlines could have a material adverse effect on the Company.

Item 3. Quantitative and Qualitative Disclosure about Market Risk

There have been no material changes in the Company's market risk from June 30, 1998. For information regarding the Company's market risk, refer to the Company's Annual Report on Form 10-K dated as of June 30, 1998.

Part II - OTHER INFORMATION

Item 1. Legal Proceedings

None.

Item 2. Changes in Securities

None.

Item 3. Defaults Upon Senior Securities

None.

## Item 4. Submission of Matters to a Vote of Security Holders

### SUMMARY OF VOTING AT 11/10/98 ANNUAL SHAREHOLDERS' MEETING

At the Annual Meeting of Shareholders held in Auburn, Maine on November 10, 1998, the following matters were submitted to a vote of, and approved by, the Company's shareholders, each such proposal receiving the vote of the Company's outstanding common and preferred shares, voting as one class, as follows:

Proposal 1 - Election of Directors:

| | Votes For | Votes Withheld |
|---|---|---|
| John W. Trinward, D.M.D. | 2,082,411 | 61,350 |
| John B. Bouchard | 2,081,411 | 62,350 |
| A. William Cannan | 2,082,411 | 61,350 |
| Ronald J. Goguen | 2,079,411 | 64,350 |
| Judith W. Hayes | 2,082,411 | 61,350 |
| John Rosmarin | 2,081,411 | 62,350 |
| John Schiavi | 2,077,061 | 66,700 |
| Stephen W. Wight | 2,075,911 | 67,850 |
| Dennis A. Wilson | 2,082,411 | 61,350 |

Proposal 2 - Approval of increased Number of Shares of Authorized Common Stock. Proposal to approve and adopt an amendment to the Articles of Incorporation of the Company to increase the number of its shares of authorized common stock to 15 million shares.

| Votes For | Votes Against | Votes Abstain | Non-Vote |
|---|---|---|---|
| 1,971,287 | 154,222 | 15,625 | 2,627 |

Proposal 3 - Ratification of Appointment of Auditors. Proposal to ratify the appointment of Baker, Newman & Noyes, Limited Liability Company, as the Company's auditors for the 1999 fiscal year.

| Votes For | Votes Against | Votes Abstain |
|---|---|---|
| 2,132,156 | 3,640 | 7,965 |

Item 5. Other Information

None.

Item 6. Exhibits and Reports on Form 8 - K

(a) Exhibits

3.1 Conformed Articles of Incorporation of Northeast Bancorp as amended November 10, 1998.

11 Statement regarding computation of per share earnings.

27 Financial data schedule

(b) Reports on Form 8 - K

No reports on Form 8-K have been filed during the quarter ended December 31, 1998.

SIGNATURES

Pursuant to the requirements of the Securities Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: February 10, 1999 NORTHEAST BANCORP

By: /s/ James D. Delamater

James D. Delamater
President and CEO

By: /s/ Richard Wyman

Richard Wyman
Chief Financial Officer

NORTHEAST BANCORP
Index to Exhibits

| EXHIBIT NUMBER | DESCRIPTION |
|---|---|
| 3.1 | Conformed Articles of Incorporation of Northeast Bancorp as amended November 10, 1998. |
| 11 | Statement regarding computation of per share earnings |

27 Financial data schedule

NORTHEAST BANCORP
ARTICLES OF INCORPORATION

FIRST: The name of the corporation is NORTHEAST BANCORP.

SECOND: The name of its Clerk, who must be a Maine resident and the address of its registered office shall be:
Mary Ann Brown
232 Center Street, Auburn, Maine 04212

THIRD: The number of directors constituting the initial board of directors of the corporation is nine, as follows:
Gordon M. Gillies, 3 Broad St, Bethel, Maine 04217
E. Louise Lincoln, PO Box 527, Bethel, Maine 04217
John W. Trinward, 8 Vernon St, Bethel, Maine 04217
Stephen W. Wight, RFD 2, Box 1688, Bethel, Maine 04217
Edmond J. Vachon, Paradise St, Bethel, Maine 04217
Ronald C. Kendall, PO Box 1, Bethel, Maine 04217
Norris T. Brown, Clark St, Bethel, Maine 04217
Philip C. Jackson, 12 Smith St, Bethel, Maine 04217
James D. Delamater, Route 121, Oxford, Maine 04270

FOURTH: The board of directors is authorized to increase or decrease the number of directors. The minimum number shall be nine directors and the maximum number shall be twelve directors.

FIFTH: SHARES - There shall be 15,000,000 authorized shares of $1.00 par value Common Stock, which may be issued by the Corporation from time to time by vote of the Board without the approval of the holders of the Common Stock. Upon payment of lawful consideration, such shares shall be deemed fully paid and nonassessable. Except as the Board shall have otherwise specified or except as otherwise provided by law, voting power shall be vested exclusively in the Common Stock. The holders of the Common Stock shall be entitled to one vote for each share of Common Stock owned. Dividends, as declared by the Board out of lawfully available funds, shall be payable on the Common Stock subject to any rights or preferences of the Preferred Stock.

There shall be 1,000,000 authorized shares of $1.00 par value Preferred Stock which may be issued from time to time in one or more series as may be determined by the Board of Directors of the Corporation. Each series of Preferred is to be distinctly designated to distinguish the shares in the series from the shares of all other series and classes. The relative rights and preferences of the Preferred Stock and the variations of rights and preferences between different series of Preferred Stock may be fixed



and determined by the Board of Directors by resolution or resolutions adopted prior to the issuance of any shares of a particular series of Preferred Stock. All shares of Preferred shall be identical except as to the following relative rights and preferences, as to which there may be variations between different series:

a. The rate of dividend;
b. Whether shares may be redeemed and, if so, the redemption price and the terms and conditions of redemption;
c. The amount payable upon shares in event of voluntary and involuntary liquidation;
d. Sinking fund provisions, if any, for the redemption or purchase of shares;
e. The terms and conditions, if any, on which shares may be converted; or
f. Voting rights, if any.

Upon any liquidation, dissolution or winding up of the affairs of the Corporation, whether voluntary or involuntary, holders of Common Stock are entitled to receive pro rata the remaining assets of the Corporation after the holders of Preferred Stock have been paid in full any sums to which they may be entitled.

There shall be no cumulative voting for Directors or otherwise.

SUMMARY

The aggregate par value of all authorized shares (of all classes) having a par value is $16,000,000. The total number of authorized shares (of all classes) without par value is zero shares.

SIXTH: Meetings of the shareholders may be held outside the State of Maine.

SEVENTH: There are no preemptive rights.

EIGHTH: INTERNAL AFFAIRS OF THE CORPORATION

Section 1.
- ----------

(a) Number, Qualifications and Term of Office.

Subject to the provisions hereof relating to the initial Board, the number of directors of the corporation shall be no less than 9 and no more than 12. The exact number of Directors within the minimum and maximum limitations specified in the preceding sentence shall be fixed from time to time by the Board pursuant to a resolution adopted by the majority of the entire Board. No decrease in the number of directors constituting the Board shall shorten the term of any incumbent director. Each Director elected to succeed those directors whose terms expire at or after the 1997 annual meeting of Shareholders shall be elected to serve until the next annual meeting of shareholders and until his or her successor is elected and qualified. Directors need not be Shareholders or residents of the State of Maine.

(b) Vacancies.

Any vacancy in the Board caused by death, resignation, retirement, disqualification, removal or other cause, shall be filled by a majority vote of the remaining Directors, though less than a quorum. A Director so chosen shall hold office for the unexpired term of their predecessors in office. Any Directorship to be filled by reason of an increase in the authorized number of directors may be filled by the Board for a term of office continuing only until the next election of Directors by Shareholders.

(c) Removal of Directors.

At any meeting of Shareholders called expressly for the purpose, any Director may be removed from office by the affirmative vote of the holders of seventy-five percent (75%) of the shares entitled to vote or if removal is for cause, then by a majority of the shares then entitled to vote. For "cause" shall mean a final adjudication by a court of competent jurisdiction that the Director (i) is liable for negligence or misconduct in the performance of his duty, (ii) guilty of a felony conviction, or (iii) has failed to act or has acted in a manner which is in derogation of the Director's duties.

(d) Nomination of Directors.

In addition to the right of the Board to make nominations for the election of Directors, nominations for the election of Directors may be made by any Shareholder entitled to vote for the election of Directors if that Shareholder complies with all of the following provisions:

a. Advance notice of such proposed nomination shall be received by the Secretary of the Corporation not less than thirty (30) days nor more than sixty (60) days prior to any meeting of the Shareholders called for the election of the Directors; provided, however, that if fewer than fourteen (14) days' notice of the meeting is given to Shareholders, such written notice of a proposed nomination shall be received not later than the close of the tenth day following the day on which the notice of the meeting was mailed to Shareholders.

b. Each notice shall set forth (i) the name, age, business address and, if known, residence address of each nominee proposed in such notice, (ii) the principal occupation or employment of each such nominee; and (iii) the number of shares of stock of the Corporation which are beneficially owned by each such nominee. In addition, the Shareholder making such nomination shall promptly provide any other information reasonably requested by the Corporation.

c. The nomination made by a Shareholder may only be made in a meeting of the Shareholders of the Corporation called for the election of Directors at which such Shareholder is present in person or by proxy, and can only be made by a Shareholder who has complied with the notice provisions of (a) and (b) above.

d. The Chairman of the meeting may in his discretion determine and declare to the meeting that a nomination was not made in accordance with the foregoing procedures, and if he should so determine, he shall so declare to the meeting and the defective nomination shall be disregarded.

Section 2. Voting for Business Combinations.

(a) Neither the Corporation nor any subsidiary of which the Corporation owns at least a majority of the equity securities ordinarily entitled to vote for the election of Directors ("Subsidiary"), shall be a party to any of the transactions specified herein (a "Business Combination") or enter into any agreement providing for any Business Combination unless the conditions specified in (b), (c) and (d) below shall have been satisfied:

(i) any merger or consolidation (whether in a single transaction or a series of related transactions) other than a merger or consolidation of the Corporation and any of its subsidiaries or a merger or consolidation of any subsidiaries of the Corporation; or

(ii) any sale, lease, exchange, transfer or distribution of all or substantially all or a substantial portion of the property or assets of the Corporation or any of its subsidiaries, including its goodwill; or

(iii) the issuance of any securities, or of any rights warrants or options to acquire any securities of the Corporation or any of its subsidiaries, to any Shareholders other than by stock dividend declared and paid to all Shareholders of the Corporation or pursuant to an employee stock ownership plan or an employee stock option plan established by the Corporation; or

(iv) any reclassification of the stock of the Corporation or any of its subsidiaries or any recapitalization or other transaction (other than a redemption of stock) which has the effect, directly or indirectly, of increasing the proportionate share of stock of the Corporation or any of its subsidiaries held by any person; or

(v) the dissolution of the Corporation or any subsidiary thereof or any partial or complete liquidation of the Corporation or any subsidiary thereof.

(b) The vote of the holders of at least eighty percent (80%) of the outstanding shares entitled to vote for the election of Directors shall be required to approve or authorize any Business Combination to which the Corporation or any Subsidiary is party unless the aggregate of the cash and fair market value of the consideration to be paid to all the holders of the Common Stock of the Corporation in connection with the Business Combination (when adjusted for stock splits, stock dividends, reclassification of shares or otherwise) shall be equal to the highest price per share paid by the other party or parties to the Business Combination (the "Acquiring Party") in acquiring any of the Corporation's Common Stock; provided however, that the consideration to be paid to the holders of the Common Stock of the Corporation shall be in the same form as that paid by the Acquiring Party in acquiring the shares of the Common

Stock held by it except to the extent that any Stockholder of the Corporation shall otherwise agree.

(c) Subject to the provisions in (b) above, the vote of the holders of at least seventy-five percent (75%) of the outstanding shares entitled to vote for the election of Directors shall be required to approve or authorize any Business Combination to which the Corporation or any Subsidiary is a party unless the Business Combination shall have been approved by at least two-thirds (2/3) of the Directors of the Corporation who are not affiliated with, or Shareholders of, the Acquiring Party.

In connection with the exercise of its judgment in determining what is in the best interests of the Corporation and of the Shareholders, when evaluating a Business Combination or a proposal by another person or persons to make a Business Combination or a tender or exchange offer, the Board may, in addition to considering the adequacy of the amount to be paid in connection with any such transaction, consider all of the following factors and other factors which it deems relevant: (i) the social and economic effects of the transaction on the Corporation and its subsidiaries, employees, depositors, loan and other customers, creditors and other elements of the communities in which the Corporation and its subsidiaries operate or are located; (ii) the business and financial condition and earnings prospects of the acquiring person or persons, including but not limited to debt service and other existing financial obligations, financial obligations to be incurred in connection with the acquisition, and other likely financial obligations of the acquiring person or persons, and the possible effect of such conditions upon the Corporation and its subsidiaries and the other elements of the communities in which the Corporation and its subsidiaries operate or are located; and (iii) the competence, experience and integrity of the acquiring person or persons and its or their management.

(d) In the event that all of the conditions set forth in (b) and (c) above are met, the Corporation or any Subsidiary may enter into any Business Combination under the terms and conditions specified in the Maine Business Corporation Act.

(e) The affirmative vote of the holders of at least eighty percent (80%) of all of the shares of the Corporation entitled to vote for the election of Directors shall be required to amend or repeal, or to adopt any provisions in contravention of or inconsistent with this Section 2, notwithstanding the fact that a lesser percentage may be specified by law.

Section 3. Special Meetings and Consent Meetings.

Special meetings of the Shareholders may be called by the Chairman, President, the Board, or by the Secretary upon written request of the holders of not less than ten percent (10%) of all the shares entitled to vote.

Section 4. Acquisition of Stock.

(a) Restrictions on Offers and Acquisitions.

For a period of five (5) years from the effective date of the conversion, no person shall directly or indirectly offer to acquire or acquire the beneficial ownership of (i) more than ten percent (10%) of the issued and outstanding shares of any class of an equity security of the Corporation; (ii) more than ten percent (10%) of any class of securities convertible into, or exercisable for, any class of an equity security of the Corporation; (iii) any securities convertible into, or exercisable for, any equity securities of the Corporation if assuming conversion or exercise by such person of all securities of which such person is the beneficial owner which are convertible into, or exercisable for, such equity securities (but of no securities convertible into, or exercisable for, such equity securities of which such person is not the beneficial owner), such person would be the beneficial owner of more than ten percent (10%) of any class of an equity security of the Corporation.

For the same five year period, each share beneficially owned in violation of the foregoing percentage limitation, as determined by the Board, shall not be voted by any person or counted as voting shares in connection with any matter submitted to the shareholders for a vote.

For the purposes of this Section 4:

(i) The term "person" shall mean and include any individual, group acting in concert, Corporation, partnership, or other organization or entity, together with its affiliates and associates; and

(ii) The term "offer" includes every offer to buy or acquire, solicitation of an offer to sell, tender offer for, or request or invitation for tenders of, a security (including, without limitation, shares of any class of capital stock of the Corporation) or interest in a security for value.

(iii) The term "conversion" shall mean the completed process whereby Bethel Savings, FSB Bank will be converted from a federally chartered mutual savings bank to a federally charted stock savings bank and Bethel Bancorp shall become the holding company for Bethel Savings Bank, FSB.

(b) Exclusion for Underwriters, Directors, Officers and Employees.
The restriction contained in this Section 4 shall not apply to any offer with a view toward public resale made exclusively to the Corporation or the underwriters or a selling group acting on its behalf. In addition, the Directors, Officers and employees of the Corporation or any subsidiary thereof shall not be deemed to be a group with respect to their individual acquisition of equity stock of the Corporation.

(c) Readoption of Restriction by Shareholders.
This Section 4 may be readopted for additional one-year or longer periods by vote of the holders of a majority of the outstanding voting shares present or represented at a duly convened annual or

special meeting of Shareholders of the Corporation.

(d) Exception in Cases of Advance Approval.

This Section 4 shall not apply to any offer or acquisition referred to in (a) above if such offer or acquisition was approved in advance of such offer or acquisition by two-thirds (2/3) of the entire Board utilizing the standard set forth in Section 2(c).

(e) Enforcement of this Section 4.

The Corporation may by law or by resolution of the Directors adopt such provisions or resolutions as are necessary to provide for the enforcement of this Section 4.

(f) Amendments of this Section 4.

Notwithstanding any other provisions of these Articles of Incorporation or the By-Laws of the Corporation, and notwithstanding the fact that some lesser percentage may be specified by law, this Section 4 shall not be amended, altered, changed or repealed without:

a. the affirmative vote of two-thirds (2/3) of the Board; and
b. the affirmative vote by the holders of at least two-thirds (2/3) of the outstanding shares entitled to vote.

This vote shall be in addition to any vote of the Preferred Stock as may be required by the provisions of any series thereof or applicable by law.

The readoption of Section 4 for additional one-year or longer periods, as provided in (c) above, shall not be an amendment, alteration or change for the purposes of this paragraph.

Section 5. Amendments.

(a) Amendments to Articles of Incorporation.

Except as otherwise provided for in the Articles above, the affirmative vote of the holders of at least two-thirds (2/3) of all of the shares of the Corporation entitled to vote for the election of Directors, shall be required to amend or repeal, or to adopt any provision in contravention of or inconsistent with these Articles notwithstanding the fact that a lesser percentage may be specified by law.

(b) Amendments to By-Laws.

The By-Laws of the Corporation may be amended at any time by the affirmative vote of a majority of the entire Board, subject to repeal, change or adoption of any contravening or inconsistent provision only by vote of the holders of at least two-thirds (2/3) of all the shares entitled to vote on the matter at a meetings expressly called for that purpose.

Section 6. Right of Shareholders Following Control Transaction.

- -----------------------------------------------------------------
The provisions of ME Rev. Stat. Ann.Title 13-A, Section 910 shall not be applicable to the Corporation.

NORTHEAST BANCORP
Exhibit 11. Statement Regarding Computation of Per Share Earnings

| | Three Months Ended December 31, 1998 | Three Months Ended December 31, 1997 |
|---|---|---|
| EQUIVALENT SHARES: | | |
| Weighted Average Shares Outstanding | 2,692,802 | 2,222,543 |
| Total Diluted Shares | 2,786,889 | 2,753,434 |
| Net Income | $ 700,568 | $ 356,066 |
| Less Preferred Stock Dividend | 8,167 | 35,000 |
| Income Available to Common Stockholders | $ 692,401 | $ 321,066 |
| Basic Earnings Per Share | $ 0.26 | $ 0.14 |
| Diluted Earnings Per Share | $ 0.25 | $ 0.13 |

| | Six Months Ended December 31, 1998 | Six Months Ended December 31, 1997 |
|---|---|---|
| EQUIVALENT SHARES: | | |
| Weighted Average Shares Outstanding | 2,654,158 | 2,220,297 |
| Total Diluted Shares | 2,790,300 | 2,734,423 |
| Net Income | $ 1,336,605 | $ 926,631 |
| Less Preferred Stock Dividend | 25,667 | 69,999 |
| Income Available to Common Stockholders | $ 1,310,938 | $ 856,632 |
| Basic Earnings Per Share | $ 0.49 | $ 0.39 |
| Diluted Earnings Per Share | $ 0.48 | $ 0.35 |

9
1

6-MOS
JUN-30-1999
DEC-31-1998
5,092,834
13,765,064
0
0
17,372,783
0
0
284,313,294
2,869,000
336,194,991
201,930,962
38,384,275
5,836,232
63,844,266
0
0
2,755,076
23,444,180
336,194,991
12,488,988
371,438
382,447
13,242,873
4,287,652
7,243,946
5,998,927
369,421
58,490
4,802,886
2,089,760
2,089,760
0
0
1,336,605
0.49
0.48
3.725
1,594,000
0
184,896
614,056
2,978,000
542,375
63,954
2,869,000
74,000
0
2,795,000