NORTHWAY FINANCIAL INC
Form 10-Q
November 10, 2003

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549
FORM 10-Q

(Mark One)
[X] Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

For the quarterly period ended September 30, 2003

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 000-23129

NORTHWAY FINANCIAL, INC
(Exact name of registrant as specified in its charter)

New Hampshire	04-3368579
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
9 Main Street Berlin, New Hampshire	03570
(Address of principal executive offices)	(Zip Code)

(603) 752-1171
(Registrant's telephone number, including area code)

No Change
(Former name, former address and former fiscal year, if changed since last year)

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 twelve (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 ninety (90) days. YES [X] NO [ ]

Indicate by check mark whether the registrant is an accelerated filer (as defined in 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 practical date. At October 17, 2003, there were 1,499,574 shares of common stock outstanding, par value $1.00 per share.

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NORTHWAY FINANCIAL, INC.

PART 1. FINANCIAL INFORMATION

Item 1. Financial Statements.

NORTHWAY FINANCIAL, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

(Dollars in thousands)	Sep. 30, 2003

	(Unaudited)
Assets:	
Cash and due from banks and interest bearing deposits	$ 16,645
Federal funds sold	18,355
Securities available-for-sale	83,163
Federal Home Loan Bank stock	4,705
Federal Reserve Bank stock	365
Loans held-for-sale	957
Loans, net before allowance for loan losses	465,540
Less: allowance for loan losses	5,021
Loans, net	460,519
Other real estate owned	211
Premises and equipment, net	12,941
Core deposit intangible	4,142
Goodwill	10,152
Other assets	7,827
Total assets	$619,982
Liabilities and Stockholders' Equity:	
Liabilities	
Interest bearing deposits	$397,231
Noninterest bearing deposits	76,644
Securities sold under agreements to repurchase	8,633
Long-term Federal Home Loan Bank advances	67,000
Guaranteed preferred beneficial interest in junior subordinated debentures	20,000
Other liabilities	3,804
Total liabilities	573,312
Stockholders' equity	
Preferred stock, $1.00 par value; 1,000,000 shares authorized; none issued	-
Common stock, $1 par value; 9,000,000 shares authorized; 1,731,969 issued at September 30, 2003 and December 31, 2002 and 1,499,574 outstanding at September 30, 2003 and 1,516,574 outstanding at December 31, 2002	1,732
Surplus	2,088
Retained earnings	49,367
Treasury stock, at cost (232,395 and 215,395 shares, respectively)	(6,213
Accumulated other comprehensive loss, net of tax	(304
Total stockholders' equity	46,670
Total liabilities and stockholders' equity	$619,982

The accompanying notes are an integral part of these condensed consolidated financial statements.

NORTHWAY FINANCIAL, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

	Three Months	Nin

	Ended Sep. 30,		End
(Dollars in thousands, except per share data)	2003	2002	200
Interest and dividend income:			
Loans	$ 6,749	$ 6,837	$ 21,
Interest on debt securities:			
Taxable	744	687	2,
Tax-exempt	106	73	
Dividends	59	62	
Federal funds sold	54	119	
Interest bearing deposits	1	--	
Total interest and dividend income	7,713	7,778	23,
Interest expense:			
Deposits	1,057	1,552	3,
Borrowed funds	771	651	2,
Guaranteed preferred beneficial interest in junior subordinated debentures	248	271	
Total interest expense	2,076	2,474	6,
Net interest and dividend income	5,637	5,304	17,
Provision for loan losses	210	225	
Net interest and dividend income after provision for loan losses	5,427	5,079	16,
Noninterest income:			
Service charges and fees on deposit accounts	404	365	1,
Securities gains, net	614	(7)	
Loan servicing income	73	86	
Other	625	423	1,
Total noninterest income	1,716	867	3,
Noninterest expense:			
Salaries and employee benefits	2,861	2,435	8,
Office occupancy and equipment	894	801	2,
Amortization of core deposit intangible	238	82	
Write-down of equity securities	65	814	
Other	1,549	1,530	4,
Total noninterest expense	5,607	5,662	16,
Income before income tax expense	1,536	284	4,
Income tax expense	558	109	1,
Net income	$ 978	$ 175	$ 2,
Comprehensive net income	$ 141	$ 3	$ 3,
Per share data:			
Earnings per common share	$ 0.65	$ 0.12	$ 1
Earnings per common share (assuming dilution)	$ 0.65	$ 0.12	$ 1
Cash dividends declared	$ 0.17	$ 0.17	$ 0
Weighted average number of common shares	1,502,563	1,516,422	1,506,

The accompanying notes are an integral part of these condensed consolidated financial statements.

NORTHWAY FINANCIAL, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

(Dollars in thousands)	Fo
Cash flows from operating activities:	
Net income	$ 2
Adjustments to reconcile net income to net cash provided by operating activities:	
Provision for loan losses	
Depreciation and amortization	1
Deferred income tax expense	
Write-down of equity securities	
Gains on sales of securities available-for-sale, net	
Loss (gain) on disposal and write-down of premises and equipment	
Amortization of premiums and accretion of discounts on securities, net	
Increase in unearned income, net	
Amortization of discount on loans acquired	
Loss on sales of other real estate owned and other personal property, net	
Net (increase) decrease in loans held-for-sale	
Net change in other assets and other liabilities	1
Net cash provided by operating activities	5
Cash flows from investing activities:	
Proceeds from sales of securities available-for-sale	14
Proceeds from maturities of securities available-for-sale	61
Purchase of securities available-for-sale	(66
Loan originations and principal collections, net	(24
Recoveries of previously charged-off loans	
Proceeds from sales of and payments received on other real estate owned	
Proceeds from sales of and payments received on other personal property	
Additions to premises and equipment	(1
Net cash used in investing activities	(15
Cash flows from financing activities:	
Net (decrease) increase in deposits	(2
Advances from FHLB	28
Repayment of FHLB advances	(7
Net (decrease) increase in securities sold under agreements to repurchase	
Exercise of stock options	
Purchases of treasury stock	
Issuance of guaranteed preferred beneficial interest in junior subordinated debentures	
Cash dividends paid	
Net cash provided by financing activities	17
Net increase in cash and cash equivalents	7
Cash and cash equivalents at beginning of period	27
Cash and cash equivalents at end of period	$ 35
Supplemental disclosure of cash flows:	
Interest paid	$ 6
Taxes paid	$ 1

Loans transferred to other real estate owned	$
Loans transferred to other personal property	$

The accompanying notes are an integral part of these condensed consolidated financial statements.

NORTHWAY FINANCIAL, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2003
(Unaudited)

1. Basis of Presentation.

The unaudited condensed consolidated financial statements of Northway Financial, Inc. and its four wholly-owned subsidiaries, The Berlin City Bank, The Pemigewasset National Bank of Plymouth, the Northway Capital Trust I (an issuer of trust preferred securities) and the Northway Capital Trust II (also an issuer of trust preferred securities) (collectively, "the Company") included herein have been prepared by the Company in accordance with the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") have been condensed or omitted in accordance with such rules and regulations. The Company, however, believes that the disclosures are adequate to make the information presented not misleading. The amounts shown reflect, in the opinion of management, all adjustments necessary for a fair presentation of the financial statements for the periods reported.

The results of operations for the three and nine month periods ended September 30, 2003 and 2002 are not necessarily indicative of the results of operations to be expected for the full year or any other interim periods. The interim financial statements are meant to be read in conjunction with the Company's audited financial statements presented in its Annual Report on Form 10-K for the fiscal year ended December 31, 2002.

In preparing financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the dates of the balance sheet and revenues and expenses for the reported periods. Actual results could differ from these estimates. Material estimates that are particularly susceptible to change relate to the determination of the allowance for loan losses.

The year-end condensed consolidated balance sheet data was derived from audited financial statements, but does not include all disclosures required by GAAP.

2. Stock-Based Compensation

As of September 30, 2003, the Company has a stock-based employee compensation plan which is described more fully in its Annual Report on Form 10-K for the fiscal year ended December 31, 2002. The Company accounts for this plan under the recognition and measurement principles of the Auditing Practice Board ("APB") Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations. No stock-based employee compensation cost is reflected in net income, as all options granted under this plan had an exercise price equal to the market value of the underlying common stock on the date of the grant. The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of Statement of Financial Accounting Standards ("SFAS") No. 123, Accounting for Stock-Based Compensation, to stock-based employee compensation.

		($000 Omitted, Three Month Ended Sep. 3 2003	2002
Net income	As reported	$ 978	$
Deduct: Total stock-based employee compensation expense determined under fair value based methods awards, net of related tax effects		10	
	Pro forma	$ 968	$
Earnings per common share	As reported	$0.65	$
	Pro forma	$0.64	$
Earnings per common share (assuming dilution)	As reported	$0.65	$
	Pro forma	$0.64	$

3. Impact of New Accounting Standards.

SFAS No. 142, Goodwill and Other Intangible Assets, requires that goodwill no longer be amortized to earnings, but instead be reviewed for impairment. The amortization of goodwill ceased upon adoption of the statement, which for the Company was January 1, 2002. The effect of the adoption of SFAS No. 142 on the Company's consolidated financial statements is described below.

In October 2002, the Financial Accounting Standards Board (the "FASB") issued SFAS No. 147, Acquisitions of Certain Financial Institutions, an Amendment of SFAS Nos. 72 and 144 and FASB Interpretation No. 9. SFAS No. 72, Accounting for Certain Acquisitions of Banking or Thrift Institutions and FASB Interpretation No. 9, Applying APB Opinions No. 16 and 17 When a Savings and Loan Association or a Similar Institution Is Acquired in a Business Combination Accounted for by the Purchase Method, provided interpretive guidance on the application of the purchase method to acquisitions of financial institutions. Except for transactions between two or more mutual enterprises, SFAS No. 147 removes acquisitions of financial institutions from the scope of both Statement 72 and Interpretation 9 and requires that those transactions be accounted for in accordance with SFAS No. 141, Business Combinations and No. 142, Goodwill and Other Intangible Assets. Thus, the requirement in paragraph 5 of Statement 72 to recognize (and subsequently amortize) any excess of the fair value of liabilities assumed over the fair value of tangible and identifiable intangible assets acquired as an unidentifiable intangible asset no longer applies to acquisitions within the scope of SFAS No. 147. In addition, SFAS No. 147 amends SFAS No. 144 Accounting for the Impairment or Disposal of Long-Lived Assets to include in its scope long-term customer-relationship intangible assets of financial institutions such as depositor- and borrower-relationship intangible assets and credit cardholder intangible assets. Consequently, those intangible assets are subject to the same undiscounted cash flow recoverability test and impairment loss recognition and measurement provisions that SFAS No. 144 requires for other long-lived assets that are held and used.

Paragraph 5 of SFAS No. 147, which relates to the application of the purchase method of accounting, was effective for acquisitions for which the date of acquisition is on or after October 1, 2002. The provisions in paragraph 6 related to accounting for the impairment or disposal of certain long-term customer-relationship intangible assets were effective on October 1, 2002. Transition provisions for previously recognized unidentifiable intangible assets in paragraphs 8-14 were effective on October 1, 2002, with earlier application permitted.

In accordance with paragraph 9 of SFAS No. 147, the Company has reclassified, as of September 30, 2002 its recognized unidentifiable intangible asset related to branch acquisitions. This asset was reclassified as goodwill ("reclassified goodwill"). The amount reclassified was $5,386,000, the carrying amount as of January 1, 2002. The reclassified goodwill is being accounted for and reported prospectively as goodwill under SFAS No. 142, with no amortization expense. Accordingly, the consolidated financial statements for the three- and nine-months ended September 30, 2002 do not reflect amortization in the amount of $83,000 and $229,000, respectively, that would have been recorded if SFAS No. 147 had not been issued.

In accordance with SFAS No. 147 the Company tested its reclassified goodwill for impairment as of January 1, 2002 and December 31, 2002. The Company determined that its goodwill as of those dates was not impaired.

Also in accordance with paragraph 9 of SFAS No. 147, as of September 30, 2002, the Company reclassified its core deposit intangible ("CDI") asset and accounted for it as an asset apart from the unidentifiable intangible asset and not as goodwill. CDI is amortized over the expected life of the acquired deposits and is tested annually for impairment. As of December 31, 2002, the Company tested its CDI asset for impairment and determined that as of that date it was not impaired.

The effect of the Company's adoption of SFAS No. 147 was to increase net income for the three- and nine-month periods ended September 30, 2002 by $51,000 and $140,000, respectively.

In May 2003, FASB issued SFAS No. 150 Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity. This statement establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. SFAS No. 150 required the Company to reclassify on its balance sheet the line item "Guaranteed preferred beneficial interest in junior subordinated debentures" in the amount of $20,000,000. Prior to SFAS No. 150, this line item was presented between the liabilities section and the equity section of the Company's balance sheet. SFAS No. 150 requires that the line item now be classified as a liability. No additional disclosures are required in connection with SFAS No. 150.

On a related matter, FASB Interpretation Number 46, Consolidation of Variable Interest Rate Entities ("FIN 46") Interpretation of Accounting Research Bulletin No. 51 has been deferred until the end of the first reporting period that ends after December 15, 2003. Future regulatory pronouncements regarding the interpretation of FIN 46 may affect the capital treatment of the Company's outstanding guaranteed preferred beneficial interest in junior subordinated debentures.

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

The following discussion and analysis and the related condensed consolidated financial statements relate to Northway Financial, Inc. and its four wholly-owned subsidiaries, The Berlin City Bank, The Pemigewasset National Bank of Plymouth, Northway Capital Trust I and Northway Capital Trust II (collectively, the "Company").

Forward-Looking Statements

Certain statements in this Form 10-Q are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements can be identified by the use of the words "expect," "believe," "estimate," "will" and other expressions which predict or indicate future trends and which do not relate to historical matters. Forward-looking statements may include, but are not limited to, projections of revenue, income or loss, plans for future operations, including in new markets, and acquisitions, and plans related to products or services of the Company. Such forward-looking statements are subject to known and unknown risks, uncertainties and contingencies, many of which are beyond the control of the Company. The Company's actual results could differ materially from those projected in the forward-looking statements as the result of, among other factors, changes in interest rates, changes in the securities or financial markets, a deterioration in general economic conditions on a national basis or in the local markets in which the Company operates, including changes in local business conditions resulting in rising unemployment and other circumstances which adversely affect borrowers' ability to service and repay our loans, changes in loan defaults and charge-off rates, reduction in deposit levels necessitating increased borrowing to fund loans and investments, the passing of adverse government regulation, changes in assumptions used in making such forward-looking statements, as well as those factors set forth in the Company's Annual Report on Form 10-K for the year ending December 31, 2002, and in the Company's other filings with the Securities & Exchange Commission. These forward-looking statements were based on information, plans and estimates at the date of this report, and the Company does not promise to update any forward-looking statements to reflect changes in underlying assumptions or factors, new information, future events or other changes.

Financial Condition

The Company's total assets at September 30, 2003 were $619,982,000 compared to $598,318,000 at December 31, 2002, an increase of $21,664,000. Net loans, including loans held-for-sale, increased $23,575,000 to $461,476,000, the result of increases in all loan categories. Cash and cash equivalents increased $7,574,000 to $35,000,000, compared to $27,426,000 at December 31, 2002, due primarily to an increase in Federal Funds Sold. This was partially offset by a decrease in securities available-for-sale of $7,876,000 to $88,233,000 due primarily to lower mortgage-backed security balances partially offset by US Government Agency purchases.

Deposits decreased $2,319,000 from December 31, 2002 due to a decrease in time deposits and money market accounts, which was partially offset by an increase in NOW, DDA and savings account balances. Long-term Federal Home Loan Bank advances increased $21,000,000 to $67,000,000 from December 31, 2002 due to twelve new advances, totaling $28,000,000, during the year ranging in term from two years to seven years with an average interest rate of 2.74% which was partially offset by the maturity of $7,000,000 in advances. Total stockholders' equity increased $2,404,000 to $46,670,000 at September 30, 2003 from $44,266,000 at December 31, 2002 due primarily to net income of $2,613,000 and an increase in accumulated other comprehensive gain of $1,062,000 which was partially offset by dividends paid of $768,000 and an increase in treasury stock of $502,000. At September 30, 2003, unrealized equity security losses of $344,000 are included in accumulated other comprehensive loss, net of tax. Management does not consider the underlying equity securities to be other than temporarily impaired.

The Company maintains an allowance for loan losses to absorb charge-offs of loans in the existing portfolio. The allowance is increased when a loan loss provision is recorded as an expense. When a loan, or portion thereof, is considered uncollectible, it is charged against this allowance. Recoveries of amounts previously charged-off are added to the allowance when collected. At September 30, 2003 the allowance for loan losses was $5,021,000, or 1.08% of total loans, compared to $4,920,000, or 1.11% of total loans at December 31, 2002. The allowance for loan losses is based on an evaluation by each bank's management and Board of Directors of current and anticipated economic conditions, changes in the diversification, size and risk within the loan portfolio, and other factors. The composition of the allowance for loan losses for the three and nine month periods ended September 30, 2003 and 2002 is as follows:

(Dollars in thousands)	Three Months Ended Sep. 30, 2003	Three Months Ended Sep. 30, 2002	Nine Months Ended Sep. 30, 2003	Nine Months Ended Sep. 30, 2002
Balance at beginning of period	$4,994	$4,870	$4,920	$4,642
Charge-offs	(231)	(208)	(695)	(534)
Recoveries	48	60	141	164
Net charge-offs	(183)	(148)	(554)	(370)
Provision for loan losses	210	225	655	675
Balance at end of period	$5,021	$4,947	$5,021	$4,947

Nonperforming loans totaled $4,102,000 as of September 30, 2003, compared to $3,619,000 at December 31, 2002. The ratio of nonperforming loans to loans net of unearned income was 0.88% as of September 30, 2003 compared to 0.82% at December 31, 2002. Nonperforming assets, which include nonperforming loans, other real estate owned and other chattels owned, totaled $4,441,000 as of September 30, 2003, compared to $3,892,000 at December 31, 2002. The ratio of nonperforming assets to total assets was 0.72% as of September 30, 2003 compared to 0.65% at December 31, 2002.

Results of Operations

The Company reported net income of $978,000, or $0.65 per common share, for the three months ended September 30, 2003, compared to $175,000, or $0.12 per common share, for the three months ended September 30, 2002. Net income for the nine months ended September 30, 2003 was $2,613,000, or $1.74 per common share, compared to $2,216,000, or $1.46 per common share, for the nine months ended September 30, 2002. The increase in net income for both the quarter and year-to-date is attributable to an improvement in net interest income, an increase in noninterest income, and a decrease in write-down of equity securities. This is partially offset by an increase in noninterest expense, excluding the write-down of equity securities.

Net interest and dividend income for the third quarter increased $333,000 to $5,637,000 compared to $5,304,000 for the third quarter of 2002. For the nine months ended September 30, 2003 net interest and dividend income increased $1,381,000, or 8.6%, to $17,438,000 compared to $16,057,000 for the same period of the prior year due primarily to an increase in average earning assets of $78,229,000 partially offset by a decrease in the net interest margin of 0.30%.

The provision for loan losses decreased $15,000 to $210,000 for the third quarter of 2003 compared to $225,000 for the third quarter of 2002. In addition, the provision decreased $20,000 to $655,000 for the nine months ended September 30, 2003 compared to $675,000 for the nine months ended September 30,

2002. The provision for loan losses is based upon a review of the adequacy of the allowance for loan losses, which is conducted on a quarterly basis. This review is based upon many factors including the risk characteristics of the portfolio, trends in loan delinquencies, and an assessment of existing economic conditions. In addition, various regulatory agencies, as part of their examination process, review the banks' allowances for loan losses and such review may result in changes to the allowance based on judgments different from those of management.

The decrease in the provision was due in part to the recording of $70,000 to other expense for a provision for losses related to unfunded loan commitments such as unused lines of credit and unused portions of home-equity loans. This provision had previously been calculated as part of the allowance for loan losses.

Noninterest income increased $849,000 to $1,716,000 in the third quarter of 2003 compared to $867,000 in the third quarter of 2002. Service charges and fees on deposit accounts increased $39,000 due to increases in overdraft fee income and service charge income resulting from the branch acquisitions in the fourth quarter 2002. Net securities gains increased $621,000 in the third quarter of 2003 compared to the third quarter of 2002 due primarily to the sale of corporate securities. Other noninterest income increased $202,000 due primarily to increases in gains on sales of loans and the recognition of other loan fees resulting from transactions with Federal Home Loan Mortgage Corporation ("FHLMC"). This was partially offset by a decrease in gain on sale of property resulting from the 2002 sale of a former branch facility. For the nine months ended September 30, 2003 noninterest income increased $1,166,000, or 45.4%, to $3,737,000 compared to $2,571,000 for the same period of the prior year. The increase was primarily the result of increases in service charges on deposit accounts and overdraft fees, gains on sales of securities, debit card fee income, gain on sale of loans, FHLMC fee income, and a valuation adjustment on split dollar life insurance. This was partially offset by decreases in gain on sale of property, loan servicing income and extension fees associated with our skip-a-payment program for indirect auto loans.

Noninterest expense decreased $55,000 to $5,607,000 for the quarter ended September 30, 2003, compared to the $5,662,000 recorded during the same period last year. Noninterest expense increased $1,867,000, or 12.8%, to $16,418,000 for the nine months ended September 30, 2003, compared to $14,551,000 for the same period last year.

Although the equity investment market has improved significantly over last year when an impairment of $814,000 was experienced during the third quarter, stocks within certain market segments have underperformed. Accordingly, based on the Company's ongoing analysis of its equity holdings during the third quarter of 2003 and for the year-to-date period impairment write-downs of $65,000 and $184,000, respectively were recorded.

Excluding this write-down of equity securities noninterest expense increased $694,000 for the quarter and $2,497,000 year-to-date. For both the quarter and year-to-date these increases were attributable to the following: As a result of the branch acquisitions in the fourth quarter of 2002, the Company experienced increases in salaries and benefits, office occupancy and equipment, the amortization of core deposit intangibles and other expenses. Increases were also recognized in salaries and benefits due to staff additions to support increased loan demand and expansion into new markets. In addition, other expenses increased due to staff development initiatives in support of a customer focused Northway culture.

Additionally, year-to-date noninterest expense has been impacted by an increase in depreciation expense resulting from the technology purchases made during the third quarter of 2002. Further, the year-to-date noninterest expense was impacted by an increase in legal expense due primarily to the review of new disclosure requirements and loan documentation. In addition, during the second and third quarters of 2003, the Company recognized an expense to record a provision for losses related to unfunded loan commitments such as unused lines of credits and unused portions of home-equity loans. Management will review this provision quarterly and adjustments to expense will be made as appropriate.

Income Tax Expense

The Company recognized income tax expense of $1,489,000 and $1,186,000 for the nine months ended September 30, 2003 and 2002, respectively. The effective tax rates were 36.3% and 34.9% for those respective periods.

Liquidity

Liquidity risk management refers to the Company's ability to raise funds in order to meet existing and anticipated financial obligations. These obligations to make payment include withdrawal of deposits on demand or at their contractual maturity, the repayment of borrowings as they mature, funding new and existing loan commitments as well as new business opportunities. Liquidity may be provided through amortization, maturity or sale of assets such as loans and securities available-for-sale, liability sources such as increased deposits, utilization of the Federal Home Loan Bank ("FHLB") credit facility, purchased or other borrowed funds, and access to the capital markets. Liquidity targets are subject to change based on economic and market conditions and are controlled and monitored by the Company's Asset/Liability Committee.

At the subsidiary bank level, liquidity is managed by measuring the net amount of marketable assets, after deducting pledged assets, plus lines of credit, primarily with the FHLB, that are available to fund liquidity requirements. Management then measures the adequacy of that aggregate amount relative to the aggregate amount of liabilities deemed to be sensitive or volatile. These include core deposits in excess of $100,000, term deposits with short maturities, and credit commitments outstanding.

Additionally, Northway Financial, Inc. requires cash for various operating needs, including dividends to shareholders, the stock repurchase program, capital injections to the subsidiary banks, and the payment of general corporate expenses. The primary sources of liquidity for Northway Financial, Inc. are dividends from its subsidiary banks.

Management believes that the Company's current level of liquidity and funds available from outside sources is sufficient to meet the Company's needs.

Capital

The Company's Tier 1 and Total Risk Based Capital ratios were 8.98% and 12.19%, respectively, at September 30, 2003. The Company's Tier 1 leverage ratio at September 30, 2003 was 6.85%. As of September 30, 2003, the capital ratios of the Company and the subsidiary banks exceeded the minimum capital ratio requirements of the "well-capitalized" category under the Federal Deposit Insurance Corporation Improvement Act of 1991.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Since December 31, 2002, there have been no material changes in the Company's quantitative and qualitative disclosures about market risk. A fuller description of the quantitative and qualitative disclosures about market risk was provided by the Company on pages 11 through 22 of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2002.

Item 4. Controls and Procedures

(a) Evaluation of disclosure controls and procedures.

As required by Rule 13a-15 under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), the Company's management conducted an evaluation with the participation of the Company's Chief Executive Officer and Chief Financial Officer, regarding the effectiveness of the Company's disclosure controls and procedures, as of the end of the last fiscal quarter. In designing and evaluating the Company's disclosure controls and procedures, the Company and its management recognize that any controls and procedures, no matter how well designed and operated, can provide only a reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating and implementing possible controls and procedures. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that they believe the Company's disclosure controls and procedures are reasonably effective to ensure that information required to be disclosed by the Company in the reports it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. We intend to continue to review and document our disclosure controls and procedures, including our internal controls and procedures for financial reporting, and we may from time to time make changes to the disclosure controls and procedures to enhance their effectiveness and to ensure that our systems evolve with our business.

(b) Changes in internal controls.

There were no changes in the Company's internal controls over financial reporting identified in connection with the Company's evaluation of its disclosure controls and procedures that occurred during the Company's last fiscal quarter that has materially affected, or is reasonably likely to materially affect the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings - None

Item 2. Changes in Securities and Use of Proceeds - None

Item 3. Defaults upon Senior Securities - None

Item 4. Submission of Matters to a Vote of Security Holders - None

Item 5. Other Information - None

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

Exhibit Number	Description of Exhibit
11	Statement Re Computation of per share earnings(1)
31.1	Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934(1)
31.2	Certification of Chief Financial Officer Pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934(1)
32.1	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the

Sarbanes-Oxley Act of 2002(1)

32.2	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002(1)

(1) Filed herewith.

(b) Current Report on Form 8-K filed on July 31, 2003.
Item reported: Earnings announcement for second quarter ending June 30, 2003.

SIGNATURES

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

NORTHWAY FINANCIAL, INC.

November 4, 2003 BY:/S/ William J. Woodward

William J. Woodward
President & CEO
(Principal Executive Officer)

November 4, 2003 BY:/S/ Richard P. Orsillo

Richard P. Orsillo
Senior Vice President & CFO
(Principal Financial and Accounting Officer)

INDEX OF EXHIBITS

Exhibit Number	Description of Exhibit
11	Statement Re Computation of per share earnings(1)
31.1	Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934(1)
31.2	Certification of Chief Financial Officer Pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934(1)
32.1	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002(1)
32.2	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002(1)

(1) Filed herewith.