HEALTHWAYS, INC
Form PREC14A
April 18, 2014

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

SCHEDULE 14A
(Rule 14a-101)

INFORMATION REQUIRED IN PROXY STATEMENT

SCHEDULE 14A INFORMATION

Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934

(Amendment No. 1)

Filed by the Registrant o

Filed by a Party other than the Registrant x

Check the appropriate box:

x Preliminary Proxy Statement

¨ Confidential, for Use of the Commission Only (as permitted by Rule14a-6(e)(2))

¨ Definitive Proxy Statement

o Definitive Additional Materials

o Soliciting Material Under Rule 14a-12

HEALTHWAYS, INC.
(Name of Registrant as Specified in Its Charter)

NORTH TIDE CAPITAL MASTER, LP
NORTH TIDE CAPITAL, LLC
CONAN J. LAUGHLIN
EDWIN "MAC" CRAWFORD
BRADLEY S. KARRO
PAUL H. KECKLEY
(Name of Persons(s) Filing Proxy Statement, if Other Than the Registrant)

Payment of Filing Fee (Check the appropriate box):

x No fee required.

¨ Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

(1) Title of each class of securities to which transaction applies:

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(2) Aggregate number of securities to which transaction applies:

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(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

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(4) Proposed maximum aggregate value of transaction:

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(5) Total fee paid:

¨ Fee paid previously with preliminary materials:

¨ Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the form or schedule and the date of its filing.

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(1) Amount previously paid:

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(2) Form, Schedule or Registration Statement No.:

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(3) Filing Party:

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(4) Date Filed:

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PRELIMINARY COPY SUBJECT TO COMPLETION
DATED APRIL __, 2014

NORTH TIDE CAPITAL MASTER, LP

__________________, 2014

Dear Fellow Healthways Stockholder:

North Tide Capital Master, LP and the other participants in this solicitation (collectively, "North Tide" or "we") are the beneficial owners of an aggregate of 3,850,000 shares of common stock, par value $.001 per share (the "Common Stock"), of Healthways, Inc., a Delaware corporation ("Healthways" or the "Company"), representing close to 11% of the outstanding shares of Common Stock of the Company. We have nominated a slate of four (4) highly qualified director candidates for election at Healthways' upcoming 2014 annual meeting of stockholders (the "Annual Meeting"). We did so because we believe the current board of directors (the "Board") has failed to represent the best interests of stockholders and because we believe that the individuals we have nominated are highly qualified, capable and ready to serve stockholders to help make Healthways a stronger, more profitable, and ultimately more valuable company.

We have serious concerns with Healthways' prolonged underperformance under the direction of the current management team and Board. Despite our efforts to recommend specific actions to enhance stockholder value and to place highly-qualified independent directors on the Board while avoiding a costly and distracting proxy battle, we believe the Board has been unwilling to embrace the level of change required at Healthways. In both private and public letters as well as numerous conversations with representatives of the Company, we have clearly articulated our view that in order to maximize value for stockholders, we believe change is needed on the Board to ensure that appropriate actions are taken to improve execution, drive better financial performance and hold management accountable.

We strongly believe significant representation on the Board is required at this juncture and will help stockholders to realize maximum value for their investment in the Company. We are therefore seeking your support at the Annual Meeting to elect four (4) director candidates in order to ensure that the interests of the stockholders, the true owners of the Company, are appropriately represented in the boardroom at all times. We believe these director candidates collectively possess a well-balanced mix of skill sets to ensure that the Board (i) fulfills its duty to provide effective oversight of the Company, (ii) determines the appropriate corporate strategy to create value for the benefit of all stockholders, and (iii) holds management accountable for executing against those objectives.

The Company has a classified Board, which is currently divided into three classes. The terms of four (4) Class II directors expire at the Annual Meeting and four (4) directors will be elected at the Annual Meeting. We are seeking your support at the Annual Meeting to elect our four (4) nominees in opposition to the Company's director nominees for annual terms ending in 2015. North Tide believes that any attempt to increase the size of the current Board or the number of directors up for election at the Annual Meeting would constitute an improper manipulation of Healthways' corporate machinery. Your vote to elect our nominees will have the legal effect of replacing four incumbent directors with our nominees. If elected, there can be no guarantee that our nominees will be able to implement the actions that they believe are necessary to enhance stockholder value.

We urge you to carefully consider the information contained in the attached Proxy Statement and then support our efforts by signing, dating and returning the enclosed BLUE proxy card today. The attached Proxy Statement and the enclosed BLUE proxy card are first being furnished to the stockholders on or about __________, 2014.

If you have already voted for the incumbent management slate, you have every right to change your vote by signing, dating and returning a later dated proxy.

If you have any questions or require any assistance with your vote, please contact Okapi Partners LLC, who is assisting us, at its address and toll-free numbers listed below.

Thank you for your support.

/s/ Conan J. Laughlin

Conan J. Laughlin
Managing Member, North Tide Capital, LLC

If you have any questions, require assistance in voting your BLUE proxy card,
or need additional copies of North Tide's proxy materials,
please contact Okapi Partners at the phone numbers or email listed below.

OKAPI PARTNERS LLC
437 Madison Avenue, 28th Floor
New York, N.Y. 10022
(212) 297-0720
Stockholders Call Toll-Free at: 877-869-0171
E-mail: info@okapipartners.com

2014 ANNUAL MEETING OF STOCKHOLDERS
OF
HEALTHWAYS, INC.

PROXY STATEMENT
OF
NORTH TIDE CAPITAL MASTER, LP

PLEASE SIGN, DATE AND MAIL THE ENCLOSED BLUE PROXY CARD TODAY

North Tide Capital Master, LP ("North Tide Master"), North Tide Capital, LLC ("North Tide Capital") and Conan J. Laughlin (collectively, "North Tide" or "we") are significant stockholders of Healthways, Inc., a Delaware corporation ("Healthways" or the "Company"), owning close to 11% of the outstanding shares of common stock, par value $0.001 per share (the "Common Stock"), of the Company. We are seeking representation on the Board of Directors of the Company (the "Board") because we believe that the Board could be improved with directors who have strong, relevant backgrounds and who are committed to fully exploring all opportunities to unlock stockholder value. We are seeking your support at the annual meeting of stockholders scheduled to be held at the Franklin Marriott Cool Springs located at 700 Cool Springs Boulevard, Franklin, Tennessee, 37067 on Tuesday, June 24, 2014 at 9:30 a.m., Central time (including any adjournments or postponements thereof and any meeting which may be called in lieu thereof, the "Annual Meeting"), for the following:

1. To elect North Tide Master's director nominees, Edwin "Mac" Crawford, Bradley S. Karro, Paul H. Keckley and Conan J. Laughlin, (each a "Nominee" and, collectively, the "Nominees") to serve until the 2015 annual meeting of stockholders and until their respective successors are duly elected and qualified;

2. To consider and act upon a non-binding, advisory vote to approve compensation of Healthways' named executive officers (the "Say-on-Pay Proposal");

3. To ratify the appointment of Ernst & Young LLP as the Company's independent registered public accounting firm for fiscal 2014;

4. To consider and act upon a proposal to approve a new 2014 Stock Incentive Plan;

5. To consider and act upon a proposal to approve an amendment to the Company's Amended and Restated Bylaws, as amended (the "Bylaws"), to implement majority voting for uncontested elections of directors; and

6. To transact such other business as may properly come before the Annual Meeting.

As of the date hereof, the members of North Tide and the Nominees collectively own 3,850,000 shares of Common Stock. We intend to vote such shares of Common Stock FOR the election of the Nominees, [FOR/AGAINST] the approval of the Say-on-Pay Proposal, [FOR] the ratification of Ernst & Young LLP as the Company's independent auditor for the 2014 fiscal year, [FOR/AGAINST] the approval of the 2014 Stock Incentive Plan, and [FOR] approval of an amendment to the Company's Bylaws to implement majority voting for uncontested elections of directors, as described herein.

The Company has set the close of business on Monday, May 5, 2014 as the record date for determining stockholders entitled to notice of and to vote at the Annual Meeting (the "Record Date"). The mailing address of the principal executive offices of the Company is 701 Cool Springs Boulevard, Franklin, Tennessee 37067. Stockholders of record at the close of business on the Record Date will be entitled to vote at the Annual Meeting. According to the Company, as of the Record Date, there were [_________] shares of Common Stock outstanding.

THIS SOLICITATION IS BEING MADE BY NORTH TIDE AND NOT ON BEHALF OF THE BOARD OF DIRECTORS OR MANAGEMENT OF THE COMPANY. WE ARE NOT AWARE OF ANY OTHER MATTERS TO BE BROUGHT BEFORE THE ANNUAL MEETING OTHER THAN AS SET FORTH IN THIS PROXY STATEMENT. SHOULD OTHER MATTERS, WHICH NORTH TIDE IS NOT AWARE OF A REASONABLE TIME BEFORE THIS SOLICITATION, BE BROUGHT BEFORE THE ANNUAL MEETING, THE PERSONS NAMED AS PROXIES IN THE ENCLOSED BLUE PROXY CARD WILL VOTE ON SUCH MATTERS IN OUR DISCRETION.

NORTH TIDE URGES YOU TO SIGN, DATE AND RETURN THE BLUE PROXY CARD IN FAVOR OF THE ELECTION OF THE NOMINEES.

IF YOU HAVE ALREADY SENT A PROXY CARD FURNISHED BY COMPANY MANAGEMENT OR THE BOARD, YOU MAY REVOKE THAT PROXY AND VOTE ON EACH OF THE PROPOSALS DESCRIBED IN THIS PROXY STATEMENT BY SIGNING, DATING AND RETURNING THE ENCLOSED BLUE PROXY CARD. THE LATEST DATED PROXY IS THE ONLY ONE THAT COUNTS. ANY PROXY MAY BE REVOKED AT ANY TIME PRIOR TO THE ANNUAL MEETING BY DELIVERING A WRITTEN NOTICE OF REVOCATION OR A LATER DATED PROXY FOR THE ANNUAL MEETING OR BY VOTING IN PERSON AT THE ANNUAL MEETING.

Important Notice Regarding the Availability of Proxy Materials for the Annual Meeting—
This Proxy Statement and our BLUE proxy card are available at
[_______________________]

IMPORTANT

Your vote is important, no matter how few shares of Common Stock you own. North Tide urges you to sign, date, and return the enclosed BLUE proxy card today to vote FOR the election of the Nominees.

- If your shares of Common Stock are registered in your own name, please sign and date the enclosed BLUE proxy card and return it to North Tide, c/o Okapi Partners LLC ("Okapi Partners") the enclosed postage-paid envelope today.

- If your shares of Common Stock are held in a brokerage account or bank, you are considered the beneficial owner of the shares of Common Stock, and these proxy materials, together with a BLUE voting form, are being forwarded to you by your broker or bank. As a beneficial owner, you must instruct your broker, trustee or other representative how to vote. Your broker cannot vote your shares of Common Stock on your behalf without your instructions.

- Depending upon your broker or custodian, you may be able to vote either by toll-free telephone or by the Internet. Please refer to the enclosed voting form for instructions on how to vote electronically. You may also vote by signing, dating and returning the enclosed voting form.

Since only your latest dated proxy card will count, we urge you not to return any proxy card you receive from the Company. Even if you return the management proxy card marked "withhold" as a protest against the incumbent directors, it will revoke any proxy card you may have previously sent to us. Remember, you can vote for our Nominees only on our BLUE proxy card. So please make certain that the latest dated proxy card you return is the BLUE proxy card.

OKAPI PARTNERS LLC

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Background to the Solicitation

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Background to the Solicitation

The following is a chronology of material events leading up to this proxy solicitation.

- On August 12, 2013, North Tide met with Healthways CEO Ben Leedle, CFO Alfred Lumsdaine and Charles Wochomurka, SVP of Investor Relations, at Healthways' headquarters in Franklin, Tennessee and discussed general business trends, Healthways' performance and the Company's capital structure.

- On September 12, 2013, Mr. Laughlin met with Messrs. Leedle, Lumsdaine and Wochomurka at the Stifel Nicolaus healthcare conference in Boston, Massachusetts.

- On October 24, 2013, North Tide and Messrs. Leedle, Lumsdaine and Wochomurka had a teleconference and discussed Healthways' guidance for 2013 and 2014.

- On October 28, 2013, North Tide filed a Schedule 13D disclosing a 9.88% stake in Healthways. In the Schedule 13D, North Tide disclosed that it may initiate discussions with the Board regarding the performance of the Healthways' management team and/or other matters concerning the management of Healthways.

- On November 4, 2013, North Tide and Mr. Lumsdaine had a teleconference and discussed Healthways' Silver Sneakers business.

- On November 15, 2013, Mr. Laughlin met with John Ballantine, Chairman of the Board, and Mary Flipse, the Company's General Counsel, in New York City. At this meeting, Mr. Laughlin detailed management's poor track record, the Company's terrible shareholder returns over almost any measuring period, and the need for the Board to act to restore accountability and credibility, and make long overdue changes to improve shareholder value.

- On December 2, 2013, North Tide delivered a letter to the Board in which it stated that it believes there is considerable value in Healthways shares but that it has deep concerns about the ability of the current management team, in particular CEO Ben Leedle, to deliver and/or achieve recognition for that value. In the letter, North Tide stated that it believed the value destruction for Healthways stockholders during Mr. Leedle's tenure as CEO is irrefutable. North Tide further stated that one of the hallmarks of Mr. Leedle's tenure is a pattern of "hype" and disappointment, and that senior management team will miss internally established EPS targets published in annual proxy statements on file with the Securities and Exchange Commission (the "SEC"), for the third year in a row, the fourth year in the last six, and the sixth year in the last ten. North Tide stated that Mr. Leedle had lost all remaining credibility in the investment community, and the Board needs to recognize what this means from a stockholder value standpoint going forward. North Tide provided that in spite of its concerns around the management at Healthways, it believes the Company's share price is significantly undervalued, and there are steps the Board can take to significantly enhance stockholder value, including by: (i) removing Mr. Leedle from his CEO position; (ii) unlocking the value of the Company's Silver Sneakers business; (iii) terminating the Company's international operations; and (iv) re-focusing Healthways on its core domestic population health and wellness business.

- On December 19, 2013, North Tide filed an amendment to its Scehdule 13D disclosing that it had increased its stake in Healthways to 11% of the outstanding shares of Common Stock.

- On December 20, 2013, Mr. Laughlin conversed with Mr. Ballantine and reiterated the points made in North Tide's December 2, 2013 letter to Healthways. During this conversation, Mr. Laughlin asked for the Board to acknowledge the need for change at the Company and to act on North Tide's recommendations by removing Mr. Leedle as CEO of the Company and initiating a strategic review of the Company and its prospects to boost shareholder value.

- On December 27, 2013, Mr. Laughlin and Mr. Ballantine had a phone conversation during which Mr. Ballantine stated that the Board fully supported management and Healthways' strategic plans. Mr. Laughlin reiterated his frustration with the status quo and his dissatisfaction with the Board's unwillingness to acknowledge or address the need for change at Healthways.

- On January 14, 2014, North Tide delivered a letter to the Board. In the letter, North Tide stated that while it sincerely appreciates the open dialogue that the Board has maintained with North Tide over the previous two months, North Tide is concerned by the Board's apparent laissez–faire attitude toward the need for change at Healthways and unwavering support for CEO Ben Leedle despite the substantial value destruction that stockholders have suffered during his tenure. In the letter, North Tide emphasized its serious concerns regarding: (i) the Board's failure to hold Mr. Leedle accountable for his continued operational shortcomings or meaningfully respond to the serious concerns that North Tide raised in its December 2, 2013 letter to the Board and in North Tide's ensuing private conversations with Mr. Ballantine; (ii) the Board's failure to address the severe underperformance and decline of the Company's core health and wellness operations, which has been masked to a large extent by the success of the Silver Sneakers business; and (iii) the current Board members' seeming unwillingness to act as unbiased stewards in their service to Healthways' stockholders and set a new direction for the Company to reverse the years of disappointment to which stockholders have unfortunately grown accustomed. North Tide stated in the letter that it intended to pursue all available options to effect necessary leadership change at Healthways, including, but not limited to, nominating a slate of directors at the Annual Meeting, in order to ensure that the best interests of all stockholders are properly represented in the boardroom.

- On February 19, 2014, Mr. Ballantine contacted North Tide with an offer from the Board to appoint one of North Tide's nominees to the Board and grant North Tide with access to a strategic review process conducted by J.P. Morgan. This offer was subject to North Tide's entry into a standstill agreement. North Tide responded by pointing out that the Board's settlement proposal failed to meaningfully address any of North Tide's stated concerns, and that North Tide would be willing to enter into a settlement with the Board only around a framework that involves substantial Board representation and Ben Leedle's resignation as CEO.

- Also on February 19, 2014, North Tide delivered a letter to Mr. Ballantine in which it stated that Tom Cigarran's resignation letter and the Board's enduring support of CEO Ben Leedle, despite his repeated failures including the prior week's disappointing earnings report, points to a Board that is committed to perpetuating the troubling status quo. In the letter, North Tide stated that it remains steadfast in its belief that material change in leadership and board composition is required at Healthways and that the Board's February 19, 2014 offer of one Board seat was an inadequate response to North Tide's serious concerns. North Tide further provided that it would be amenable to a settlement that included the following: (i) at the Annual Meeting, three North Tide director nominees would be nominated in place of three of Healthways' Class II directors; (ii) a fourth director nominee would be a candidate mutually agreeable to North Tide and the Board; (iii) Ben Leedle would resign as CEO of the Company; and (iv) North Tide would enter into a customary standstill arrangement wherein it would agree not to submit any nominations for the Annual Meeting and would be reimbursed for certain of its expenses.

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- On February 24, 2014, Mr. Ballantine presented North Tide with the Board's revised settlement offer (the "February 24 Settlement"), pursuant to which the Board would nominate five directors at the Annual Meeting. The February 24 Settlement provided that two of the nominees would be proposed by North Tide, subject to confirmation by the Nominating and Governance Committee and confirmation that such nominees are independent and not otherwise affiliated with North Tide. Two of the nominees would be selected by the Board from its existing Class II directors. The Board would be expanded to twelve (12), with one additional independent nominee proposed by Healthway, subject to the Board's approval. In addition, the Board would create a Strategic Review Committee for the purpose of assisting management and the Board in reviewing and refining the Company's long range strategy. One of North Tide's director nominees would serve on each standing committee of the Board (presuming the director meets applicable legal qualification standards) and on the Strategic Review Committee. North Tide would enter into a customary voting agreement, including North Tide agreeing to vote its shares in favor of the Board's recommendations for matters presented for stockholder vote at the Annual Meeting. North Tide would enter into a customary standstill agreement expiring on the date ending thirty (30) days prior to the deadline for stockholders to nominate directors for the 2015 annual meeting of stockholders. The Company would reimburse North Tide for its out-of-pocket expenses, subject to an agreed upon cap. During a phone conversation on the same date, Mr. Ballantine indicated to North Tide that the Board would not consider a settlement that included Mr. Leedle's resignation as CEO.

- On February 26, 2014, North Tide delivered a letter to the Board in which it provided that it disagreed with the Board's assessment of management but would be willing to settle with the Board and avoid a costly and distracting proxy contest if the Board would accommodate North Tide's request for substantial Board representation. North Tide provided that its nominee candidates would go a long way toward restoring the credibility of Healthways within the investment community, as they are deeply qualified in healthcare and turnaround situations. North Tide proposed a settlement that included what it believes is necessary for Healthways: (i) the Board's support of the nomination of North Tide's four (4) Nominees; (ii) the appointment of one of North Tide's nominees as Chairman of the Board; and (iii) Mr. Ballantine's resignation from the Board.

- On February 27, 2014, the Mr. Ballantine sent a letter to North Tide in which the Board expressed its confidence in Healthways' management and leadership under CEO Ben Leedle as well as the Company's current strategy. In the letter, the Board expressed its disagreement with North Tide's proposals and North Tide's "apparent determination to proceed with a disruptive and costly proxy contest at the expense of all Healthways shareholders", and reiterated the February 24 Settlement.

- On February 28, 2014, North Tide delivered a letter to the Board in which it reiterated its belief that material changes in board composition, executive leadership, and corporate strategy are immediately required at Healthways. In the letter, North Tide stated that it has made significant efforts to communicate constructively with the Board to arrive at a mutually agreeable resolution that would provide for the level of management and Board change required at Healthways without the need for an election contest. North Tide also stated that the Board has entrenched itself in support of the status quo, and in so doing has put its own interests ahead of those of the Company's stockholders. North Tide therefore believes that change is needed on the Board to ensure that appropriate actions are taken to improve execution, drive better financial performance, hold management accountable and create value for all stockholders. To that end, North Tide delivered a letter to the Company (the "Nomination Letter") nominating Conan J. Laughlin, Edwin "Mac" Crawford, Bradley S. Karro and Paul H. Keckley for election to the Board at the Annual Meeting.

- Also on February 28, 2014, Healthways issued a press release in which Mr. Ballantine expressed his confidence in the Board's strategy and management's ability to move the Company forward. In the press release, Mr. Ballantine reiterated the February 24 Settlement and stated that the Board regrets North Tide's rejection of the proposal and decision to move forward with a proxy contest.

- On March 31, 2014, North Tide filed its preliminary proxy statement with the SEC in connection with the Annual Meeting.

- Also on March 31, 2014, North Tide issued an investor presentation, in which it detailed its case for change at Healthways.

- On April 14, 2014, Healthways filed its preliminary proxy statement with the SEC in connection with the Annual Meeting.

- Also on April 14, 2014, Healthways issued a press release in connection with the Annual Meeting.

REASONS FOR THE SOLICITATION

We are soliciting your support to elect our Nominees at the Annual Meeting because we have little confidence that the Board, as currently composed, has the objectivity and commitment to take the steps necessary to enhance stockholder value at Healthways. In putting forth the Nominees for election at the Annual Meeting, we are not attempting to take control of the Board. However, we do believe significant change to the composition of the Board is warranted given the strong qualifications of our Nominees and the serious issues facing the Company. If the Nominees are elected to the Board, they will comprise less than a majority of the Board.

THE TIME HAS COME FOR REAL CHANGE AT HEALTHWAYS

We have serious concerns with Healthways' prolonged underperformance under the direction of the current management team and Board. As we have continuously stated in both private and public letters, we believe the Board's apparent laissez-faire attitude toward the need for change at Healthways and unwavering support for CEO Ben Leedle, despite the substantial value destruction that stockholders have suffered during his tenure, is unacceptable.

We believe that change is needed on the Board to ensure that appropriate actions are taken to improve execution, drive better financial performance, hold management accountable, and create value for all stockholders. These changes should include new highly qualified independent directors with relevant credentials for Healthways, as well as direct stockholder representation to ensure the best interests of all stockholders are appropriately represented on the Board.

WE ARE CONCERNED WITH THE COMPANY'S PROLONGED POOR STOCK PERFORMANCE

HWAY shares have dramatically underperformed over the past 1 year, 3 years, 5 years, and 10 years. Healthways' shares have dramatically underperformed the S&P 500 Index, the S&P Healthcare Index, and the Company's peer group (as specified in the Company's proxy statement for the 2013 Annual Meeting) over almost any measurement period.

The chart above illustrates the performance of Healthways' Common Stock relative to the S&P 500 Index and the S&P Healthcare Index for the period beginning October 2003 and leading up to the filing of North Tide's initial Schedule 13D with the SEC in October 2013.

WE ARE CONCERNED WITH THE COMPANY'S PROLONGED POOR OPERATIONAL PERFORMANCE

Over the past five years, EBITDA has declined 64%, EPS have declined precipitously and are now negative, and the Company is dangerously close to violating its recently modified debt covenants. EBITDA was lower in 2013 than it was ten years ago despite roughly $600 million spent on acquisitions and a 411% increase in debt over that time period.

Senior management has missed its internal financial targets in six out of the past ten years, including 4 of the last 6 years, and in each of the last 3 years.

WE BELIEVE THAT MISMANAGEMENT AND POOR EXECUTIVE DECISIONS ARE ERODING STOCKHOLDER VALUE

We strongly believe management's actions have caused significant damage to stockholders and that steps must be taken to repair this damage. Mr. Leedle's tenure as CEO has been marked by a consistent pattern of a pattern irresponsibly promoting various growth opportunities, and downplaying potential risks, most of which have gone the "wrong way", and shareholders have suffered greatly as a result. We believe the Board, with its limited relevant healthcare operating experience, is relying on management's characterization of the Company's growth opportunities to justify its support for the strategy currently in place. We question how the Board could take seriously the projections and prognostications of a management team that has missed the mark on almost everything it has targeted over the last decade.

The most apparent example of this was Mr. Leedle's proclamation on the third quarter 2007 earnings call that the Medicare Health Support pilot could turn into a $20 billion revenue opportunity, and of course when that did not materialize in 2008, Healthways shareholders paid a huge price. Mr. Leedle failed to see and react to a trend of health plan insourcing beginning in 2008, and he has been promoting the international "opportunity" since 2006 with little to show for it now seven years later. Throughout the last year, Mr. Leedle has been touting the Company's success with health systems and "accountable care organizations", only to reduce guidance in late October because these customers have not ramped as fast as he projected.

The value destruction for Healthways shareholders during Mr. Leedle's tenure as CEO is irrefutable. Since Mr. Leedle was appointed CEO in September 2003, Healthways' share price performance has been abysmal on both an absolute and relative basis. From its peak in early 2008, the company's market capitalization declined more than 80% from $2.5 billion to less than $400 million as of the date that we filed our initial Schedule 13D. EBITDA was lower in 2013 than it was in Mr. Leedle's first full year as CEO, despite more than $600 million in acquisitions and an increase in the Company's debt balance from $0 to $250 million.

WE HAVE CONCERNS WITH THE HIGH LEVEL OF MANAGEMENT TURNOVER BELOW THE CEO

We note that over the past ten years there have been four different Chief Operating Officers at the Company, and there has not been a COO since 2012. In addition, the named executives in the Company's annual reports over the last decade demonstrate a level of turnover below the COO level that is equally troubling. We believe that Healthways' high level of turnover in senior management is symptomatic of poor leadership at both the CEO and Board level, and the fact that this turnover has been accompanied by terrible operating and financial performance makes it a glaring red flag.

WE ARE CONCERNED THAT EXECUTIVE COMPENSATION IS POORLY STRUCTURED AND NOT ALIGNED WITH PERFORMANCE

We believe management's ability to properly address the issues facing the Company is compromised by the misalignment between compensation and the Company's performance. In 2012, Institutional Stockholder Services (ISS) recommended against the Company's say-on-pay proposal due to a retention grant, duplicative performance metrics, and steadily increasing pay during declining performance. Following the Company's failed say-on-pay vote in 2012, Healthways' subsequent compensation changes still fell short of (ISS) standards and again ISS recommended stockholders vote "AGAINST" the Company's say-on-pay proposal at the 2013 Annual Meeting. According to ISS:

"The changes failed, however, to address the primary drivers of its pay-for-performance misalignment. Specifically, the company retains several practices that contribute significantly to the CEO's above-median compensation, even though executives failed to receive cash awards under the short- or long-term incentive programs…. Given the company's weak long-term performance and above-median pay, a vote AGAINST is warranted for a second year."

At the 2013 Annual Meeting, stockholders once again voted AGAINST the Company's say-on-pay proposal.

THE BOARD'S UNWAIVERING SUPPORT FOR MANAGEMENT IS TROUBLING

As fiduciaries, the Board has an obligation to all Healthways' stockholders to hold management accountable for the Company's long-term underperformance. As we highlighted in private and public letters to the Board, management has failed to meet its financial performance targets in six of the last ten years, including during each of the past three years, and four of the past six years. In conversations with Mr. Ballantine, we learned that instead of taking proactive steps to reverse Mr. Leedle's failures, the Board finds comfort in the fact that "management's compensation is aligned with performance, and since the company has not performed, bonuses have not been paid." We find the lack of accountability, as portrayed by this statement, unsettling. The Board's apparent tolerance for a CEO who has performed so poorly for so long causes us to fundamentally question whether Healthways is being run for the benefit of its stockholders.

WE ARE CONCERNED WITH THE LACK OF RELEVANT HEALTHCARE OPERATING EXPERIENCE ON THE BOARD

We believe there is a lack of meaningful relevant healthcare operating experience among the non-executive Directors at Healthways. The healthcare industry is complex, always changing, and requires a level of domain expertise that we believe is lacking on the Board today. Notably, the four directors up for election this year have no prior healthcare operating experience.

WE ARE CONCERNED WITH THE BOARD’S LACK OF SUFFICIENT STOCK OWNERSHIP

Collectively, the members of the Board directly own approximately [1.5%] of the outstanding shares of Common Stock, and the vast majority of such shares have been granted as stock options or restricted stock. The non-executive directors own approximately [0.8%] of the outstanding shares of Common Stock. In contrast, North Tide beneficially owns an aggregate of 3,850,000 shares of Common Stock, or close to 11% of the outstanding shares of Common Stock.

We also note that the Company’s outside directors each collected at least $100,000 in cash fees and over $200,000 in total compensation in 2013. It is worth noting that the members of the Board have purchased very few Healthways shares with their own money, despite the generous cash fees they have reaped as members of the Board.

We believe the Board’s collective lack of a substantial vested interest in shares of Healthways and the generous cash compensation paid to the outside directors may compromise the Board’s ability to properly evaluate and address the serious challenges facing the Company.

OUR FOUR NOMINEES HAVE THE EXPERIENCE, QUALIFICATIONS AND OBJECTIVITY NECESSARY TO FULLY EXPLORE AVAILABLE OPPORTUNITIES TO UNLOCK VALUE FOR STOCKHOLDERS

As Healthways’ second-largest stockholder, we have heightened concerns that the Board lacks the objectivity necessary to act in the best interest of stockholders. We have identified several highly qualified, independent directors with experience in the healthcare industry who we believe will bring a fresh perspective into the boardroom and would be extremely helpful in evaluating and executing on initiatives to unlock value at the Company.

We believe that the Board must be significantly reconfigured and view any attempt to increase the size of the current Board or the number of directors up for election at the Annual Meeting as an unlawful manipulation of Healthways’ corporate machinery.

Each of North Tide’s nominees has an exceptional track record and they collectively possess a well-balanced mix of skill sets to ensure that the Board (i) fulfills its duty to provide effective oversight of Healthways, (ii) determines the appropriate corporate strategy to create value for the benefit of all stockholders, and (iii) holds management accountable for executing against those objectives.

Edwin “Mac” Crawford most recently served as Chairman of CVS Caremark, a Fortune 20 company formed by the 2007 merger of CVS and Caremark Rx. From 1998-2007, Mr. Crawford was CEO of Caremark Rx (and its predecessor MedPartners Inc.). Mr. Crawford joined MedPartners in 1998 when the company, then the country’s largest physician practice management company, was struggling amid operating losses, significant debt obligations, and major changes in the healthcare industry. While Mr. Crawford was CEO, Caremark Rx sold certain assets and decided to strategically focus on the small but growing pharmacy benefits management (“PBM”) business. Caremark Rx’s PBM business enjoyed significantly increased revenues under Mr. Crawford’s watch as CEO* and was able to significantly lower its debt. In 2004, Caremark Rx acquired AdvancePCS, thereby making Caremark the second-largest PBM, with over $23 billion in annual revenue. By 2007, Caremark had grown to be a $37 billion PBM managing over 600 million prescriptions when Mr. Crawford, as CEO, led* Caremark Rx’s strategic merger with drug chain CVS in a transaction valued at approximately $27 billion. During Mr. Crawford’s nine-year tenure as CEO of Caremark Rx, the total stockholder return was +516% versus the S&P 500 Index total return of +52% and the S&P Healthcare Index total return of +47% over the same period*. Mr. Crawford was named Institutional Investor’s Best CEO in Healthcare Technology and Distribution for 2005, 2006 and 2007. Previously, Mr. Crawford was Chairman and CEO of Magellan Health Services, which he led through a successful restructuring and turnaround. Mr. Crawford currently serves on the Board of Trustees of Washington & Lee University. He graduated from Auburn University with a degree in Business and with a major in Accounting in 1971.

Bradley S. Karro is a principal of Hillcote Advisors, a firm focused on investing in and restructuring healthcare companies. Prior to founding Hillcote, Mr. Karro held a number of senior executive positions in the healthcare industry, including serving as Executive Vice President of Caremark Rx, a prescription benefit management company. Mr. Karro served at Caremark Rx from 1998 through 2007 and during his time at Caremark Rx, he was responsible for mergers & acquisitions, integration planning, information technology and Medicare product development. Mr. Karro was also appointed as a charter member of the Governor’s e-Health Advisory Council in Tennessee, an organization established to coordinate Tennessee’s initiatives leading towards the adoption of electronic medical records. Mr. Karro is currently a member of the Board of Directors of Angiotech Pharmaceuticals, Inc., where he chairs the Audit Committee. Mr. Karro previously served on the Board of Directors of Emageon Inc. Mr. Karro received his B.A. in Honors Business Administration from the University of Western Ontario.

Paul H. Keckley is the Editor of The Keckley Report and an expert on health industry trends and U.S. health system reform. In his thirty-five year health industry career, Dr. Keckley served as an expert commentator for national media coverage of healthcare reform, CEO of four health care companies funded by private investors, in senior management at Vanderbilt Medical Center and most recently as Executive Director of the Deloitte Center for Health Solutions in Washington, D.C, a position he held from 2006 through 2013. Dr. Keckley currently serves on the board of directors of the Healthcare Financial Management Leadership Council, Western Governors University Advisory Board and Lipscomb University College of Pharmacy. He previously served as an Independent Director at Ohio State University Medical Center, Interdent and PhyCor Inc. and as advisor to the Bipartisan Policy Center in Washington, DC. Dr. Keckley is a member of the Health Executive Network. He received his B.A. at Lipscomb University and his M.A. and PhD from Ohio State University and completed additional graduate studies at Oxford University.

Conan J. Laughlin is the Founder, Portfolio Manager, and Managing Member of North Tide Capital, a Boston-based investment firm with over $1 billion in assets under management. The firm invests in global equities utilizing a value-oriented approach with a dedicated focus on the healthcare sector. Mr. Laughlin has covered the healthcare industry as an equity research analyst since 1995. Prior to founding North Tide, from 2005-2011 Mr. Laughlin was a portfolio manager and sub-adviser to Millennium Management LLC, a multi-billion dollar investment firm based in New York. From 2002-2004, Mr. Laughlin was an equity research analyst covering the healthcare sector in the Asset Management group at American Express in Boston. Prior to joining American Express in 2002, he spent seven years as a sell-side analyst at Morgan Stanley Dean Witter (1995-1997), SG Cowen (1997-1999), and Deutsche Bank Alex. Brown (1999-2002). Mr. Laughlin graduated from the College of William and Mary with a BBA in Finance in 1995.

Mr. Laughlin currently serves on the Board of Trustees at The Park School in Brookline, MA.

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* While he was CEO of Caremark Rx during this time period, it cannot be said for certain to what extent Mr. Crawford was responsible for the actions or value enhancement at Caremark Rx during his tenure. There can be no assurance that the Company's business will enjoy similar results or improvements, or that stockholder value will similarly be enhanced, if Mr. Crawford is elected to the Board.

PROPOSAL NO. 1

ELECTION OF DIRECTORS

The Company currently has a classified Board, which is currently divided into three classes. The Board is in the process of declassification beginning with the directors elected at the Annual Meeting, who will serve terms expiring at the next annual meeting of stockholders. We believe that the terms of four (4) Class II directors expire at the Annual Meeting and that four (4) directors will be elected at the Annual Meeting. We are seeking your support at the Annual Meeting to elect our four (4) Nominees in opposition to the Company's four director nominees for terms ending in 2015. Your vote to elect such Nominees will have the legal effect of replacing four incumbent directors with the Nominees. If elected, such Nominees will represent a minority of the members of the Board, and therefore it is not guaranteed that they can implement the actions that they believe are necessary to enhance stockholder value.

THE NOMINEES

The following information sets forth the name, age, business address, present principal occupation, and employment and material occupations, positions, offices, or employments for the past five years of each of the Nominees. The nominations were made in a timely manner and in compliance with the applicable provisions of the Company's governing instruments. The specific experience, qualifications, attributes and skills that led us to conclude that the Nominees should serve as directors of the Company is set forth above in the section entitled "Reasons for the Solicitation." This information has been furnished to us by the Nominees. The Nominees are citizens of the United States of America.

Edwin "Mac" Crawford, age 65, is not currently employed. Mr. Crawford most recently served as Chairman of CVS Caremark, a Fortune 20 company formed by the 2007 merger of CVS and Caremark Rx. From 1998-2007, Mr. Crawford was CEO of Caremark Rx (and its predecessor MedPartners Inc.). Mr. Crawford joined MedPartners in 1998 when the company, then the country's largest physician practice management company, was struggling amid operating losses, significant debt obligations, and major changes in the healthcare industry. While Mr. Crawford was CEO, Caremark Rx sold certain assets and decided to strategically focus on the small but growing pharmacy benefits management ("PBM") business. Caremark Rx's PBM business enjoyed significantly increased revenues under Mr. Crawford's watch as CEO* and was able to significantly lower its debt. In 2004, Caremark Rx acquired AdvancePCS, thereby making Caremark the second-largest PBM, with over $23 billion in annual revenue. By 2007, Caremark had grown to be a $37 billion PBM managing over 600 million prescriptions when Mr. Crawford, as CEO, led* Caremark Rx's strategic merger with drug chain CVS in a transaction valued at approximately $27 billion. During Mr. Crawford's nine-year tenure as CEO of Caremark Rx, the total stockholder return was +516% versus the S&P 500 Index total return of +52% and the S&P Healthcare Index total return of +47% over the same period*. Mr. Crawford was named Institutional Investor's Best CEO in Healthcare Technology and Distribution for 2005, 2006 and 2007. Previously, Mr. Crawford was Chairman and CEO of Magellan Health Services, which he led through a successful restructuring and turnaround. Mr. Crawford currently serves on the Board of Trustees of Washington & Lee University. He graduated from Auburn University with a degree in Business and with a major in Accounting in 1971. Mr. Crawford's business address is c/o Crawford Holdings, LLC, 600 Hangar Lane, Nashville, Tennessee 37217. Mr. Crawford's extensive experience leading public and private companies within the healthcare industry, as well as his specific experience leading a Fortune 20 company from operating losses to an immensely successful strategic exit, would make him a valuable asset to the Board.

Bradley S. Karro, age 52, is a principal of Hillcote Advisors, a firm focused on investing in and restructuring healthcare companies that Mr. Karro founded in July 2008. Prior to starting Hillcote Advisors, Mr. Karro held a number of senior executive positions in the healthcare industry, including serving as Executive Vice President of Caremark Rx, a prescription benefit management company. Mr. Karro joined Medpartners (which changed its name to

Caremark Rx) in 1998, and served at Caremark Rx through 2007. During his time at Caremark Rx, Mr. Karro was responsible for mergers & acquisitions, integration planning, information technology and Medicare product development. Mr. Karro was also appointed as a charter member of the Governor's e-Health Advisory Council in Tennessee, an organization established to coordinate Tennessee's initiatives leading towards the adoption of electronic medical records. Mr. Karro is currently a member of the Board of Directors of Angiotech Pharmaceuticals, Inc., where he chairs the Audit Committee. Mr. Karro previously served on the Board of Directors of Emageon Inc. Mr. Karro received his B.A. in Honors Business Administration from the University of Western Ontario. Mr. Karro's address is 3800 Woodlawn Drive, Nashville, Tennessee 37215. Mr. Karro has over twenty-five years of healthcare industry experience, and his extensive knowledge of the healthcare industry, his executive management experience and prior public board experience would make him a valuable asset to the Board.

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* While he was CEO of Caremark Rx during this time period, it cannot be said for certain to what extent Mr. Crawford was responsible for the actions or value enhancement at Caremark Rx during his tenure. There can be no assurance that the Company's business will enjoy similar results or improvements, or that stockholder value will similarly be enhanced, if Mr. Crawford is elected to the Board.

Conan J. Laughlin, age 41, is the Founder, Portfolio Manager, and Managing Member of North Tide Capital, a Boston-based investment firm with over $1 billion in assets under management that Mr. Laughlin launched in September 2011. The firm invests in global equities utilizing a value-oriented approach with a dedicated focus on the healthcare sector. Mr. Laughlin has covered the healthcare industry as an equity research analyst since 1995. Prior to founding North Tide Capital, from 2005-2011, Mr. Laughlin was a portfolio manager and sub-adviser to Millennium Management LLC, a multi-billion dollar investment firm based in New York. From 2002-2004, Mr. Laughlin was a senior analyst covering the healthcare sector in the Asset Management group at American Express in Boston. Prior to joining American Express in 2002, he spent seven years as a sell-side analyst at Morgan Stanley Dean Witter (1995-1997), SG Cowen (1997-1999), and Deutsche Bank Alex. Brown (1999-2002). Mr. Laughlin received his B.B.A in Finance from the College of William and Mary. Mr. Laughlin currently serves on the Board of Trustees at The Park School in Brookline, MA. Mr. Laughlin's business address is c/o North Tide Capital LLC, 500 Boylston Street, Suite 310, Boston, Massachusetts 02116. Mr. Laughlin's extensive knowledge of the healthcare industry and experience managing investments in the healthcare sector would make him a valuable asset to the Board.

Paul H. Keckley, age 64, is the Editor of The Keckley Report, which Dr. Keckley began publishing in September 2013, and an expert on health industry trends and U.S. health system reform. In his thirty-five year health industry career, Dr. Keckley served as an expert commentator for national media coverage of healthcare reform, CEO of four health care companies funded by private investors, in senior management at Vanderbilt Medical Center and most recently as Executive Director of the Deloitte Center for Health Solutions in Washington, D.C, a position he held from 2006 through September 2013. Dr. Keckley currently serves on the Board of Directors of the Ohio State University Medical Center, Healthcare Financial Management Leadership Council, Western Governors University Advisory Board and Lipscomb University College of Pharmacy. Dr. Keckley is a member of the Health Executive Network and advisor to the Bipartisan Policy Center in Washington, D.C. Dr. Keckley received his B.A. from Lipscomb University and his M.A. and PhD from Ohio State University and completed a fellowship in economic policy at Oxford University. Dr. Keckley's address is 1115B Biltmore Drive, Nashville, Tennessee 37204. Dr. Keckley's extensive involvement with the healthcare industry as well as his executive leadership experience in the public and private sectors would make him a valuable asset to the Board.

As of the date hereof, Mr. Laughlin, by virtue of his relationship with North Tide Capital, which is the investment manager of North Tide Master as well as a certain managed account (the "Account"), may be deemed the beneficial owner of the 3,850,000 shares of Common Stock owned in the aggregate by North Tide Master and the Account. Mr. Laughlin disclaims beneficial ownership of such shares of Common Stock, except to the extent of his pecuniary interest therein. Mr. Laughlin has not entered into any transactions in the shares of Common Stock in the past two years. For information regarding purchases and sales during the past two years by North Tide Master and the Account in securities of the Company, see Schedule I.

As of the date hereof, none of Messrs. Crawford, Karro or Dr. Keckley owns beneficially or of record any securities of the Company, and none has made any direct purchases or sales of any securities of the Company during the past two years.

North Tide Capital and certain of its affiliates have signed letter agreements, pursuant to which they agree to indemnify each of Messrs. Crawford, Karro and Dr. Keckley against claims arising from the solicitation of proxies from the Company stockholders in connection with the Annual Meeting and any related transactions.

On February 28, 2014, the North Tide Master, North Tide Capital and the Nominees (collectively the "Group") entered into a Joint Filing and Solicitation Agreement in which, among other things, (a) the Group agreed to the joint filing on behalf of each of them of statements on Schedule 13D with respect to the securities of the Company, (b) the Group agreed to solicit proxies or written consents for the election of the Nominees at the 2014 Annual Meeting (the "Solicitation"), and (c) North Tide Capital agreed to bear all expenses incurred in connection with the Solicitation, including approved expenses incurred by any of the parties in connection with the Solicitation, subject to certain limitations.

Other than as stated herein, there are no arrangements or understandings between members of North Tide Master and any of the Nominees or any other person or persons pursuant to which the nomination of the Nominees described herein is to be made, other than the consent by each of the Nominees to be named in this Proxy Statement and to serve as a director of the Company if elected as such at the Annual Meeting. None of the Nominees is a party adverse to the Company or any of its subsidiaries or has a material interest adverse to the Company or any of its subsidiaries in any material pending legal proceedings.

Each Nominee presently is, and if elected as a director of the Company, each of the Nominees would be, an "independent director" within the meaning of (i) applicable NASDAQ Global Select Market listing standards applicable to board composition, and (ii) Section 301 of the Sarbanes-Oxley Act of 2002. No Nominee is a member of the Company's compensation, nominating or audit committee that is not independent under any such committee's applicable independence standards.

We do not expect that the Nominees will be unable to stand for election, but, in the event any Nominee is unable to serve or for good cause will not serve, the shares of Common Stock represented by the enclosed BLUE proxy card will be voted for substitute nominee(s), to the extent this is not prohibited under the Bylaws and applicable law. In addition, we reserve the right to nominate substitute person(s) if the Company makes or announces any changes to its Bylaws or takes or announces any other action that has, or if consummated would have, the effect of disqualifying any Nominee, to the extent this is not prohibited under the Bylaws and applicable law. In any such case, shares of Common Stock represented by the enclosed BLUE proxy card will be voted for such substitute nominee(s). We reserve the right to nominate additional person(s), to the extent this is not prohibited under the Bylaws and applicable law, if the Company increases the size of the Board above its existing size or increases the number of directors whose terms expire at the Annual Meeting. Additional nominations made pursuant to the preceding sentence are without prejudice to the position of North Tide that any attempt to increase the size of the current Board or to reconstitute or reconfigure the classes on which the current directors serve constitutes an unlawful manipulation of the Company's corporate machinery.

WE URGE YOU TO VOTE FOR THE ELECTION OF THE NOMINEES ON THE ENCLOSED BLUE PROXY CARD.

PROPOSAL NO. 2

ADVISORY VOTE TO APPROVE EXECUTIVE COMPENSATION

As discussed in further detail in the Company's proxy statement, the Company is asking stockholders to indicate their support for the compensation of the Company's named executive officers. This proposal, commonly known as a "say-on-pay" proposal, is not intended to address any specific item of compensation, but rather the overall compensation of the Company's named executive officers and the philosophy, policies and practices described in the Company's proxy statement. Accordingly, the Company is asking stockholders to vote for the following resolution:

"RESOLVED, that the Company's stockholders approve, on an advisory basis, the compensation of the NEOs, as disclosed in the Company's Proxy Statement for the 2014 Annual Meeting of Stockholders pursuant to the compensation disclosure rules of the Securities and Exchange Commission, including the Compensation Discussion and Analysis, the 2013 Summary Compensation Table and the other related tables and disclosures."

According to the Company's proxy statement, the stockholder vote on the Say-on-Pay Proposal is an advisory vote only, and it is not binding on the Company, the Board, or the Compensation Committee of the Board.

WE MAKE NO RECOMMENDATION WITH RESPECT TO THIS PROPOSAL AND INTEND TO VOTE OUR SHARES ["FOR"/ "AGAINST"] THIS PROPOSAL.

PROPOSAL NO. 3

RATIFICATION OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

As discussed in further detail in the Company's proxy statement, the Audit Committee of the Board has appointed Ernst & Young LLP as the Company's independent registered public accounting firm to audit the Company's financial statements for the fiscal year ending December 31, 2014. The Company is submitting the appointment of Ernst & Young LLP for ratification by the stockholders at the Annual Meeting.

WE MAKE NO RECOMMENDATION WITH RESPECT TO THE RATIFICATION OF THE APPOINTMENT OF ERNST & YOUNG LLP AS THE COMPANY'S INDEPENDENT AUDITOR FOR THE 2014 FISCAL YEAR AND INTEND TO VOTE OUR SHARES ["FOR"] THIS PROPOSAL.

PROPOSAL NO. 4

APPROVAL OF THE COMPANY'S 2014 STOCK INCENTIVE PLAN

As discussed in further detail in the Company's proxy statement, the Board has adopted the Company's 2014 Stock Incentive Plan, effective as of June 24, 2014, subject to the approval of the Company's stockholders at the Annual Meeting. A summary of the key provisions and principal features of the 2014 Stock Incentive Plan and the full text of the 2014 Stock Incentive Plan are made part of the Company's proxy statement.

WE MAKE NO RECOMMENDATION WITH RESPECT TO THE APPROVAL OF THE COMPANY'S 2014 STOCK INCENTIVE PLAN AND INTEND TO VOTE OUR SHARES ["FOR"/"AGAINST"] THIS PROPOSAL.

PROPOSAL NO. 5

AMENDMENT TO BYLAWS TO IMPLEMENT MAJORITY VOTING FOR
UNCONTESTED ELECTIONS OF DIRECTORS

As discussed in further detail in the Company's proxy statement, the Board has proposed to amend the Company's Bylaws to implement a majority voting standard for uncontested director elections.

Under a majority voting standard, each vote is specifically counted "for" or "against" the director's election. An affirmative majority of the total number of votes cast "for" a director nominee will be required for election. Abstentions and broker non-votes will have no effect in determining whether the required affirmative majority vote has been obtained. Director nominees in contested elections would continue to be elected by plurality vote. A contested election is one in which the number of director nominees exceeds the number of directors to be elected.

WE MAKE NO RECOMMENDATION WITH RESPECT TO THE APPROVAL OF THE AMENDMENT TO THE BYLAWS TO IMPLEMENT MAJORITY VOTING FOR UNCONTESTED ELECTIONS OF DIRECTORS INTEND TO VOTE OUR SHARES [“FOR”] THIS PROPOSAL.

VOTING AND PROXY PROCEDURES

Only stockholders of record on the Record Date will be entitled to notice of and to vote at the Annual Meeting. Stockholders who sell their shares of Common Stock before the Record Date (or acquire them without voting rights after the Record Date) may not vote such shares of Common Stock. Stockholders of record on the Record Date will retain their voting rights in connection with the Annual Meeting even if they sell such shares of Common Stock after the Record Date. Based on publicly available information, North Tide believes that the only outstanding class of securities of the Company entitled to vote at the Annual Meeting is the shares of Common Stock.

Shares of Common Stock represented by properly executed BLUE proxy cards will be voted at the Annual Meeting as marked and, in the absence of specific instructions, will be voted FOR the election of the Nominees, [FOR/AGAINST] the approval of the Say-on-Pay Proposal, [FOR] the ratification of Ernst & Young LLP as the Company's independent auditor for the 2014 fiscal year, [FOR/AGAINST] the approval of the 2014 Stock Incentive Plan, and [FOR] approval of an amendment to the Company's Bylaws, as amended, to implement majority voting for uncontested elections of directors, as described herein.

You are being asked to elect the Nominees. According to the Company's proxy statement for the Annual Meeting, the current Board intends to nominate four candidates for election as directors at the Annual Meeting. This Proxy Statement is soliciting proxies to elect only our Nominees. Accordingly, the enclosed BLUE proxy card may only be voted for the Nominees and does not confer voting power with respect to the Company's nominees. The participants in this solicitation intend to vote all of their Shares in favor of the Nominees.

QUORUM; BROKER NON-VOTES; DISCRETIONARY VOTING

A quorum is the minimum number of shares of Common Stock that must be represented at a duly called meeting in person or by proxy in order to legally conduct business at the meeting. For the Annual Meeting, the presence, in person or by proxy, of a majority of the outstanding shares entitled to vote will be considered a quorum, allowing votes to be taken and counted for the matters before the stockholders.

Abstentions will be counted as present for the purpose of determining the presence of a quorum. Broker non-votes will not be counted for the purpose of determining the presence of a quorum, as they are not shares entitled to vote.

If you are a stockholder of record, you must deliver your vote by mail or attend the Annual Meeting in person and vote in order to be counted in the determination of a quorum. If you are a beneficial owner, your broker will vote your shares pursuant to your instructions, and those shares will count in the determination of a quorum. As further described below, brokers do not have discretionary authority to vote on any of the matters to be presented at the Annual Meeting. Accordingly, unless you vote via proxy card or provide instructions to your broker, your shares of Common Stock will not count for purposes of attaining a quorum.

Generally, broker non-votes occur when shares held by a broker in "street name" for a beneficial owner are not voted with respect to a particular proposal because (1) the broker has not received voting instructions from the beneficial owner and (2) the broker lacks discretionary voting power to vote those shares. Usually, a broker is entitled to vote shares held for a beneficial owner on routine matters, such as the ratification of the appointment of Ernst & Young LLP as independent registered public accounting firm, without instructions from the beneficial owner of those shares. However, because this is a contested election, it is likely that none of the proposals at the Annual Meeting will be considered a "routine" matter, and, therefore, your shares will not be voted on any matter unless you instruct your brokerage firm to vote in a timely manner. As there will likely be no "routine" matters at the Annual Meeting, broker non-votes will have no effect on the outcome of any of the proposals presented at the Annual Meeting. Abstentions will have the same effect as a vote "AGAINST" each of the proposals presented at the Annual Meeting, except for the election of directors, with respect to which abstentions will have no effect.

VOTES REQUIRED FOR APPROVAL

Election of Directors According to the Company's proxy statement, the four nominees for director receiving the highest vote totals will be elected as directors of the Company. With respect to the election of directors, a properly executed proxy card marked "WITHHOLD" with respect to the election of a director nominee will be counted for purposes of determining if there is a quorum at the Annual Meeting, but will not be considered to have been voted for the director nominees. Broker non-votes (as discussed above) will also not be considered to have been voted for any director nominee. Therefore, abstentions and broker non-votes will have no direct effect on the outcome of the election of directors.

Other Proposals Other than for the approval of the Say-on-Pay Proposal and ratification of Ernst & Young LLP as the Company's independent auditor for the 2014 fiscal year, the affirmative vote of a majority of the Common Stock represented at the Annual Meeting will be required to approve the other proposals. Stockholders may vote "FOR" or "AGAINST" or may "ABSTAIN" from voting on each of these proposals. If you "ABSTAIN," it will have the same effect as a vote "AGAINST" these proposals. Broker non-votes (as discussed above) will not be considered to have been voted for any of these proposals. If you sign and submit your BLUE proxy card without specifying how you would like your shares voted, your shares will be voted in accordance with North Tide's recommendations specified herein and in accordance with the discretion of the persons named on the BLUE proxy card with respect to any other matters that may be voted upon at the Annual Meeting.

REVOCATION OF PROXIES

Stockholders of the Company may revoke their proxies at any time prior to exercise by attending the Annual Meeting and voting in person (although attendance at the Annual Meeting will not in and of itself constitute revocation of a proxy) or by delivering a written notice of revocation. The delivery of a subsequently dated proxy which is properly completed will constitute a revocation of any earlier proxy. The revocation may be delivered either to North Tide in care of Okapi Partners at the address set forth on the back cover of this Proxy Statement or to the Company at 701 Cool Springs Boulevard, Franklin, Tennessee 37067 or any other address provided by the Company. Although a revocation is effective if delivered to the Company, we request that either the original or photostatic copies of all revocations be mailed to North Tide in care of Okapi Partners at the address set forth on the back cover of this Proxy Statement so that we will be aware of all revocations and can more accurately determine if and when proxies have been received from the holders of record on the Record Date of a majority of the outstanding shares of Common Stock. Additionally, Okapi Partners may use this information to contact stockholders who have revoked their proxies in order to solicit later dated proxies for the election of the Nominees.

IF YOU WISH TO VOTE FOR THE ELECTION OF THE NOMINEES TO THE BOARD, PLEASE SIGN, DATE AND RETURN PROMPTLY THE ENCLOSED BLUE PROXY CARD IN THE POSTAGE-PAID ENVELOPE

PROVIDED.

SOLICITATION OF PROXIES

The solicitation of proxies pursuant to this Proxy Statement is being made by North Tide Capital. Proxies may be solicited by mail, facsimile, telephone, telegraph, Internet, in person and by advertisements.

North Tide Capital has entered into an agreement with Okapi Partners for solicitation and advisory services in connection with this solicitation, for which Okapi Partners will receive a fee not to exceed $_________, together with reimbursement for its reasonable out-of-pocket expenses, and will be indemnified against certain liabilities and expenses, including certain liabilities under the federal securities laws. Okapi Partners will solicit proxies from individuals, brokers, banks, bank nominees and other institutional holders. North Tide Capital has requested banks, brokerage houses and other custodians, nominees and fiduciaries to forward all solicitation materials to the beneficial owners of the shares of Common Stock they hold of record. North Tide Capital will reimburse these record holders for their reasonable out-of-pocket expenses in so doing. It is anticipated that Okapi Partners will employ approximately ____ persons to solicit stockholders for the Annual Meeting.

The entire expense of soliciting proxies is being borne by North Tide Capital. Costs of this solicitation of proxies are currently estimated to be approximately $___________. North Tide Capital estimates that through the date hereof its expenses in connection with this solicitation are approximately $75,000. North Tide Capital intends to seek reimbursement from the Company of all expenses it incurs in connection with this solicitation. North Tide Capital does not intend to submit the question of such reimbursement to a vote of security holders of the Company.

ADDITIONAL PARTICIPANT INFORMATION

The Nominees and the members of North Tide are participants in this solicitation. The principal business of North Tide Master is serving as a private investment fund. North Tide Master has been formed for the purpose of making equity investments and, on occasion, taking an active role in the management of portfolio companies in order to enhance stockholder value. North Tide Capital provides investment advisory and management services and acts as the investment manager of North Tide Master and the Account.

The address of the principal office of each of North Tide Capital and North Tide Master is 500 Boylston Street, Suite 310, Boston, Massachusetts 02116.

As of the date hereof, North Tide Master directly 3,425,000 shares of Common Stock. As of the date hereof, North Tide Capital, as the investment manager of North Tide Master and the Account, may be deemed to beneficially own the 3,425,000 shares of Common Stock directly owned by North Tide Master and 425,000 shares of Common Stock beneficially owned by the Account.

For information regarding purchases and sales of securities of the Company during the past two years by the participants in this solicitation, see Schedule I.

The shares of Common Stock directly owned by North Tide Master and held in the Account were purchased with working capital (which may, at any given time, include margin loans made by brokerage firms in the ordinary course of business).

Except as set forth in this Proxy Statement (including the Schedules hereto), (i) during the past 10 years, no participant in this solicitation has been convicted in a criminal proceeding (excluding traffic violations or similar misdemeanors); (ii) no participant in this solicitation directly or indirectly beneficially owns any securities of the Company; (iii) no participant in this solicitation owns any securities of the Company which are owned of record but not beneficially; (iv) no participant in this solicitation has purchased or sold any securities of the Company during the past two years; (v) no part of the purchase price or market value of the securities of the Company owned by any participant in this solicitation is represented by funds borrowed or otherwise obtained for the purpose of acquiring or holding such securities; (vi) no participant in this solicitation is, or within the past year was, a party to any contract, arrangements or understandings with any person with respect to any securities of the Company, including, but not limited to, joint ventures, loan or option arrangements, puts or calls, guarantees against loss or guarantees of profit, division of losses or profits, or the giving or withholding of proxies; (vii) no associate of any participant in this solicitation owns beneficially, directly or indirectly, any securities of the Company; (viii) no participant in this solicitation owns beneficially, directly or indirectly, any securities of any parent or subsidiary of the Company; (ix) no participant in this solicitation or any of his or its associates was a party to any transaction, or series of similar transactions, since the beginning of the Company's last fiscal year, or is a party to any currently proposed transaction, or series of similar transactions, to which the Company or any of its subsidiaries was or is to be a party, in which the amount involved exceeds $120,000; (x) no participant in this solicitation or any of his or its associates has any arrangement or understanding with any person with respect to any future employment by the Company or its affiliates, or with respect to any future transactions to which the Company or any of its affiliates will or may be a party; and (xi) no participant in this solicitation has a substantial interest, direct or indirect, by securities holdings or otherwise in any matter to be

acted on at the Annual Meeting.

There are no material proceedings to which any participant in this solicitation or any of his or its associates is a party adverse to the Company or any of its subsidiaries or has a material interest adverse to the Company or any of its subsidiaries. With respect to each of the Nominees, none of the events enumerated in Item 401(f)(1)-(8) of Regulation S-K of the Exchange Act occurred during the past ten years.

OTHER MATTERS AND ADDITIONAL INFORMATION

North Tide is unaware of any other matters to be considered at the Annual Meeting. However, should other matters, which North Tide is not aware of a reasonable time before this solicitation, be brought before the Annual Meeting, the persons named as proxies on the enclosed BLUE proxy card will vote on such matters in their discretion.

STOCKHOLDER PROPOSALS

The Company's 2015 annual meeting of stockholders (the "2015 Annual Meeting") is expected to be held in May 2015, although this date may be subject to change. Stockholders' proposals will be eligible for consideration for inclusion in the Company's proxy statement for the 2015 Annual Meeting pursuant to Rule 14a-8 under the Securities Exchange Act of 1934, as amended, if such proposals are received by the Company at 701 Cool Springs Blvd., Franklin, Tennessee, 37067, addressed to the Company's Secretary before the close of business on [ ], 2015. Notices of stockholders' proposals (including nominations) submitted outside the processes of Rule 14a-8 will generally be considered timely (but not considered for inclusion in the Company's proxy statement), pursuant to the advance notice requirement set forth in the Company's bylaws, if such notices are filed with the Company's Secretary not less than 90 days nor more than 120 days prior to the first anniversary of this year's Annual Meeting (i.e., not earlier than February 24, 2015 and not later than March 26, 2015); provided, however, that in the event that the date of the 2015 Annual Meeting is advanced by more than 30 days or delayed by more than 60 days from such anniversary date, notice by the stockholder to be timely must be so delivered not earlier than the 120th day prior to such annual meeting and not later than the close of business on the later of the 90th day prior to such annual meeting or the 10th day following the day on which public announcement of the date of such meeting is first made. For proposals that are timely filed, the named proxies will retain discretion to vote proxies that the Company receives, provided: (1) the Company includes in its proxy statement advice on the nature of the proposal and how the named proxies intend to exercise their voting discretion and (2) the proponent does not issue a proxy statement. In order to curtail any controversy as to the date on which the Company received a proposal, the Company suggests that stockholders submit their proposals by certified mail, return receipt requested. Nothing in this paragraph shall be deemed to require the Company to include any stockholder proposal that does not meet all of the requirements for such inclusion established by the SEC at the time in effect.

The information set forth above regarding the procedures for submitting stockholder proposals for consideration at the 2015 Annual Meeting is based on information contained in the Company's proxy statement. The incorporation of this information in this proxy statement should not be construed as an admission by North Tide that such procedures are legal, valid or binding.

INCORPORATION BY REFERENCE

WE HAVE OMITTED FROM THIS PROXY STATEMENT CERTAIN DISCLOSURE REQUIRED BY APPLICABLE LAW THAT IS EXPECTED TO BE INCLUDED IN THE COMPANY'S PROXY STATEMENT RELATING TO THE ANNUAL MEETING. THIS DISCLOSURE IS EXPECTED TO INCLUDE, AMONG OTHER THINGS, CURRENT BIOGRAPHICAL INFORMATION ON THE COMPANY'S DIRECTORS, INFORMATION CONCERNING EXECUTIVE COMPENSATION, AND OTHER IMPORTANT INFORMATION. SEE SCHEDULE II FOR INFORMATION REGARDING PERSONS WHO BENEFICIALLY OWN MORE THAN 5% OF THE SHARES AND THE OWNERSHIP OF THE SHARES BY THE DIRECTORS

AND MANAGEMENT OF THE COMPANY.

The information concerning the Company contained in this Proxy Statement and the Schedules attached hereto has been taken from, or is based upon, publicly available information.

NORTH TIDE CAPITAL MASTER, LP

__________, 2014

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SCHEDULE I

TRANSACTIONS IN SECURITIES OF THE COMPANY
DURING THE PAST TWO YEARS

Shares of Common Stock Purchased / (Sold)	Date of Transaction
NORTH TIDE MASTER	
301	03/02/2012
301	03/02/2012
7,183	04/12/2012
7,183	04/12/2012
5,317	04/12/2012
5,317	04/12/2012
2,250	04/23/2012
2,250	04/23/2012
7,225	04/24/2012
7,225	04/24/2012
3,025	04/25/2012
3,025	04/25/2012
25,000	06/01/2012
25,000	06/01/2012
25,000	06/04/2012
25,000	06/04/2012
25,000	06/05/2012
25,000	06/05/2012
25,000	07/17/2012
25,000	07/17/2012
25,000	10/19/2012
25,000	10/19/2012
25,000	10/19/2012
25,000	10/19/2012
25,000	11/01/2012
25,000	11/01/2012
12,500	11/13/2012
12,500	11/13/2012
12,500	11/14/2012
12,500	11/14/2012
12,500	12/03/2012
12,500	12/03/2012
12,500	12/04/2012
12,500	12/04/2012
25,000	12/05/2012
25,000	12/05/2012
12,500	12/06/2012
12,500	12/06/2012

12,500	12/07/2012
12,500	12/07/2012

65,000	12/07/2012
65,000	12/07/2012
10,000	12/10/2012
10,000	12/10/2012
12,500	12/11/2012
12,500	12/11/2012
111	12/11/2012
111	12/11/2012
22,502	12/11/2012
22,500	12/11/2012
14,887	12/12/2012
14,889	12/12/2012
100,000	12/17/2012
100,000	12/17/2012
25,000	01/03/2013
25,000	01/03/2013
25,000	01/07/2013
25,000	01/07/2013
12,500	01/17/2013
12,500	01/17/2013
25,000	01/18/2013
25,000	01/18/2013
25,000	02/11/2013
25,000	02/11/2013
9,287	02/12/2013
9,287	02/12/2013
8,825	02/12/2013
8,823	02/12/2013
32,646	02/13/2013
32,648	02/13/2013
22,000	02/14/2013
22,000	02/14/2013
14,742	02/15/2013
14,742	02/15/2013
53,900	07/08/2013
53,900	07/08/2013
46,100	07/09/2013
46,100	07/09/2013
100,000	07/18/2013
100,000	07/18/2013
50,000	09/12/2013
50,000	09/12/2013
28,751	09/13/2013
28,749	09/13/2013
21,250	09/16/2013
21,250	09/16/2013
25,000	09/20/2013
25,000	09/20/2013
22,350	09/23/2013

22,350	09/23/2013

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201	09/23/2013
199	09/23/2013
2,449	09/24/2013
2,451	09/24/2013
50,000	10/03/2013
50,000	10/03/2013
25,000	10/08/2013
25,000	10/08/2013
25,000	10/09/2013
25,000	10/09/2013
200,000	10/25/2013
200,000	10/25/2013
155,000	12/09/2013
155,000	12/09/2013
3,580	12/17/2013
3,579	12/17/2013
41,420	12/17/2013
41,421	12/17/2013
12,500	12/18/2013
12,500	12/18/2013

NORTH TIDE CAPITAL
(Through the Managed Account)

60,642	11/17/2011
18,858	11/18/2011
1,700	12/05/2011
35,000	12/05/2011
1,250	02/16/2012
2,844	02/16/2012
95,906	02/16/2012
24,809	02/21/2012
25,193	02/22/2012
8,798	03/02/2012
14,366	04/12/2012
10,634	04/12/2012
4,500	04/23/2012
14,450	04/24/2012
6,050	04/25/2012
10,000	05/22/2012
(50,000)	07/17/2012
(10,000)	08/03/2012
25,000	09/24/2012
25,000	09/25/2012
25,000	09/26/2012
25,000	09/27/2012
25,000	09/28/2012
37,500	10/19/2012
25,000	10/19/2012

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17,500	11/13/2012
(130,000)	12/07/2012
10,000	12/11/2012
78	12/11/2012
14,998	12/11/2012
9,924	12/12/2012
60,000	12/17/2012
5,000	12/26/2012
49,800	01/14/2013
200	01/14/2013
25,000	01/17/2013
6,426	02/12/2013
7,352	02/12/2013
27,206	02/13/2013
15,300	02/14/2013
18,716	02/15/2013
(200,000)	07/18/2013
25,000	12/18/2013

SCHEDULE II

The following table is reprinted from the definitive proxy statement filed by Healthways, Inc. with the Securities and Exchange Commission on April 14, 2014.

Security Ownership of Certain Beneficial Owners and Management

The following table sets forth certain information with respect to those persons that we know to be the beneficial owners (as defined by Rule 13d-3 under the Securities Exchange Act of 1934, as amended) of more than 5% of our Common Stock, our only voting security, and with respect to the beneficial ownership of our Common Stock by all directors and nominees, each of the executive officers named in the Summary Compensation Table and all of our executive officers and directors as a group. The information set forth below is based on ownership information we received as of April 10, 2014 (except as otherwise noted below). Unless specified otherwise, the shares indicated are presently outstanding, and each of the stockholders listed below has sole voting and investment power with respect to the shares beneficially owned.

Name and Address of Beneficial Owner	Amount and Nature of Beneficial Ownership (1)		Percent of Class (1)	
Prudential Financial, Inc. 751 Broad Street Newark, NJ 07102-3777	5,568,014	(2)	15.80	%
North Tide Capital, LLC 500 Boylston Street Suite 310 Boston, MA 02116	3,850,000	(3)	10.93	%
BlackRock, Inc. 40 East 52nd Street New York, NY 10022	3,254,885	(4)	9.24	%
EARNEST Partners, LLC 1180 Peachtree Street NE Suite 2300 Atlanta, GA 30309	2,756,961	(5)	7.82	%
The Vanguard Group 100 Vanguard Boulevard Malvern, PA 19355	2,110,311	(6)	5.99	%

Dimensional Fund Advisors LP Palisades West, Building One 6300 Bee Cave Road Austin, TX 78746	1,933,320	(7)	5.49	%
Wells Fargo & Company 420 Montgomery Street San Francisco, CA 94104	1,878,623	(8)	5.33	%
Ben R. Leedle, Jr.****	1,242,814	(9)	3.43	%
Michael Farris***	389,932	(10)	1.11	%
Alfred Lumsdaine***	147,579	(11)	*	
Daniel J. Englander**	115,000	(12)	*	
C. Warren Neel, Ph.D**	97,105	(13)	*	
Peter Choueiri***	92,486	(14)	*	
John W. Ballantine**	72,475	(15)	*	
Mary Jane England, M.D.**	65,611	(16)	*	
Jay C. Bisgard, M.D.**	64,624	(17)	*	
Alison Taunton-Rigby, Ph. D.**	55,919	(18)	*	
John A. Wickens**	57,475	(19)	*	
Glenn Hargreaves***	49,520	(20)	*	
William D. Novelli**	31,191	(21)	*	
Mary Flipse***	14,674	(22)	*	
Kevin G. Wills**	9,132	(23)	*	
Donato Tramuto**	7,950	(24)	*	
All directors and executive officers as a group (16 persons)	2,511,762	(25)	6.84	%

*	Indicates ownership of less than one percent of our outstanding Common Stock
**	Director of the Company
***	Named Executive Officer
****	Director and Named Executive Officer

(1) Pursuant to the rules of the Commission, certain shares of our Common Stock that an individual owner set forth in this table has a right to acquire within 60 days after April 10, 2014 pursuant to the exercise of options to purchase shares of Common Stock ("stock options") or other securities are deemed to be outstanding for the purpose of computing the ownership of that owner, but are not deemed outstanding for the purpose of computing the ownership of any other individual owner shown in the table. Likewise, the shares subject to stock options or other securities held by our other directors and executive officers that are exercisable within 60 days of April 10, 2014 are all deemed outstanding for the purpose of computing the percentage ownership of all executive officers and directors as a group.

(2) Information with respect to stock ownership is based on a Schedule 13G/A filed by Prudential Financial, Inc. ("Prudential") with the Commission on January 29, 2014 and includes shares held by certain of its subsidiaries, including Jennison Associates LLC ("Jennison"). Includes 105,304 shares to which Prudential has sole voting power, 5,462,710 shares to which Prudential has shared voting power, 105,304 shares to which Prudential has sole investment power and 5,462,710 shares to which Prudential has shared investment power. Jennison filed a separate Schedule13G/A with the Commission on February 12, 2014 reporting beneficial ownership of 5,477,265 shares to which Jennison has sole voting power and shared investment power. These shares have not been listed separately because they are included in the shares reported by Prudential, which indirectly owns 100% of the equity interests of Jennison. The address of Jennison is 466 Lexington Avenue, New York, New York 10017.

(3) Information with respect to stock ownership is based on a Schedule 13D/A filed with the Commission on March 3, 2014. Includes 3,850,000 shares to which North Tide Capital, LLC has shared voting and investment power. Includes 3,425,000 shares to which North Tide Capital Master, LP has shared voting and investment power. Includes 3,850,000 shares to which Conan Laughlin, who serves as the Manager of North Tide Capital, LLC, has shared voting and investment power. The address of North Tide Capital Master, LP and Conan Laughlin is 500 Boylston Street, Suite 310, Boston, Massachusetts, 02116.

(4) Information with respect to stock ownership is based on a Schedule 13G/A filed by BlackRock, Inc. with the Commission on January 29, 2014 and includes shares held by certain of its subsidiaries. Includes 3,142,378 shares to which BlackRock, Inc. has sole voting power and 3,254,885 shares to which BlackRock, Inc. has sole investment power.

(5) Information with respect to stock ownership is based on a Schedule 13G/A filed with the Commission on February 14, 2014. Includes 1,164,444 shares to which EARNEST Partners, LLC ("EARNEST") has sole voting power, 379,742 shares to which EARNEST has shared voting power and 2,756,961 shares to which EARNEST has sole investment power.

(6) Information with respect to stock ownership is based on a Schedule 13G/A filed by The Vanguard Group, Inc. ("Vanguard") with the Commission on February 11, 2014 and includes shares held by certain of its subsidiaries. Includes 54,994 shares to which Vanguard has sole voting power, 2,057,217 shares to which Vanguard has sole investment power and 53,094 shares to which Vanguard has shared investment power.

(7) Information with respect to stock ownership is based on a Schedule 13G filed with the Commission on February 10, 2014. Includes 1,865,966 shares to which Dimensional Fund Advisors LP ("Dimensional") has sole voting power and 1,933,320 shares to which Dimensional has shared investment power.

(8) Information with respect to stock ownership is based on a Schedule 13G/A filed by Wells Fargo & Company ("WFC") with the Commission on January 28, 2014 and includes shares held by certain of its subsidiaries. Includes 116 shares to which WFC has sole voting power, 1,873,010 shares to which WFC has shared voting power, 116 shares to which WFC has sole investment power and 1,878,507 shares to which WFC has shared investment power.

(9) Includes 985,916 shares that, as of April 10, 2014, were issuable upon the exercise of outstanding stock options within 60 days after April 10, 2014.

(10) Includes 389,611 shares held in trust.

(11) Includes 113,567 shares that, as of April 10, 2014, were issuable upon the exercise of outstanding stock options within 60 days after April 10, 2014.

(12) Consists of 115,000 shares held indirectly with Ursula Capital Partners, of which Mr. Englander is the Managing Partner. Mr. Englander disclaims beneficial ownership of these securities except to the extent of his pecuniary interest therein.

(13) Includes 43,764 shares that, as of April 10, 2014, were issuable upon the exercise of outstanding stock options within 60 days after April 10, 2014.

(14) Includes 74,754 shares that, as of April 10, 2014, were issuable upon the exercise of outstanding stock options within 60 days after April 10, 2014.

(15) Includes 43,764 shares that, as of April 10, 2014, were issuable upon the exercise of outstanding stock options within 60 days after April 10, 2014, and 20,000 shares held in trust.

(16) Includes 53,764 shares that, as of April 10, 2014, were issuable upon the exercise of outstanding stock options within 60 days after April 10, 2014.

(17) Includes 43,764 shares that, as of April 10, 2014, were issuable upon the exercise of outstanding stock options within 60 days after April 10, 2014, and 20,860 shares held in trust.

(18) Includes 33,764 shares that, as of April 10, 2014, were issuable upon the exercise of outstanding stock options within 60 days after April 10, 2014.

(19) Includes 43,764 shares that, as of April 10, 2014, were issuable upon the exercise of outstanding stock options within 60 days after April 10, 2014, and 1,100 shares held jointly by Mr. Wickens and his spouse.

(20) Includes 40,497 shares that, as of April 10, 2014, were issuable upon the exercise of outstanding stock options within 60 days after April 10, 2014.

(21) Includes 27,724 shares that, as of April 10, 2014, were issuable upon the exercise of outstanding stock options within 60 days after April 10, 2014.

(22) Includes 11,784 shares that, as of April 10, 2014, were issuable upon the exercise of outstanding stock options within 60 days after April 10, 2014.

(23) Consists of 9,132 shares that, as of April 10, 2014, were issuable upon the exercise of outstanding stock options within 60 days after April 10, 2014.

(24) Includes 3,750 shares that, as of April 10, 2014, were issuable upon the exercise of outstanding stock options within 60 days after April 10, 2014.

(25) Includes 1,529,708 shares that, as of April 10, 2014, were issuable upon the exercise of outstanding stock options within 60 days after April 10, 2014.

IMPORTANT

Tell your Board what you think! Your vote is important. No matter how many shares of Common Stock you own, please give North Tide your proxy FOR the election of the Nominees by taking three steps:

SIGNING the enclosed BLUE proxy card,

DATING the enclosed BLUE proxy card, and

MAILING the enclosed BLUE proxy card TODAY in the envelope provided (no postage is required if mailed in the United States).

If any of your shares of Common Stock are held in the name of a brokerage firm, bank, bank nominee or other institution, only it can vote such shares of Common Stock and only upon receipt of your specific instructions. Depending upon your broker or custodian, you may be able to vote either by toll-free telephone or by the Internet. Please refer to the enclosed voting form for instructions on how to vote electronically. You may also vote by signing, dating and returning the enclosed BLUE voting form.

If you have any questions or require any additional information concerning this Proxy Statement, please contact Okapi Partners at the address set forth below.

OKAPI PARTNERS LLC
437 Madison Avenue, 28th Floor
New York, N.Y. 10022
(212) 297-0720
Stockholders Call Toll-Free at: 877-869-0171
E-mail: info@okapipartners.com

PRELIMINARY COPY SUBJECT TO COMPLETION
DATED APRIL __, 2014

HEALTHWAYS, INC.

2014 ANNUAL MEETING OF STOCKHOLDERS

THIS PROXY IS SOLICITED ON BEHALF OF NORTH TIDE CAPITAL MASTER, LP

THE BOARD OF DIRECTORS OF HEALTHWAYS, INC.
IS NOT SOLICITING THIS PROXY

P R O X Y

The undersigned appoints Conan J. Laughlin and [Stephen Shorey], and each of them, attorneys and agents with full power of substitution to vote all shares of Common Stock of Healthways, Inc. (the "Company") which the undersigned would be entitled to vote if personally present at the 2014 Annual Meeting of Stockholders of the Company scheduled to be held at the Franklin Marriott Cool Springs located at 700 Cool Springs Boulevard, Franklin, Tennessee, 37067 on Tuesday, June 24, 2014 at 9:30 a.m., Central time (including any adjournments or postponements thereof and any meeting which may be called in lieu thereof, the "Annual Meeting").

The undersigned hereby revokes any other proxy or proxies heretofore given to vote or act with respect to the shares of common stock of the Company held by the undersigned, and hereby ratifies and confirms all action the herein named attorneys and proxies, their substitutes, or any of them may lawfully take by virtue hereof. If properly executed, this Proxy will be voted as directed on the reverse and in the discretion of the herein named attorneys and proxies or their substitutes with respect to any other matters as may properly come before the Annual Meeting that are unknown to North Tide Capital Master, LP ("North Tide") a reasonable time before this solicitation.

IF NO DIRECTION IS INDICATED WITH RESPECT TO THE PROPOSALS ON THE REVERSE, THIS PROXY WILL BE VOTED "FOR" PROPOSAL 1, ["FOR"/"AGAINST"] PROPOSAL 2, ["FOR"] PROPOSAL 3, ["FOR"/"AGAIN PROPOSAL 4, AND ["FOR"] PROPOSAL 5.

This Proxy will be valid until the completion of the Annual Meeting. This Proxy will only be valid in connection with North Tide's solicitation of proxies for the Annual Meeting.

IMPORTANT: PLEASE SIGN, DATE AND MAIL THIS PROXY CARD PROMPTLY!

CONTINUED AND TO BE SIGNED ON REVERSE SIDE

[X] Please mark vote as in this example

NORTH TIDE STRONGLY RECOMMENDS THAT STOCKHOLDERS VOTE IN FAVOR OF THE NOMINEES LISTED BELOW IN PROPOSAL 1. [NORTH TIDE MAKES NO RECOMMENDATION WITH RESPECT TO PROPOSALS 2, 3, 4 AND 5].

1. North Tide's proposal to elect Edwin "Mac" Crawford, Bradley S. Karro, Paul H. Keckley and Conan J. Laughlin as directors of the Company.

		FOR ALL NOMINEES	WITHHOLD AUTHORITY TO VOTE FOR ALL NOMINEES	FOR ALL EXCEPT NOMINEE(S) WRITTEN BELOW
Nominees:	Edwin "Mac" Crawford	[ ]	[ ]	[ ]
	Bradley S. Karro			______________
	Paul H. Keckley			
	Conan J. Laughlin			______________
				______________

North Tide does not expect that the Nominees will be unable to stand for election, but, in the event any Nominee is unable to serve or for good cause will not serve, the Shares represented by this proxy card will be voted for substitute nominee(s), to the extent this is not prohibited under the Bylaws and applicable law. In addition, North Tide has reserved the right to nominate substitute person(s) if the Company makes or announces any changes to its Bylaws or takes or announces any other action that has, or if consummated would have, the effect of disqualifying any Nominee, to the extent this is not prohibited under the Bylaws and applicable law. In any such case, Shares represented by this proxy card will be voted for such substitute nominee(s).

2. Company's proposal regarding advisory vote to approve executive compensation.

¨ FOR ¨ AGAINST ¨ ABSTAIN

3. Company's proposal to ratify the preliminary appointment of Ernst & Young LLP as independent auditor for the 2014 fiscal year.

¨ FOR ¨AGAINST ¨ ABSTAIN

4. Company's proposal to approve a new 2014 Stock Incentive Plan.

o FOR o AGAINST o ABSTAIN

5. Company's proposal to approve an amendment to the Company's Bylaws to implement a majority voting standard for uncontested election of directors.

o FOR o AGAINST o ABSTAIN

DATED: ____________________________

____
(Signature)

____
(Signature, if held jointly)

____
(Title)

WHEN SHARES ARE HELD JOINTLY, JOINT OWNERS SHOULD EACH SIGN. EXECUTORS, ADMINISTRATORS, TRUSTEES, ETC., SHOULD INDICATE THE CAPACITY IN WHICH SIGNING. PLEASE SIGN EXACTLY AS NAME APPEARS ON THIS PROXY.

ES, SERIF" SIZE="2">25,293 7,418 353 42 33,106
4.01 5.00%
34,348 1,434 577 314 36,673
5.01 6.00%
14,206 4,591 37 18,834

6.01 7.00%

Total

$74,365 $13,499 $930 $393 $89,187

The following table shows the amount of certificates of deposit of more than $100,000 by time remaining until maturity as of June 30, 2007:

	(In thousands)
3 months or less	$ 5,712
Over 3 to 6 months	4,210
Over 6 to 12 months	5,978
Over 12 months	1,986
Total	$17,886

The following table sets forth the net changes in deposit accounts for the periods indicated:

	Year Ended June 30,	
	2007	2006
	(Dollars in thousands)	
Opening balance	$174,342	$172,496
Deposits(Withdrawals), Net	1,279	(1,110)
Interest credited	4,026	2,956
Ending balance	$179,647	$174,342
Net increase	$ 5,305	$ 1,846
Percent increase	3.04%	1.07%
Weighted average cost of deposits during the period	2.37%	1.87%
Weighted average cost of deposits at end of period	2.64%	2.05%

Our depositors are primarily residents of the state of Montana. We issued $4.41 million in brokered deposits during this fiscal year.

Borrowings.

Deposits are the primary source of funds for our lending and investment activities and for general business purposes. However, as the need arises, or in order to take advantage of funding opportunities, we also borrow funds in the form of advances from the Federal Home Loan Bank of Seattle and other borrowings from PNC Financial Services, Inc. (PNC) to supplement our supply of lendable funds and to meet deposit withdrawal requirements.

During the previous fiscal year, Eagle formed a special purpose subsidiary, Eagle Bancorp Statutory Trust I (the Trust), for the purpose of issuing trust preferred securities in the amount of $5.0 million. Eagle has issued subordinated debentures to the Trust, and the coupon on the debentures matches the dividend payment on the trust preferred securities. For regulatory purposes, the securities qualify as Tier 1 Capital, while for accounting purposes they are recorded as long term debt. The securities have a 30 year maturity and carry a fixed coupon of 6.02% for the first five years, at which time the coupon becomes variable, at a spread of 142 basis points over 3 month LIBOR.

The following table sets forth information concerning our borrowing from the Federal Home Loan Bank of Seattle and PNC at the end of, and during, the periods indicated:

	Year Ended June 30, 2007	2006
	(Dollars in thousands)	
Advances and other borrowings:		
Average balance	$29,071	$12,665
Maximum balance at any month-end	36,695	22,602
Balance at period end	33,800	22,371
Weighted average interest rate during the period	5.04%	4.31%
Weighted average interest rate at period end	4.90%	4.96%

Subsidiary Activity

We are permitted to invest in the capital stock of, or originate secured or unsecured loans to, subsidiary corporations. We do not have any subsidiaries, except for American Federal Savings Bank and Eagle Bancorp Statutory Trust I.

Personnel

As of June 30, 2007, we had 72 full-time employees and 8 part-time employees. The employees are not represented by a collective bargaining unit. We believe our relationship with our employees to be good.

REGULATION

Set forth below is a brief description of laws which relate to the regulation of American Federal and Eagle Bancorp. The description does not purport to be complete and is qualified in its entirety by reference to applicable laws and regulations.

Regulation of American Federal Savings Bank

General.

As a federally chartered savings bank and a member of the FDIC s Deposit Insurance Fund, American Federal Savings Bank is subject to extensive regulation by the Office of Thrift Supervision and the FDIC. Lending activities and other investments must comply with federal statutory and regulatory requirements. American Federal Savings Bank is also subject to reserve requirements of the Federal Reserve System. Federal regulation and supervision establishes a comprehensive framework of activities in which an institution can engage and is intended primarily for the protection of the Deposit Insurance Fund of the FDIC and depositors. This regulatory structure gives the regulatory authorities extensive discretion in connection with their supervisory and enforcement activities and examination policies, including policies regarding the classification of assets and the establishment of adequate loan loss reserves.

The Office of Thrift Supervision regularly examines American Federal Savings Bank and provides a report on its examination findings to American Federal s board of directors. American Federal s relationship with its depositors and borrowers is also regulated by federal law, especially in such matters as the ownership of savings accounts and the form and content of American Federal s mortgage documents.

American Federal Savings Bank must file reports with the Office of Thrift Supervision and the FDIC concerning its activities and financial condition, and must obtain regulatory approvals prior to entering into transactions such as mergers with or acquisitions of other financial institutions. Any change in such regulations, whether by the Office of Thrift Supervision, the FDIC or the United States Congress, could have a material adverse impact on Eagle and American Federal, and their operations.

Insurance of Deposit Accounts.

The deposit accounts held by American Federal Savings Bank are insured by the Deposit Insurance Fund of the FDIC to a maximum of $100,000 as permitted by law (qualifying retirement funds are insured up to $250,000). Insurance on deposits may be terminated by the FDIC it if finds an institution has engaged in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC or the institution s primary regulator.

Regulatory Capital Requirements.

Office of Thrift Supervision (OTS) capital regulations require savings institutions to meet three capital standards. The standards for capital adequacy are tangible capital equal to 1.5% of adjusted total assets, core capital (leverage ratio) equal to at least 4% of total adjusted assets, and risk-based capital equal to 8% of total risk-weighted assets. In order to be deemed Well Capitalized , OTS rules require a leverage ratio of at least 5%, a Tier 1 risk-based ratio of at least 6%, and a total risk-based ratio of at least 10%. American Federal s capital ratios at June 30, 2007 are set forth below.

	Actual		For Capital Adequacy Purposes	
	Amount	**Ratio**	**Amount**	**Ratio**
	(Dollars in thousands)			
Tangible	$25,314	10.48	$ 3,623	1.50
Leverage	$25,314	10.48	$ 7,246	3.00
Tier 1 risk-based	$25,314	14.50	$ 6,984	4.00
Total risk-based	$25,797	14.78	$13,967	8.00

Tangible capital is defined as core capital less all intangible assets, less nonqualifying mortgage servicing rights and investments. Core capital is defined as common stockholders equity, noncumulative perpetual preferred stock and minority interests in the equity accounts of consolidated subsidiaries, nonwithdrawable accounts and pledged deposits of mutual savings associations and qualifying supervisory goodwill, less nonqualifying intangible assets, mortgage servicing rights and investments.

The risk-based capital standard for savings institutions requires the maintenance of total risk-based capital of 8% of risk-weighted assets. Risk-based capital is comprised of core and supplementary capital. The components of supplementary capital include, among other items, cumulative perpetual preferred stock, perpetual subordinated debt, mandatory convertible subordinated debt, intermediate-term preferred stock, and the portion of the allowance for loan losses not designated for specific loan losses. The portion of the allowance for loan and lease losses includable in supplementary capital is limited to a maximum of 1.25% of risk-weighted assets. Overall, supplementary capital is limited to 100% of core capital. A savings association must calculate its risk-weighted assets by multiplying each asset and off-balance sheet item by various risk factors as determined by the Office of Thrift Supervision, which range from 0% for cash to 100% for delinquent loans, property acquired through foreclosure, commercial loans, and other assets.

Office of Thrift Supervision rules require a deduction from capital for institutions which have unacceptable levels of interest rate risk. The Office of Thrift Supervision calculates the sensitivity of an institution s net portfolio value based on data submitted by the institution in a schedule to its quarterly Thrift Financial Report and using the interest rate risk measurement model adopted by the Office of Thrift Supervision. The amount of the interest rate risk component, if any, is deducted from an institution s total capital in order to determine if it meets its risk-based capital requirement. Federal savings institutions with less than $300 million in assets and a risk-based capital ratio above 12% are exempt from filing the interest rate risk schedule. However, the Office of Thrift Supervision may require any exempt institution to file such schedule on a quarterly basis and may be subject to an additional capital requirement based on its level of interest rate risk as compared to its peers.

Dividend and Other Capital Distribution Limitations.

The Office of Thrift Supervision imposes various restrictions or requirements on the ability of savings institutions to make capital distributions, including dividend payments.

Office of Thrift Supervision regulations impose limitations on all capital distributions by savings institutions, such as cash dividends, payment to repurchase or otherwise acquire its shares, payments to stockholders of another institution in a cash-out merger, and other distributions charged

against capital. The rule establishes three tiers of institutions based primarily on an institution s capital level. An institution that exceeds all capital requirements before and after a proposed capital distribution and has not been advised by the Office of Thrift Supervision that it is in need of more than the normal supervision has the greatest amount of flexibility for determining dividends. Such institutions can, after prior notice but without the approval of the Office of Thrift Supervision, make capital distributions during a calendar year. These distributions can be equal to the greater of 100% of its net income to date during the calendar year plus the amount that would reduce by one-half its excess capital divided by its fully phased-in capital requirements at the beginning of the calendar year. At the institution s discretion, dividends can also be 75% of its net income over the most recent four-quarter period. Any additional capital distributions require prior regulatory notice. As of June 30, 2007, American Federal Savings Bank had this level of flexibility with respect to dividends.

Qualified Thrift Lender Test.

Federal savings institutions must meet a qualified thrift lender test or they become subject to operating restrictions. The Bank anticipates that it will maintain an appropriate level of investments consisting primarily of residential mortgages, mortgage-backed securities and other mortgage-related investment, and otherwise qualify as a qualified thrift lender. The required percentage of these mortgage-related investments is 65% of portfolio assets. Portfolio assets are all assets minus intangible assets, property used by the institution in conducting its business and liquid assets equal to 10% of total assets. Compliance with the qualified thrift lender test is determined on a monthly basis in nine out of every twelve months.

Transactions With Affiliates.

Generally, federal banking law requires that transactions between a savings institution or its subsidiaries and its affiliates must be on terms as favorable to the savings institution as comparable transactions with non-affiliates. In addition, some transactions can be restricted to an aggregate percentage of the savings institution s capital. Collateral in specified amounts must usually be provided by affiliates in order to receive loans from the savings institution. In addition, a savings institution may not extend credit to any affiliate engaged in activities not permissible for a bank holding company or acquire the securities of any affiliate that is not a subsidiary. The Office of Thrift Supervision has the discretion to treat subsidiaries of a savings institution as affiliates on a case-by-case basis.

Liquidity Requirements.

The Bank is required to maintain minimum levels of liquid assets as defined by the Office of Thrift Supervision regulations. The OTS states that the liquidity requirement is retained for safety and soundness purposes, and that appropriate levels of liquidity will depend upon the types of activities in which the bank engages.

Federal Home Loan Bank System.

We are a member of the Federal Home Loan Bank of Seattle, which is one of 12 regional Federal Home Loan Banks. Each Federal Home Loan Bank serves as a reserve or central bank for its members within its assigned region. It is funded primarily from funds deposited by financial institutions and proceeds derived from the sale of consolidated obligations of the Federal Home Loan Bank System. It makes loans to members pursuant to policies and procedures established by the board of directors of the Federal Home Loan Bank.

As a member, we are required to purchase and maintain stock in the Federal Home Loan Bank of Seattle in an amount equal to at least 1% of our aggregate unpaid residential mortgage loans, home purchase contracts or similar obligations at the beginning of each year, or 5% of our outstanding advances, whichever is larger. We are in compliance with this requirement. The Federal Home Loan Bank imposes various limitations on advances such as limiting the amount of real estate related collateral to 30% of a member s capital and limiting total advances to a member. As a federal savings bank, we were mandatory members of the Federal Home Loan Bank of Seattle. Under the Gramm-Leach-Bliley Financial Modernization Act of 1999, we are now voluntary members of the Federal Home Loan Bank of Seattle. We could withdraw or significantly reduce our required stock ownership in the Federal Home Loan Bank of Seattle.

Federal Reserve System.

The Federal Reserve System requires all depository institutions to maintain noninterest-bearing reserves at specified levels against their checking, NOW and Super NOW checking accounts and non-personal time deposits. The balances maintained to meet the reserve requirements imposed by the Federal Reserve System may be used to satisfy the Office of Thrift Supervision liquidity requirements.

Savings institutions have authority to borrow from the Federal Reserve System discount window, but Federal Reserve System policy generally requires savings institutions to exhaust all other sources before borrowing from the Federal Reserve System.

Regulation of Eagle Bancorp

General.

Eagle Bancorp, as a federal stock corporation in a mutual holding company structure, is deemed a federal mutual holding company within the meaning of Section 10(o) of the Home Owners Loan act (HOLA). Eagle is registered and files reports with the Office of Thrift Supervision and is subject to regulation and examination by the Office of Thrift Supervision. In addition, the Office of Thrift Supervision has enforcement authority over Eagle and any nonsavings institution subsidiary of Eagle. The Office of Thrift Supervision can restrict or prohibit activities that it determines to be a serious risk to us. This regulation is intended primarily for the protection of our depositors and not for the benefit of stockholders of Eagle.

Federal Taxation

Savings institutions are subject to the Internal Revenue Code of 1986, as amended, in the same general manner as other corporations. Prior to changes to the Internal Revenue Code in 1996, thrift institutions enjoyed a tax advantage over banks with respect to determining additions to its bad debt reserves.

The Internal Revenue Code was revised in August 1996 to equalize the taxation of thrift institutions and banks, effective for taxable years beginning after 1995. All thrift institutions are now subject to the same provisions as banks with respect to deductions for bad debt. Now only thrift institutions that are treated as small banks under the Internal Revenue Code may continue to account for bad debts under the reserve method; however, such institutions may only use the experience method for determining additions to their bad debt reserve. Thrift institutions that are not treated as small banks may no longer use the reserve method to account for their bad debts but must now use the specific charge-off method.

The revisions to the Internal Revenue Code in 1996 also provided that all thrift institutions must generally recapture any applicable excess reserves into their taxable income, over a six year period beginning in 1996; however, such recapture may be delayed up to two years if a thrift institution meets a residential-lending test. Generally, a thrift institution s applicable excess reserves equals the excess of the balance of its bad debt reserves as of the close of its taxable year beginning before January 1, 1996, over the balance of such reserves as of the close of its last taxable year beginning before January 1, 1988. These are known as pre-1988 reserves. American Federal Savings Bank had recaptured all of it s remaining applicable excess reserve as of June 30, 2007.

In addition, all thrift institutions must continue to keep track of their pre-1988 reserves because this amount remains subject to recapture in the future under the Internal Revenue Code. A thrift institution such as American Federal, would generally be required to recapture into its taxable income its pre-1988 reserves in the case of excess distributions, and redemptions of American Federal s stock and in the case of a reduction in American Federal s outstanding loans when comparing loans currently outstanding to loans outstanding at the end of the base year. For taxable years after 1995, American Federal Savings Bank will continue to account for its bad debts under the reserve method. The balance of American Federal s pre-1988 reserves equaled $915,000.

Eagle may exclude from its income 100% of dividends received from American Federal Savings Bank as a member of the same affiliated group of corporations. A 70% dividends received deduction generally applies with respect to dividends received from corporations that are not members of such affiliated group.

American Federal s federal income tax returns for the last five tax years have not been audited by the IRS.

State Taxation

American Federal Savings Bank files Montana tax returns. For Montana tax purposes, savings institutions are presently taxed at a rate equal to 6.75% of taxable income which is calculated based on federal taxable income, subject to adjustments (including the addition of interest income on state and municipal obligations).

American Federal s state tax returns have not been audited for the past five years by the state of Montana.

ITEM 2. DESCRIPTION OF PROPERTY.

The Company s business activities consist of its ownership of 100% of the common stock of the Bank. The Bank s executive office is located at 1400 Prospect Avenue in Helena, Montana. American Federal conducts its business through five offices, which are located in Helena, Bozeman,

Butte, and Townsend, Montana. All of its offices are owned. Its principal banking office in Helena also serves as its executive headquarters and operations center. This office houses over 50% of American Federal full-time employees. The following table sets forth the location of each of American Federal s offices, the year the office was opened, and the net book value including land, buildings, computer software and its related equipment and furniture. The square footage at each location is also shown.

Location	Address	Opened	Value at June 30, 2007 (in thousands)	Square Footage
Helena Main Office	1400 Prospect Ave. Helena, MT 59601	1997	$4,232	32,304
Helena Downtown Drive-up	28 Neill Ave. Helena, MT 59601	1987	$ 373	1,391
Butte Office	3401 Harrison Ave. Butte, MT 59701	1979	$ 535	3,890
Bozeman Office	606 North Seventh Bozeman, MT 59715	1980	$ 600	5,886
Townsend Office	416 Broadway Townsend, MT 59644	1979	$ 65	1,973

As of June 30, 2007, the net book value of land, buildings, furniture, and equipment owned by American Federal, less accumulated depreciation, totaled $5.81 million. Eagle has an earnest money deposit for the purchase of land in Bozeman for potential branch relocation and has spent approximately $67,000 on architect fees for preliminary building plans.

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ITEM 3. LEGAL PROCEEDINGS.

American Federal, from time to time, is a party to routine litigation, which arises in the normal course of business, such as claims to enforce liens, condemnation proceedings on properties in which American Federal Savings Bank holds security interests, claims involving the making and servicing of real property loans, and other issues incident to the business of American Federal. There were no lawsuits pending or known to be contemplated against Eagle or American Federal at June 30, 2007.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

No matters were submitted to a vote of security holders in the fourth quarter of the fiscal year ended June 30, 2007.

PART II

ITEM 5. MARKET FOR COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND SMALL BUSINESS ISSUERS' PURCHASES OF EQUITY SECURITIES.

The common stock is traded on the OTC Bulletin Board under the symbol EBMT. At the close of business on June 30, 2007, there were 1,084,357 shares of common stock outstanding, held by approximately 600 shareholders of record. Eagle Financial MHC, Eagle s mutual holding company, held 648,493 shares (or 59.8%) of the outstanding common stock.

The high bid and asked prices noted below for the four quarters of fiscal 2006 and the four quarters of the current fiscal year were obtained from the OTC Bulletin Board. The quotations reflect interdealer prices without retail markup,

	High Bid	Low Bid
Fourth quarter 2007	$34.00	$31.43
Third quarter 2007	$34.50	$31.50

	High Bid	Low Bid
Second quarter 2007	$34.00	$31.30
First quarter 2007	$34.00	$31.25
Fourth quarter 2006	$33.00	$30.30
Third quarter 2006	$34.50	$31.50
Second quarter 2006	$36.00	$32.15
First quarter 2006	$35.00	$30.00

The closing price of the common stock on June 30, 2007, was $32.70. The company had paid four quarterly dividends during the year, all in the amount of $0.22per share. Eagle Financial MHC waived receipt of its dividends during the year.

ITEM 5 (c) SMALL BUSINESS ISSUER PURCHASES OF EQUITY SECURITIES

Period	(a) Total Number of Shares Purchased*	(b) Average Price Paid Per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	(d) Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
April 2007	None	N/A	N/A	N/A
May 2007	1,000	$33.00	1,000	4,535
June 2007	None	N/A	N/A	N/A
Total	1,000	$33.00	1,000	N/A

*The Company publicly announced a stock repurchase program on July 21, 2006. The Company is authorized to acquire up to 28,750 shares of common stock with the price subject to market conditions. No expiration date was set for the repurchase program. As of August 27, 2007, 25,465 shares had been purchased.

ITEM 6. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION.

Note Regarding Forward-Looking Statements

This report contains certain forward-looking statements. Eagle desires to take advantage of the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 and is including this statement for the express purpose of availing itself of the protections of the safe harbor with respect to all such forward-looking statements. These forward-looking statements, which are included in Management s Discussion and Analysis, describe future plans or strategies and include Eagle s expectations of future financial results. The words believe , expect , anticipate , estimate , project , and similar expressions identify forward-looking statements. Eagle s ability to predict results or the effect of future plans or strategies or qualitative or quantitative changes based on market risk is inherently uncertain. Factors which could affect actual results but are not limited to include (i) change in general market interest rates, (ii) general economic conditions, (iii) local economic conditions, (iv) legislative/regulatory changes, (v) monetary and fiscal policies of the U.S. Treasury and Federal Reserve, (vi) changes in the quality or composition of Eagle s loan and investment portfolios, (vii) demand for loan products, (viii) deposit flows, (ix) competition, and (x) demand for financial services in Eagle s markets. These factors should be considered in evaluating the forward-looking statements. You are cautioned not to place undue reliance on these forward-looking statements that speak only as of their dates.

General

Eagle Bancorp s subsidiary, American Federal Savings Bank, operates as a community savings bank. It raises money by offering FDIC-insured deposit products and lending this money, primarily for the purpose of home financing. As of June 30, 2007, 43.11% of its total loans were residential mortgage loans with fixed rates and 8.91% were residential mortgage loans with adjustable rates. Total first lien mortgage loans at

June 30, 2007, were $115.83 million or 73.04% of the total loan portfolio. Other loan products include home equity loans, consumer and commercial loans. These loans totaled $42.76 million or 26.96% of the total loan portfolio.

The consolidated financial condition and operating results of Eagle are primarily dependent on its wholly owned subsidiary, American Federal Savings Bank. All references to the Company prior to April 4, 2000, except where otherwise indicated, are to the Bank.

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Analysis of Net Interest Income

The Bank s earnings have historically depended primarily upon net interest income, which is the difference between interest income earned on loans and investments and interest paid on deposits and any borrowed funds. It is the single largest component of Eagle s operating income. Net interest income is affected by (i) the difference between rates of interest earned on loans and investments and rates paid on interest-bearing deposits and borrowings (the interest rate spread) and (ii) the relative amounts of loans and investments and interest-bearing deposits and borrowings.

The following table presents the average balances of and the interest and dividends earned or paid on each major class of loans and investments and interest-bearing deposits and borrowings. Nonaccruing loans are included in balances for all periods. Average balances are daily average balances. The yields and costs include fees, which are considered adjustments to yields.

	For the twelve months ended June 30,					
	2007			2006		
	(Dollars in thousands)					
	Average Daily Balance	Interest and Dividends	Yield/ Rate	Average Daily Balance	Interest and Dividends	Yield/ Rate
Assets:						
Interest-earning assets:						
FHLB stock	$ 1,315	$ 7	0.53%	$ 1,315	$	0.00%
Loans receivable, net	149,818	9,731	6.50	124,282	7,799	6.28
Investment securities	66,723	2,854	4.28	69,700	2,641	3.79
Interest-bearing deposits with banks	922	50	5.42	1,473	59	4.01
Total interest-earning assets	218,778	12,642	5.78	196,770	10,499	5.34
Noninterest-earning assets	18,351			18,274		
Total assets	$237,129			$215,044		
Liabilities and Equity:						
Interest-bearing liabilities:						
Deposit accounts:						
Money market	$ 25,648	$ 525	2.05	$ 29,388	$ 492	1.67
Passbooks	23,139	152	0.66	24,994	164	0.66
Checking	30,789	63	0.20	31,024	55	0.18
Certificates of deposit	83,753	3,451	4.12	75,842	2,300	3.03
Advances from FHLB & subordinated debt	34,226	1,766	5.16	16,573	774	4.67
Total interest-bearing liabilities	197,555	5,957	3.02	177,821	3,785	2.13
Non-interest checking	13,382			12,612		
Other noninterest-bearing liabilities	2,189			1,956		
Total liabilities	213,126			192,389		
Total equity	24,003			22,655		
Total liabilities and equity	$237,129			$215,044		
Net interest income/interest rate spread[1]		$ 6,685	2.76%		$ 6,714	3.21%

	For the twelve months ended June 30,	
Net interest margin[2]	3.06%	3.41%
Total interest-earning assets to int-bearing liabilities	110.74%	110.66%

(1) Interest rate spread represents the difference between the average yield on interest-earning assets and the average rate on interest-bearing liabilities.

(2) Net interest margin represents income before the provision for loan losses divided by average interest-earning assets.

Rate/Volume Analysis

The following table sets forth information regarding changes in interest income and interest expense for the periods indicated. For each category of our loans and investments and our interest-bearing deposits and borrowings, information is provided on changes attributable to change in volume (change in volume multiplied by the old rate). The table also provides information on change in rate (changes in rate multiplied by old volume). The combined effects of changes in rate and volume have been allocated proportionately to the change due to rate and the change due to volume.

	For the Years Ended June 30, Increase (Decrease) (In thousands)					
	2007 vs 2006			2006 vs 2005		
	Volume	Due to Rate	Net	Volume	Due to Rate	Net
Interest earning assets:						
Loans receivable, net	$1,603	$ 329	$1,932	$1,645	$ 37	$1,682
Investment securities	(113)	326	213	(462)	231	(231)
Interest-bearing deposits with banks	(22)	13	(9)	(9)	34	25
Other earning assets		7	7		(20)	(20)
Total interest earning assets	1,468	675	2,143	1,174	282	1,456
Interest-bearing liabilities:						
Passbook, money market and checking accounts	(49)	78	29	1	195	196
Certificates of deposit	239	912	1,151	8	412	420
Borrowings	824	168	992	379	227	606
Total interest-bearing liabilities	1,014	1,158	2,172	388	834	1,222
Change in net interest income	$ 454	$ (483)	$ (29)	$ 786	$(552)	$ 234

Interest Rate Risk Analysis

In addition to the asset/liability committee, the board of directors reviews our asset and liability policies. The board of directors reviews interest rate risk and interest rate trends quarterly, as well as liquidity and capital ratio requirements. Management administers the policies and determinations of the board of directors with respect to our asset and liability goals and strategies. Our asset and liability policy and strategies are expected to continue as described so long as competitive and regulatory conditions in the financial institution industry and market interest rates continue as they have in recent years.

Overview

The Company s primary activity is its ownership of its wholly owned subsidiary, American Federal Savings Bank (the Bank). The Bank is a federally chartered savings bank, engaging in typical banking activities: acquiring deposits from local markets and investing in loans and investment securities. The Bank s primary component of earnings is its net interest margin (also called spread or margin), the difference between interest income and interest expense. The net interest margin is managed by management (through the pricing of its products and by the types of products offered and kept in portfolio), and is affected by moves in interest rates. Noninterest income in the form of fee income and gain on sale of loans adds to the Bank s income.

The Bank has a strong mortgage lending focus, with the majority of its loans in single-family residential mortgages. This has led to successfully marketing home equity loans to its customers, as well as a wide range of shorter term consumer loans for various personal needs (automobiles, recreational vehicles, etc.). In recent years the Bank has focused on adding commercial loans to its portfolio, both real estate and non-real estate. The purpose of this diversification is to mitigate the Bank s dependence on the residential mortgage market, as well as to improve its ability to manage its spread. The Bank s management recognizes the need for sources of fee income to complement its margin, and the Bank now maintains a significant loan serviced portfolio, which provides a steady source of fee income. The gain on sale of loans also provides significant fee income in periods of high mortgage loan origination volumes. Fee income is also supplemented with fees generated from the Bank s deposit accounts. The Bank has a high percentage of non-maturity deposits, such as checking accounts and savings accounts, which allows management flexibility in managing its spread. Non-maturity deposits do not automatically reprice as interest rates rise, as do certificates of deposit.

For the past two years, management s focus has been on improving the Bank s core earnings. Core earnings can be described as income before taxes, with the exclusion of gain on sale of loans and adjustments to the market value of the Bank s loan serviced portfolio. Management believes that the Bank will need to continue to focus on increasing net interest margin, other areas of fee income, and control operating expenses to achieve earnings growth going forward. Management s strategy of growing the bank s loan portfolio and deposit base is expected to help achieve these goals: loans typically earn higher rates of return than investments; a larger deposit base will yield higher fee income; increasing the asset base will reduce the relative impact of fixed operating costs. The biggest challenge to the strategy is funding the growth of the Bank s balance sheet in an efficient manner. Deposit growth will be difficult due to fierce competition and wholesale funding (which is usually more expensive than retail deposits) will likely be needed to supplement deposit growth.

The level and movement of interest rates impacts the Bank s earnings as well. For the 2007 fiscal year the yield curve continued to be flat, i.e. short-term interest rates were approximately at the same level as long-term interest rates. This can have a negative impact on the Bank s net interest margin as its deposits are typically priced relative to short-term rates, while the majority of its loan products are priced relative to long-term rates. The Bank has been able to partially offset this effect by reinvesting investment proceeds in the loan portfolio, because as noted earlier, loans typically earn higher rates of return than investments. Additionally, many of the Bank s investments which mature in the coming year are at low (below current market) interest rates, affording an opportunity to reinvest the proceeds at the current higher rates and increasing interest income in the coming quarters. Much of the Bank s certificate of deposit portfolio has already repriced to current levels, leading to a slower increase in interest expense on deposits in the next fiscal year.

Financial Condition

Introduction.

Total assets increased $18.51 million, or 8.18%, to $244.69 million at June 30, 2007, compared to $226.18 million at June 30, 2006. Total liabilities increased by $16.97 million, or 8.33%, to $220.60 million at June 30, 2007, from $203.63 million at June 30, 2006. The loan portfolio grew $17 million during the year, approximately one-half of the previous year s growth, due to an increase in loan sales. The rate of deposit growth was up from the previous year s pace, with certificates of deposit showing the largest increase, due in part to the issuance of $4.41 million in brokered deposits. Much of the asset growth was funded by increased borrowings.

Balance Sheet Details.

Loans receivable increased $17.28 million, or 12.27% to $158.14 million from $140.86 million. Increased originations in most loan categories contributed to the higher loan balances, and consequently all categories except consumer and commercial loans showed an increase in balances compared to last year. Commercial real estate and land loans increased $6.97 million during the year, and residential mortgage loans increased $6.05 million. The available-for-sale (AFS) investment portfolio increased $576,000, or 0.90%, to $64.77 million at June 30, 2007 from $64.20 million at June 30, 2006. The investment category with the largest increase was municipal securities, which increased $3.59 million.

Total deposits increased $5.31 million. Certificates of deposit increased $12.00 million, to $67.65 million at June 30, 2007 from $55.65 million at June 30, 2006. This amount includes the $4.41 million of brokered certificates of deposit issued during the year. Interest-earning checking accounts increased $1.38 million while noninterest checking increased $1.12 million. Money market accounts decreased $5.84 million and savings accounts decreased $1.92 million. A significant portion of the funds which left money market and savings accounts moved to certificates of deposit. Deposit growth is expected to continue to be difficult to achieve due to fierce competition among financial institutions in our markets.

Advances from the Federal Home Loan Bank and other borrowings increased to $33.80 million at year-end 2007 from $22.37 million at year-end 2006, an increase of $11.43 million. This increase was needed to help fund loan growth.

Total shareholders equity was $24.09 million at June 30, 2007, an increase of $1.54 million. This increase was the result of net income for the year and a decrease in accumulated other comprehensive loss of $239,000 (mainly due to a decrease in net unrealized loss on securities available-for-sale), partially offset by the purchase of treasury stock and dividends paid during the year.

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Comparison of Operating Results for the Years Ending June 30, 2007 and 2006

Net Income.

Eagle s net income was $1.778 million and $1.785 million for the years ended June 30, 2007 and 2006 respectively. This decrease of $7,000, or 0.40%, was the result of an increase in noninterest expense of $149,000 and a decrease in net interest income of $29,000, offset by an increase in noninterest income of $96,000. Eagle s tax provision was $75,000 lower in 2007. Basic earnings per share for the year ended June 30, 2007 were $1.66, compared to $1.66 for the year ended June 30, 2006. Diluted earnings per share were $1.47 and $1.48 for 2007 and 2006, respectively.

Net Interest Income.

Net interest income decreased to $6.685 million for the year ended June 30, 2007, from $6.714 million for the previous year. This decrease of $29,000, or 0.43%, was the result of an increase in interest expense of $2.174 million, partially offset by an increase in interest and dividend income of $2.145 million.

Interest and Dividend Income.

Total interest and dividend income was $12.651 million for the year ended June 30, 2007, compared to $10.506 million for the year ended June 30, 2006, an increase of $2.145 million, or 20.42%. Interest and fees on loans increased to $9.731 million for 2007 from $7.799 million for 2006. This increase of $1.932 million, or 24.77%, was due primarily to the increase in the average balances on loans receivable for the year ended June 30, 2007. The average interest rate earned on loans receivable increased by 22 basis points, to 6.50% from 6.28%. Average balances for loans receivable, net, for the year ended June 30, 2007 were $149.82 million, compared to $124.28 million for the previous year. This represents an increase of $25.54 million, or 20.55% and reflects management s plan to grow the loan portfolio. Interest and dividends on investment securities available-for-sale (AFS) increased to $2.811 million for the year ended June 30, 2007 from $2.589 million for the year ended June 30, 2006, an increase of $222,000, or 8.57%. This increase was the result of higher average interest rates on the AFS portfolio during the year, as the average balances declined. Interest earned from deposits at other banks decreased slightly for the year ended June 30, 2007 due to lower average balances. Interest and dividends on investments held-to-maturity (HTM) also experienced a slight decline.

Interest Expense.

Total interest expense increased to $5.966 million for the year ended June 30, 2007 from $3.792 million for the year ended June 30, 2006, an increase of $2.174 million, or 57.33%. Interest on deposits increased to $4.191 million for the year ended June 30, 2007 from $3.011 million for the year ended June 30, 2006. This increase of $1.180 million, or 39.19%, was due primarily to an increase on average rates paid, while average balances increased slightly on deposit accounts. The average cost of deposits increased 50 basis points, to 2.37% in 2007 from 1.87% in 2006. Certificates of deposit were the only category to show an increase in average balances in 2007. An increase in the average balance of borrowings as well as an increase in the average rate paid resulted in an increase in interest paid on borrowings to $1.775 million for the year ended June 30, 2007 from $781,000 for the year ended June 30, 2006. The average balance of borrowings increased to $34.226 million for the year ended June 30, 2007, compared to $16.573 million for the year ended June 30, 2006. The average rate paid on borrowings increased to 5.16% in 2007 from 4.67% in 2006.

Provision for Loan Losses.

Provisions for loan losses are charged to earnings to maintain the total allowance for loan losses at a level considered adequate by American Federal Savings Bank to provide for probable loan losses based on prior loss experience, volume and type of lending conducted by American Federal, available peer group information, and past due loans in portfolio. The Bank s policies require the review of assets on a quarterly basis. The Bank classifies loans as well as other assets if warranted. While management believes it uses the best information available to make a determination with respect to the allowance for loan losses, it recognizes that future adjustments may be necessary. No provision was made for loan losses for either year ended June 30, 2007 or June 30, 2006. This is a reflection of the continued strong asset quality of American Federal s loan portfolio, as non-performing loan ratios continue to be low. Total classified assets decreased to $391,000 at June 30, 2007 from $700,000 at June 30, 2006. Total non-performing loans as a percentage of the total loan portfolio is 0.13%. As of June 30, 2007, American Federal Savings

Bank had no real estate owned.

Noninterest Income.

Total noninterest income increased to $2.261 million for the year ended June 30, 2007, from $2.165 million for the year ended June 30, 2006, an increase of $96,000 or 4.43%. This increase was primarily due to increases in net gain on sale of loans and other noninterest income. Net gain on sale of loans increased $151,000 to $643,000, due to management s decision to sell a higher percentage of mortgage originations. Other noninterest income increased $45,000 to $593,000, primarily due to increased fee income on electronic payments and higher fee income on loan products.

Noninterest Expense.

Noninterest expense increased by $149,000 or 2.30% to $6.614 million for the year ended June 30, 2007 from $6.465 million for the year ended June 30, 2006. This increase was primarily due to increases in salaries and benefits of $98,000, legal and accounting fees of $50,000 and marketing expense of $46,000. The increase in salaries and benefits was due to normal pay raises. Legal and accounting fees were higher due to the outsourcing of the Bank s internal audit function and higher legal expenses at the holding company level. Marketing expenses were higher due to increased promotion of deposit products. These increases were partially offset by a decrease in the amortization of mortgage servicing fees of $50,000. This decrease was due to decreased prepayment activity on mortgage loans. Other categories of noninterest expense showed modest changes.

Income Tax Expense.

Eagle s income tax expense was $554,000 for the year ended June 30, 2007, compared to $629,000 for the year ended June 30, 2006. The effective tax rate for the year ended June 30, 2007 was 23.76% as opposed to 26.06% for the year ended June 30, 2006.

Liquidity and Capital Resources

The company s subsidiary, American Federal Savings Bank, is required to maintain minimum levels of liquid assets as defined by the Office of Thrift Supervision (OTS) regulations. The OTS has eliminated the statutory requirement based upon a percentage of deposits and short-term borrowings. The OTS states that the liquidity requirement is retained for safety and soundness purposes, and that appropriate levels of liquidity will depend upon the types of activities in which the company engages. For internal reporting purposes, the Bank uses the previous regulatory definitions of liquidity. The Bank s average liquidity ratio average was 9.93% and 16.27% for the months ended June 30, 2007 and 2006, respectively. The liquidity ratio declined due to an increase in the loan portfolio (funded by other borrowings) while the investment portfolio and deposits showed smaller increases.

The Bank s primary sources of funds are deposits, repayment of loans and mortgage-backed securities, maturities of investments, funds provided from operations, advances from the Federal Home Loan Bank of Seattle and other borrowings. Scheduled repayments of loans and mortgage-backed securities and maturities of investment securities are generally predictable. However, other sources of funds, such as deposit flows and loan prepayments, can be greatly influenced by the general level of interest rates, economic conditions and competition. The Bank uses liquidity resources principally to fund existing and future loan commitments. It also uses them to fund maturing certificates of deposit, demand deposit withdrawals and to invest in other loans and investments, maintain liquidity, and meet operating expenses.

Net cash provided by the Company s operating activities, which is primarily comprised of cash transactions affecting net income was $2.89 million for the year ended June 30, 2007 and $4.90 million for the year ended June 30, 2006. The change was primarily a result of a decrease in the amount of loans held for sale in 2006.

Net cash used in the Company s investing activities, which is primarily comprised of cash transactions from the investment securities and mortgage-backed securities portfolios and the loan portfolio, was $18.80 million for the year ended June 30, 2007, and $25.57 million for the year ended June 30, 2006. The decrease in cash used was primarily due to slower growth of the loan portfolio in 2007 compared to 2006.

Net cash provided by the Company s financing activities, which is primarily cash transactions from net increases in deposits and net Federal Home Loan Bank advances and other borrowings, totaled $16.11 million for the year ended June 30, 2007, and $18.57 million for the year ended June 30, 2006. This decrease in cash provided was primarily due to the issuance of trust preferred securities in 2006.

Liquidity may be adversely affected by unexpected deposit outflows, higher interest rates paid by competitors, and similar matters. Management monitors projected liquidity needs and determines the level desirable based in part on our commitments to make loans and management s assessment of our ability to generate funds.

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At March 31, 2007 (the most recent report available), the Bank s measure of sensitivity to interest rate movements, as measured by the OTS, increased slightly from the previous quarter. The market value of the Bank s capital position has decreased slightly from the previous year. The Bank is well within the guidelines set forth by the Board of Directors for interest rate sensitivity.

As of June 30, 2007, the Bank s regulatory capital was in excess of all applicable regulatory requirements. At June 30, 2007, the Bank s tangible, core, and risk-based capital ratios amounted to 10.5%, 10.5%, and 14.8%, respectively, compared to regulatory requirements of 1.5%, 3.0%, and 8.0%, respectively.

Impact of Inflation and Changing Prices

Our financial statements and the accompanying notes, which are found in Item 7, have been prepared in accordance with generally accepted accounting principles, which require the measurement of financial position and operating results in terms of historical dollars without considering the change in the relative purchasing power of money over time and due to inflation. The impact of inflation is reflected in the increased cost of our operations. Interest rates have a greater impact on our performance than do the general levels of inflation. Interest rates do not necessarily move in the same direction or to the same extent as the prices of goods and services.

Recent Accounting Pronouncements

In December 2003, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 46R, Consolidation of Variable Interest Entities an Interpretation of ARB No. 51 (FIN 46R). This Interpretation, which replaces FASB Interpretation No. 46, Consolidation of Variable Interest Entities , clarifies the application of Accounting Research Bulletin No. 51, Consolidated Financial Statements , for certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support.

On September 28, 2006, the Company issued trust-preferred securities through a wholly-owned subsidiary trust, further described in Note 9 of the audited financial statements. Under the provisions of FIN 46R, the Company accounts for its investment in the trust as an asset and its junior subordinated debentures as a liability. Additionally, the Company reports the dividends paid and received on the securities in the statement of income as interest income and expense. In February 2006, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 155, Accounting for Certain Hybrid Financial Instruments, an amendment of SFAS Statements No. 133 and 140. SFAS No. 155 improves financial reporting by eliminating the exemption from applying SFAS No. 133 to interests in securitized financial assets so that similar instruments are accounted for similarly regardless of the form of the instruments.

This statement also improves financial reporting by allowing a preparer to elect fair value measurement at acquisition, at issuance, or when a previously recognized financial instrument is subject to a remeasurement (new basis) event, on an instrument-by-instrument basis, in cases in which a derivative would otherwise have to be bifurcated. SFAS No. 155 is effective for all financial instruments acquired, issued, or subject to a remeasurement (new basis) event occurring after the beginning of the Company s first fiscal year that begins after September 15, 2006. The Company does not anticipate that the adoption of this new accounting principle will have a material effect on its financial position, results of operations or cash flows.

On March 17, 2006, the FASB issued SFAS No. 156, Accounting for Servicing of Financial Assets, an amendment of SFAS No. 140, which permits, but does not require, an entity to account for one or more classes of servicing rights (i.e., mortgage servicing rights, or MSRs) at fair value, with the changes in fair value recorded in the Consolidated Statement of Income. Management is currently evaluating the impact and timing of the adoption of SFAS 156 on the Company s financial condition, results of operations and cash flows.

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In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements. SFAS No. 157 establishes a framework for measuring fair value and expands disclosures about fair value measurements. SFAS No. 157 clarifies the definition of exchange price as the price between market participants in an orderly transaction to sell an asset or transfer a liability in the market in which the reporting entity would transact for the asset or liability, that is, the principal or most advantageous market for the asset or liability. The changes to current practice resulting from the application of this statement relate to the definition of fair value, the methods used to measure fair value, and the expanded disclosures about fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. The Company does not anticipate that the adoption of this new accounting principle will have a material effect on its financial position, results of operations or cash flows.

On February 15, 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, which allows an entity the irrevocable option to elect fair value for the initial and subsequent measurement for certain financial assets and liabilities on a

contract-by-contract basis. Subsequent changes in fair value of these financial assets and liabilities would be recognized in earnings when they occur. SFAS No. 159 further establishes certain additional disclosure requirements. SFAS No. 159 is effective for the Company s financial statements for the year beginning on July 1, 2008, with earlier adoption permitted. Management is currently evaluating the impact and timing of the adoption of SFAS 159 on the Company s financial condition, results of operations and cash flows.

In June 2006, the FASB issued Interpretation No. 48 (FIN 48), Accounting for Uncertainty in Income Taxes. FIN 48 provides detailed guidance for the financial statement recognition, measurement and disclosure of uncertain tax positions recognized in an enterprise s financial statements in accordance with SFAS No. 109, Accounting for Income Taxes. FIN 48 requires an entity to recognize the financial statement impact of a tax position when it is more likely than not that the position will be sustained upon examination. If the tax position meets the more-likely-than-not recognition threshold, the tax effect is recognized at the largest amount of the benefit that is greater than 50% likely of being realized upon ultimate settlement. Any difference between the tax position taken in the tax return and the tax position recognized in the financial statements using the criteria above results in the recognition of a liability in the financial statements for the unrecognized benefit. Similarly, if a tax position fails to meet the more-likely-than-not recognition threshold, the benefit taken in tax return will also result in the recognition of a liability in the financial statements for the full amount of the unrecognized benefit.

FIN 48 will be effective for fiscal years beginning after December 15, 2006 (including the first interim period for calendar year companies) and the provisions of FIN 48 will be applied to all tax positions under SFAS No. 109 upon initial adoption. The cumulative effect of applying the provisions of this interpretation will be reported as an adjustment to the opening balance of retained earnings for that fiscal year. The Company does not anticipate that the adoption of this new accounting principle will have a material effect on its financial position, results of operations or cash flows.

Application of Critical Accounting Policies

There are a number of accounting estimates performed by the Company in preparing its financial statements. Some of the estimates are developed internally, while others are obtained from independent third parties. Examples of estimates using external sources are the fair market value of investment securities, fair value of mortgage servicing rights, deferred compensation, and appraised value of foreclosed properties. It is management s assertion that the external sources have access to resources, methodologies, and markets that provide adequate assurances that no material impact would occur due to changes in assumptions. The following accounting estimates are performed internally:

Allowance for Loan and Lease Losses (ALLL).

Management applies its knowledge of current local economic and real estate market conditions, historical experience, loan portfolio composition, and the assessment of delinquent borrowers situations, to determine the adequacy of its ALLL reserve. These factors are reviewed by the Bank s federal banking regulator and the Company s external auditors on a regular basis. The current level of the ALLL reserve is deemed to be more than adequate given the above factors, with no material impact expected due to a difference in the assumptions.

Deferred Loan Fees.

Management applies time study and statistical analysis to determine loan origination costs to be capitalized under SFAS No. 91. The analysis is reviewed by the Company's external auditors for reasonableness. No material impact is expected if different assumptions are used, as many of our loans have a short duration.

Deferred Tax Assets.

Management expects to realize the deferred tax assets due to the continued profitability of the Company.

Fair Value of Other Financial Instruments.

Management uses an internal model to determine fair value for its loan portfolio and certificates of deposit. The assumptions entail spreads over the Treasury yield curve at appropriate maturity benchmarks. Assumptions incorporating different spreads would naturally deliver varying results; however, due to short-term nature of the loan portfolio and certificates of deposit, changes in the results would be mitigated. Currently, the fair value is only presented as footnote information, and changes due to new assumptions would not, in management s opinion, affect the reader s opinion of the Company s financial condition.

Economic Life of Fixed Assets.

Management determines the useful life of its buildings, furniture, and equipment for depreciation purposes. These estimates are reviewed by the Company's external auditors for reasonableness. No material impact is expected if different assumptions were to be used.

ITEM 7. FINANCIAL STATEMENTS.

Eagle Bancorp s audited financial statements, notes thereto, and auditor s reports are found immediately following Part III of this report.

ITEM 8A. CONTROLS AND PROCEDURES

Based on their evaluation, the registrant s Chief Executive Officer, Larry A. Dreyer, President, Peter J. Johnson and Chief Financial Officer, Clinton J. Morrison, have concluded the registrant s disclosure controls and procedures are effective as of June 30, 2007 to ensure that information required to be disclosed in the reports that the registrant files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission s rules and forms. During the last fiscal quarter, there have been no changes in the registrant s internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the registrant s internal control over financial reporting.

ITEM 8B. OTHER INFORMATION

None.

PART III

The information required by Items 9, 10, 11, 12 and 14 of this part is presented in the proxy statement issued by the Board of Directors in connection with the annual meeting of stockholders to be held October 18, 2007, which is hereby incorporated by reference into this annual report.

Item 13. Exhibits.

A. (1) The following documents are filed as part of this report: The audited Consolidated Statements of Financial Condition of Eagle Bancorp and subsidiary as of June 30, 2007 and June 30, 2006 and the related Consolidated Statements of Income, Consolidated Statements of Changes in Stockholder Equity and Consolidated Statements of Cash Flows for the years then ended, together with the related notes and independent auditor s reports.

(2) Schedules omitted as they are not applicable.

B. Exhibits

*	2.1	Amended and Restated Plan of Mutual Holding Company Reorganization and Stock Issuance
*	3.1	Charter of Eagle Bancorp
*	3.2	Bylaws of Eagle Bancorp
*	4	Form of Stock Certificate of Eagle Bancorp
*	10.1	Employee Stock Ownership Plan and Trust
*	10.2	Employment Contract of Larry A. Dreyer
**	10.3	Stock Plan
***	10.4	Employment Contract of Peter J. Johnson
	11	Computation of per share earnings (incorporated by reference to Note 3 to Notes To Consolidated Statements of Financial Condition dated June 30, 2007)
****	14	Code of Ethics
	21.1	Subsidiaries of Registrant (incorporated by reference to Part I, Subsidiary Activity)
	23.1	Consent of Davis, Kinard & Co., P.C.
	31.1	Certification by Larry A. Dreyer, Chief Executive Officer, pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
	31.2	

	Certification by Clinton J. Morrison, Chief Financial Officer, pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification by Larry A. Dreyer, Chief Executive Officer and Clinton J. Morrison, Chief Financial Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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* Incorporated by reference to the identically numbered exhibit of the Registration Statement on Form SB- 2 (File No. 333-93077) filed with the SEC on December 20, 1999.

** Incorporated by reference to the proxy statement for 2000 Annual Meeting filed with the SEC on September 19, 2000.

*** Incorporated by reference to the Form 8-K filed with the SEC on November 6, 2006.

**** Incorporated by reference to the Form 10-KSB filed with the SEC on September 16, 2004.

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AND SUBSIDIARY

CONSOLIDATED FINANCIAL STATEMENTS

and

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

June 30, 2007 and 2006

EAGLE BANCORP AND SUBSIDIARY

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of
Eagle Bancorp and Subsidiary

We have audited the accompanying consolidated statements of financial condition of **Eagle Bancorp and Subsidiary** as of June 30, 2007, and 2006 and the related consolidated statements of income, stockholders equity and cash flows for years then ended. These financial statements are the responsibility of the company s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. The company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the company s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the 2007 and 2006 financial statements referred to above present fairly, in all material respects, the financial position of **Eagle Bancorp and Subsidiary** as of June 30, 2007 and 2006, and the results of its operations and its cash flows for years then ended in conformity with accounting principles generally accepted in the United States of America.

DAVIS, KINARD & CO., P.C.

Abilene, Texas
July 24, 2007

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EAGLE BANCORP AND SUBSIDIARY
Consolidated Statements of Financial Condition
June 30, 2007 and 2006
(Dollars in Thousands, Except for Per Share Data)

	2007	2006
Assets		
Cash and due from banks	$ 2,709	$ 2,844
Interest bearing deposits in banks	360	27
Cash and cash equivalents	3,069	2,871
Securities available for sale	64,774	64,198
Securities held to maturity (fair value approximates $930 in 2007 and $1,030 in 2006)	921	1,018
FHLB stock restricted, at cost	1,315	1,315
Investment in Eagle Bancorp Statutory Trust I	155	155
Mortgage loans held for sale	1,175	918
Loans receivable, net of deferred loan fees and allowance for loan losses of $518 in 2007 and $535 in 2006	158,140	140,858
Accrued interest and dividend receivable	1,333	1,211
Mortgage servicing rights, net	1,628	1,722
Premises and equipment, net	5,806	5,962
Cash surrender value of life insurance	5,764	5,230
Other assets	606	720
	$244,686	$226,178

	2007	2006
Liabilities and Shareholders Equity		
Noninterest bearing	$ 13,694	$ 12,575
Interest bearing	165,953	161,767
Total deposits	179,647	174,342
Accrued expenses and other liabilities	1,996	1,765
Federal funds purchased	3,800	
FHLB advances and other borrowings	30,000	22,371
Subordinated debentures	5,155	5,155
Total liabilities	220,598	203,633
Shareholders equity		
Preferred stock, no par value; 1,000,000 shares authorized, no shares issued or outstanding		
Common stock, $0.01 par value; 9,000,000 shares authorized, 1,223,572 shares issued; 1,084,357 and		
1,091,722 shares outstanding in 2007 and 2006, respectively	12	12
Capital surplus	4,387	4,274
Unallocated common stock held by ESOP	(92)	(129)
Treasury stock, at cost	(4,759)	(4,521)
Retained earnings	25,448	24,056
Net accumulated other comprehensive loss	(908)	(1,147)
Total shareholders equity	24,088	22,545
	$244,686	$226,178

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

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EAGLE BANCORP AND SUBSIDIARY

Consolidated Statements of Income

Years Ended June 30, 2007 and 2006

(Dollars in Thousands, Except for Per Share Data)

	2007	2006
Interest and dividend income		
Loans, including fees	$ 9,731	$ 7,799
Available for sale securities	2,811	2,589
Held to maturity securities	43	52
Trust preferred securities	9	7
Federal Home Loan Bank stock dividends	7	
Deposits with banks	50	59
Total interest income	12,651	10,506
Interest expense		
Deposits	4,191	3,011
FHLB advances and other borrowings	1,466	546
Subordinated debentures	309	235

	2007	2006
Total interest expense	5,966	3,792
Net interest income	6,685	6,714
Provision for loan losses		
Net interest income after provision for loan losses	6,685	6,714
Noninterest income		
Service charges on deposit accounts	496	532
Net gain on sale of loans	643	492
Mortgage loan service fees	533	593
Net realized loss on sales of available for sale securities	(4)	
Other income	593	548
Total noninterest income	2,261	2,165
Noninterest expenses		
Salaries and employee benefits	3,617	3,519
Occupancy and equipment expense	824	848
Data processing	286	274
Advertising	247	201
Amortization of mortgage servicing rights	305	355
Federal insurance premiums	21	23
Postage	86	86
Legal, accounting, and examination fees	232	182
Consulting fees	79	58
ATM processing	49	51
Other expense	868	868
Total noninterest expenses	6,614	6,465
Income before income taxes	2,332	2,414
Income tax expense	554	629
Net income	$ 1,778	$ 1,785
Basic earnings per share	$ 1.66	$ 1.66
Diluted earnings per share	$ 1.47	$ 1.48

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

EAGLE BANCORP AND SUBSIDIARY

Consolidated Statements of Changes in Stockholders' Equity

Years Ended June 30, 2007 and 2006

(Dollars in Thousands, Except for Per Share Data)

	Preferred Stock	Common Stock
Balance at July 1, 2005	$	$ 12
Net income		
Change in net unrealized depreciation on available for sale securities and cash flow hedges, net		
Total comprehensive income		

	Preferred Stock	Common Stock
Dividends paid ($.80 per share)		
Restricted stock plan shares allocated (4,600)		
Treasury stock purchased (2,500 shares @ $31.75;		
1,200 shares @ $32.20; 1,000 shares @ $32.50;		
1,400 shares @ $34.45; 2,500 shares @ $34.25;		
1,300 shares @ $32.50; 4,000 shares @ $33.25;		
1,350 shares @ $33.10; 1,600 shares @ $31.00)		
ESOP shares allocated or committed to be released for allocation (4,600) shares		
Balance at June 30, 2006		12
Net income		
Change in net unrealized depreciation on available for sale securities and cash flow hedges, net		
Total comprehensive income		
Dividends paid ($.88 per share)		
Treasury stock purchased (3,100 shares @ $31.90;		
1,056 shares @ $32.00; 1,000 shares @ $32.60;		
1,200 shares @ $33.00; 1,000 shares @ $33.00;		
ESOP shares allocated or committed to be released for allocation (4,600) shares		
Balance at June 30, 2007	$	$ 12

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

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	Additional Paid-In Capital	Unallocated ESOP Shares	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Loss	Total
Balance at July 1, 2005	$ 4,188	$ (165)	$ (4,048)	$ 22,630	$ (352)	$ 22,265
Net income				1,785		1,785
Change in net unrealized depreciation on available for sale securities and cash flow hedges, net					(795)	(795)
Total comprehensive income						990
Dividends paid ($.80 per share)				(359)		(359)
Restricted stock plan shares allocated (4,600)	(27)		80			53
Treasury stock purchased (2,500 shares @ $31.75;						
1,200 shares @ $32.20; 1,000 shares @ $32.50;						
1,400 shares @ $34.45; 2,500 shares @ $34.25;						
1,300 shares @ $32.50; 4,000 shares @ $33.25;						
1,350 shares @ $33.10; 1,600 shares @ $31.00)			(553)			(553)
ESOP shares allocated or committed to be released for allocation (4,600) shares	113	36				149

	Additional Paid-In Capital	Unallocated ESOP Shares	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Loss	Total
Balance at June 30, 2006	4,274	(129)	(4,521)	24,056	(1,147)	22,545
Net income				1,778		1,778
Change in net unrealized depreciation on available for sale securities and cash flow hedges, net					239	239
Total comprehensive income						2,017
Dividends paid ($.88 per share)				(386)		(386)
Treasury stock purchased (3,100 shares @ $31.90; 1,056 shares @ $32.00; 1,000 shares @ $32.60; 1,200 shares @ $33.00; 1,000 shares @ $33.00;			(238)			(238)
ESOP shares allocated or committed to be released for allocation (4,600) shares	113	37				150
Balance at June 30, 2007	$ 4,387	$ (92)	$ (4,759)	$ 25,448	$ (908)	$ 24,088

EAGLE BANCORP AND SUBSIDIARY
Consolidated Statements of Cash Flows
Years Ended June 30, 2007 and 2006
(Dollars in Thousands, Except for Per Share Data)

	2007	2006
Cash flows from operating activities		
Net income	$ 1,778	$ 1,785
Adjustments to reconcile net income to net cash provided by operating activities		
Provision for mortgage servicing rights valuation losses		(46)
Depreciation	482	509
Net amortization of securities	503	924
Amortization of capitalized mortgage servicing rights	305	355
Loss on sale of foreclosed assets		6
Net gain on sale of loans	(643)	(492)
Net realized loss on sales of available for sale securities	4	
Appreciation in cash surrender value of life insurance, net	(191)	(181)
Restricted stock awards		53
Net change in		
Loans held for sale	387	1,711
Accrued interest receivable	(119)	(111)
Other assets	210	(192)
Accrued expenses and other liabilities	169	577
Net cash provided by operating activities	2,885	4,898
Cash flows from investing activities		

	2007	2006
Activity in available for sale securities		
Sales	5,122	1,627
Maturities, prepayments and calls	16,097	15,845
Purchases	(21,936)	(8,616)
Activity in held to maturity securities		
Maturities, prepayments and calls	111	164
Investment in Eagle Bancorp Statutory Trust I		(155)
Loan originations and principal collections, net	(17,522)	(34,273)
Purchase of bank owned life insurance	(342)	
Proceeds from sale of foreclosed assets		69
Additions to premises and equipment	(326)	(229)
Net cash used in investing activities	(18,796)	(25,568)
Cash flows from financing activities		
Net increase in deposits	5,305	1,848
Net change in federal funds purchased	3,800	
Net change in advances from the FHLB and other borrowings	7,628	12,484
Purchase of treasury stock, at cost	(238)	(553)
Proceeds from subordinated debentures		5,155
Dividends paid	(386)	(359)
Net cash provided by financing activities	16,109	18,575
Net change in cash and cash equivalents	198	(2,095)
Cash and cash equivalents at beginning of year	2,871	4,966
Cash and cash equivalents at end of year	$ 3,069	$ 2,871

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

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EAGLE BANCORP AND SUBSIDIARY
Notes to Consolidated Financial Statements
June 30, 2007 and 2006

NOTE 1: Summary of Significant Accounting Policies

Nature of Operations

Eagle Bancorp was organized in 2000 as the majority-owned subsidiary of Eagle Financial, MHC, (the Mutual Holding Company) and the sole parent of American Federal Savings Bank (the Bank). Collectively, Eagle Bancorp and the Bank are referred to herein as the Company.

The Bank is a federally chartered savings bank subject to the regulations of the Office of Thrift Supervision (OTS). The Bank is a member of the Federal Home Loan Bank System and its deposit accounts are insured to the applicable limits by the Federal Deposit Insurance Corporation (FDIC).

The Bank is headquartered in Helena, Montana, and operates additional branches in Butte, Bozeman, and Townsend, Montana. The Bank s market area is concentrated in south central Montana, to which it primarily offers commercial, residential, and consumer loans. The Bank s principal business is accepting deposits and, together with funds generated from operations and borrowings, investing in various types of loans and securities.

Principles of Consolidation

The consolidated financial statements include the accounts of Eagle Bancorp and the Bank. All significant intercompany transactions and balances have been eliminated in consolidation.

Use of Estimates

In preparing financial statements in conformity with U.S. generally accepted accounting principles, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, mortgage servicing rights, and the valuation of foreclosed assets. In connection with the determination of the estimated losses on loans, foreclosed assets, valuation of deferred tax assets and mortgage servicing rights management obtains independent appraisals and valuations.

Significant Group Concentrations of Credit Risk

Most of the Company s business activity is with customers located within the south-central Montana area. Note 3 discusses the types of securities that the Company invests in. Note 4 discusses the types of lending that the Company engages in. The Company does not have any significant concentrations to any one industry or customer.

The Company carries certain assets with other financial institutions which are subject to credit risk by the amount such assets exceed federal deposit insurance limits. At June 30, 2007 and June 30, 2006, no account balances were held with correspondent banks that were in excess of FDIC insured levels. Also, from time to time, the Company is due amounts in excess of FDIC insurance limits for checks and transit items. Management monitors the financial stability of correspondent banks and considers amounts advanced in excess of FDIC insurance limits to present no significant additional risk to the Company.

NOTE 1: Summary of Significant Accounting Policies - continued

Cash and Cash Equivalents

For the purpose of presentation in the consolidated statements of cash flows, cash and cash equivalents are defined as those amounts included in the balance sheet captions cash and due from banks, and interest-bearing deposits in banks, all of which mature within ninety days.

The Bank is required to maintain a reserve balance with the Federal Reserve Bank. The Bank properly maintained amounts in excess of required reserves of $391,000 and $488,000 as of June 30, 2007 and 2006, respectively.

Investment Securities

The Company designates debt and equity securities as held-to-maturity, available-for-sale, or trading.

Held-to-maturity Debt investment securities that management has the positive intent and ability to hold until maturity are classified as held-to-maturity and are carried at their remaining unpaid principal balance, net of unamortized premiums or unaccreted discounts. Premiums are amortized and discounts are accreted using the interest method over the period remaining until maturity.

Available-for-sale Investment securities that will be held for indefinite periods of time, including securities that may be sold in response to changes in market interest or prepayment rates, need for liquidity, and changes in the availability of and the yield of alternative investments, are classified as available-for-sale. These assets are carried at fair value. Unrealized gains and losses, net of tax, are reported as other comprehensive income. Gains and losses on the sale of available-for-sale securities are recorded on the trade date and determined using the specific identification method.

Declines in the fair value of individual held-to-maturity and available-for-sale securities below their cost that are other than temporary are recognized by write-downs of the individual securities to their fair value. Such write-downs would be included in earnings as realized losses.

Trading No investment securities were designated as trading at June 30, 2007 and 2006.

Federal Home Loan Bank Stock

The Company s investment in Federal Home Loan Bank (FHLB) stock is a restricted investment carried at cost ($100 per share par value), which approximates its fair value. As a member of the FHLB system, the Company is required to maintain a minimum level of investment in FHLB stock based on specific percentages of its outstanding FHLB advances. The Company may request redemption at par value of any stock in excess of the amount it is required to hold. Stock redemptions are made at the discretion of the FHLB. The FHLB redeemed no shares during the years ended June 30, 2007 and 2006.

NOTE 1: Summary of Significant Accounting Policies - continued

Mortgage Loans Held-for-Sale

Mortgage loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated market value, determined in aggregate, plus the fair value of associated derivative financial instruments. Net unrealized losses, if any, are recognized in a valuation allowance by a charge to income.

Loans

The Company grants mortgage, commercial and consumer loans to customers. A substantial portion of the loan portfolio is represented by mortgage loans in south central Montana. The ability of the Company s debtors to honor their contracts is dependent upon the general economic conditions in this area.

Loans receivable that management has the intent and ability to hold until maturity are reported at the outstanding principal balance adjusted for any charge-offs, allowance for loan losses, and any deferred fees or costs on originated loans and unamortized premiums or unaccreted discounts on purchased loans. Loan origination fees, net of certain direct origination costs are deferred and amortized over the contractual life of the loan, as an adjustment of the yield, using the interest method.

The accrual of interest on loans is discontinued at the time the loan is 90 days delinquent unless the credit is well secured and in process of collection. Personal loans are typically charged off no later than 180 days past due. Past due status is based on the contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

All interest accrued but not collected for loans that are placed on nonaccrual or charged off is reversed against interest income. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Allowance for Loan Losses

The allowance for loans losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management s periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower s ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revisions as more information becomes available.

NOTE 1: Summary of Significant Accounting Policies - continued

Allowance for Loan Losses - continued

The allowance consists of specific, general and unallocated components. For such loans that are classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers non-classified loans and is based on historical loss experience adjusted for qualitative factors. An unallocated component is maintained to cover uncertainties that could affect management s estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all the circumstances surrounding the loan and the borrower, including the length of delay, the reasons for the delay, the borrower s prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan by loan basis for commercial and construction loans by either the present value of expected future cash flows discounted at the loan s effective interest rate, the loan s obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Company does not separately identify individual consumer and residential loans for impairment disclosures, unless such loans are subject of a restructuring agreement.

Mortgage Servicing Rights

Servicing assets are recognized as separate assets when rights are acquired through purchase or through sale of financial assets. Generally, purchased servicing rights are capitalized at the cost to acquire the rights. For sales of mortgage loans, a portion of the cost of originating the loan is allocated to the servicing right based on relative fair value. Fair value is based on a market price valuation model that calculates the present value of estimated future net servicing income. The valuation model incorporates assumptions that market participants would use in estimating future net servicing income, such as the cost to service, the discount rate, the custodial earnings rate, an inflation rate, ancillary income, prepayment speeds and default rates and losses.

NOTE 1: Summary of Significant Accounting Policies - continued

Mortgage Servicing Rights - continued

Servicing assets are evaluated for impairment based upon the fair value of the rights as compared to amortized cost. Impairment is determined by stratifying rights into tranches based on predominant characteristics, such as interest rate, loan type and investor type. Impairment is recognized through a valuation allowance for an individual tranche, to the extent that the fair value is less than the capitalized amount for the tranches. If the Bank later determines that all or a portion of the impairment no longer exists for a particular tranche, a reduction of the allowance may be recorded as an increase to income. Capitalized servicing rights are reported in other assets and are amortized into noninterest income in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets.

Servicing fee income is recorded for fees earned for servicing loans. The fees are based on a contractual percentage of the outstanding principal and are recorded as income when earned. The amortization of mortgage servicing rights is netted against loan servicing fee income.

Cash Surrender Value of Life Insurance

Life insurance policies are initially recorded at cost at the date of purchase. Subsequent to purchase, the policies are periodically adjusted for fair value. The adjustment to fair value increases or decreases the carrying value of the policies and is recorded as an income or expense on the consolidated statement of income. For the years ended June 30, 2007 and 2006 there were no adjustments to fair value that were outside the normal appreciation in cash surrender value.

Foreclosed Assets

Assets acquired through, or in lieu of, loan foreclosure are initially recorded at the lower of the Company s carrying amount or fair value less estimated selling cost at the date of foreclosure. All write-downs based on the asset s fair value at the date of acquisition are charged to the allowance for loan losses. After foreclosure, property held for sale is carried at the lower of the new cost basis or fair value less cost to sell. Impairment losses on property to be held and used are measured as the amount by which the carrying amount of a property exceeds its fair value. Costs of significant property improvements are capitalized, whereas costs relating to holding property are expensed. Valuations are periodically performed by management, and any subsequent write-downs are recorded as a charge to operations, if necessary, to reduce the carrying value of a property to the lower of its cost or fair value less cost to sell.

Premises and Equipment

Land is carried at cost. Property and equipment is recorded at cost less accumulated depreciation. Depreciation is computed using the straight-line method over the expected useful lives of the assets, ranging from 3 to 35 years. The costs of maintenance and repairs are expensed as incurred, while major expenditures for renewals and betterments are capitalized.

NOTE 1: Summary of Significant Accounting Policies - continued

Income Taxes

Income taxes are accounted for under the asset and liability method. Accordingly, deferred taxes are recognized for the estimated future tax effects attributable to temporary differences between the financial statement carrying amounts and the tax basis of existing assets and liabilities. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which the temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax laws or rates is recognized in income tax expense in the period that includes the enactment date of the change. A deferred tax liability is recognized for all temporary differences that will result in future taxable income. A deferred tax asset is recognized for all temporary differences that will result in future tax deductions, subject to reduction of the asset by a valuation allowance in certain circumstances. This valuation allowance is recognized if, based on an analysis of available evidence, management determines that it is more likely than not that some portion or all of the deferred tax asset will not be realized. The valuation allowance is subject to ongoing adjustment based on changes in circumstances that affect management s judgment about the realizability of the deferred tax asset. Adjustments to increase or decrease the valuation allowance are charged or credited, respectively, to income tax expense.

Treasury Stock

Treasury stock is accounted for on the cost method and consists of 139,215 shares in 2007 and 131,850 shares in 2006.

Advertising Costs

The Company expenses advertising costs as they are incurred. Advertising costs were approximately $247,000 and $201,000 for the years ended June 30, 2007 and 2006, respectively.

Employee Stock Ownership Plan

Compensation expense recognized for the Company s ESOP equals the fair value of shares that have been allocated or committed to be released for allocation to participants. Any difference between the fair value of the shares at the time and the ESOP s original acquisition cost is charged or credited to stockholders equity (capital surplus). The cost of ESOP shares that have not yet been allocated or committed to be released is deducted from stockholders equity.

Earnings Per Share

Basic earnings per share (EPS) is calculated by dividing net income by the weighted average number of common shares outstanding for the period. Diluted EPS is calculated by dividing net income by the weighted average number of common shares used to compute basic EPS plus the

incremental amount of potential common stock determined by the treasury stock method. For purposes of computing EPS, outstanding common shares include all shares issued to the Mutual Holding Company but exclude ESOP shares that have not been allocated or committed to be released for allocation to participants.

NOTE 1: Summary of Significant Accounting Policies - continued

Financial Instruments

All derivative financial instruments that qualify for hedge accounting are recognized in the financial statements and measured at fair value regardless of the purpose or intent for holding them. Changes in the fair value of derivative financial instruments used as cash flow hedges are recognized as a component of comprehensive income. At June 30, 2007 and 2006, the Company was holding forward delivery commitments that qualify as derivative financial instruments.

The carrying value of the Company s financial instruments approximates fair value. The fair value of the Company s financial instruments is generally determined by a third party s valuation of the underlying asset.

Recent Accounting Pronouncements

In December 2003, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 46R, Consolidation of Variable Interest Entities an Interpretation of ARB No. 51 (FIN 46R). This Interpretation, which replaces FASB Interpretation No. 46, Consolidation of Variable Interest Entities , clarifies the application of Accounting Research Bulletin No. 51, Consolidated Financial Statements , for certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support.

On September 28, 2005, the Company issued trust-preferred securities through a wholly-owned subsidiary trust, further described in Note 9. Under the provisions of FIN 46R, the Company accounts for its investment in the trust as an asset and its junior subordinated debentures as a liability. Additionally, the Company reports the dividends paid and received on the securities in the statement of income as interest income and expense.

In February 2006, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 155, *Accounting for Certain Hybrid Financial Instruments, an amendment of FASB Statements No. 133 and 140.* SFAS No. 155 improves financial reporting by eliminating the exemption from applying SFAS No. 133 to interests in securitized financial assets so that similar instruments are accounted for similarly regardless of the form of the instruments. This statement also improves financial reporting by allowing a preparer to elect fair value measurement at acquisition, at issuance, or when a previously recognized financial instrument is subject to a remeasurement (new basis) event, on an instrument-by-instrument basis, in cases in which a derivative would otherwise have to be bifurcated. SFAS No. 155 is effective for all financial instruments acquired, issued, or subject to a remeasurement (new basis) event occurring after the beginning of the Company s first fiscal year that begins after September 15, 2006. The Company does not anticipate that the adoption of this new accounting principle will have a material effect on its financial position, results of operations or cash flows.

NOTE 1: Summary of Significant Accounting Policies - continued

Recent Accounting Pronouncements - continued

On March 17, 2006, the FASB issued SFAS No. 156, *Accounting for Servicing of Financial Assets, an amendment of SFAS No. 140,* which permits, but does not require, an entity to account for one or more classes of servicing rights (i.e., mortgage servicing rights, or MSRs) at fair value, with the changes in fair value recorded in the Consolidated Statement of Income. Management is currently evaluating the impact and

timing of the adoption of SFAS 156 on the Company s financial condition, results of operations and cash flows.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements.* SFAS No. 157 establishes a framework for measuring fair value and expands disclosures about fair value measurements. SFAS No. 157 clarifies the definition of exchange price as the price between market participants in an orderly transaction to sell an asset or transfer a liability in the market in which the reporting entity would transact for the asset or liability, that is, the principal or most advantageous market for the asset or liability. The changes to current practice resulting from the application of this statement relate to the definition of fair value, the methods used to measure fair value, and the expanded disclosures about fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. The Company does not anticipate that the adoption of this new accounting principle will have a material effect on its financial position, results of operations or cash flows.

On February 15, 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities,* which allows an entity the irrevocable option to elect fair value for the initial and subsequent measurement for certain financial assets and liabilities on a contract-by-contract basis. Subsequent changes in fair value of these financial assets and liabilities would be recognized in earnings when they occur. SFAS No. 159 further establishes certain additional disclosure requirements. SFAS No. 159 is effective for the Company s financial statements for the year beginning on July 1, 2008, with earlier adoption permitted. Management is currently evaluating the impact and timing of the adoption of SFAS 159 on the Company s financial condition, results of operations and cash flows.

In June 2006, the FASB issued Interpretation No. 48 (FIN 48), *Accounting for Uncertainty in Income Taxes.* FIN 48 provides detailed guidance for the financial statement recognition, measurement and disclosure of uncertain tax positions recognized in an enterprise s financial statements in accordance with SFAS No. 109, Accounting for Income Taxes. FIN 48 requires an entity to recognize the financial statement impact of a tax position when it is more likely than not that the position will be sustained upon examination. If the tax position meets the more-likely-than-not recognition threshold, the tax effect is recognized at the largest amount of the benefit that is greater than 50% likely of being realized upon ultimate settlement. Any difference between the tax position taken in the tax return and the tax position recognized in the financial statements using the criteria above results in the recognition of a liability in the financial statements for the unrecognized benefit. Similarly, if a tax position fails to meet the more-likely-than-not recognition threshold, the benefit taken in tax return will also result in the recognition of a liability in the financial statements for the full amount of the unrecognized benefit.

NOTE 1: Summary of Significant Accounting Policies - continued

Recent Accounting Pronouncements - continued

FIN 48 will be effective for fiscal years beginning after December 15, 2006 (including the first interim period for calendar year companies) and the provisions of FIN 48 will be applied to all tax positions under SFAS No. 109 upon initial adoption. The cumulative effect of applying the provisions of this interpretation will be reported as an adjustment to the opening balance of retained earnings for that fiscal year. The Company does not anticipate that the adoption of this new accounting principle will have a material effect on its financial position, results of operations or cash flows.

Reclassifications

Certain 2006 amounts have been reclassified to conform to the 2007 presentation.

NOTE 2: Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per share for the years ended June 30:

	2007	**2006**
(In Thousands)		
Weighted average shares outstanding during the year on which basic earnings per share is calculated	1,073	1,078
Add: weighted average of stock held in treasury	137	127

	2007	2006
Average outstanding shares on which diluted earnings per share is calculated	1,210	1,205
Net income applicable to common stockholders	$1,778	$1,785
Basic earnings per share	$ 1.66	$ 1.66
Diluted earnings per share	$ 1.47	$ 1.48

NOTE 3: Securities

The Company s investment policy requires that the Company purchase only high-grade investment securities. Municipal obligations are categorized as AAA or better by a nationally recognized statistical rating organization. These ratings are achieved because the securities are backed by the full faith and credit of the municipality and also supported by third-party credit insurance policies. Mortgage backed securities and collateralized mortgage obligations are issued by government sponsored corporations, including Federal Home Loan Mortgage Corporation, Fannie Mae, and the Guaranteed National Mortgage Association. The amortized cost and estimated fair values of securities, together with unrealized gains and losses, are as follows:

EAGLE BANCORP AND SUBSIDIARY
Notes to Consolidated Financial Statements
June 30, 2007 and 2006

NOTE 3: Securities continued

	June 30, 2007			
(Dollars in Thousands) **Available for Sale**	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Estimated Market Value**
U.S. Government and agency	$ 3,690	$ 5	$ (52)	$ 3,643
Municipal obligations	21,198	58	(528)	20,728
Corporate obligations	13,847		(224)	13,623
Mortgage-backed securites	8,107	3	(238)	7,872
CMOs	17,408	4	(337)	17,075
Corporate preferred stock	2,000		(167)	1,833
Total securities available for sale	$66,250	$70	$(1,546)	$64,774
Held to Maturity				
Municipal obligations	$ 826	$ 9	$	$ 835
Mortgage-backed securites	95			95
Total securities held to maturity	$ 921	$ 9	$	$ 930

	June 30, 2006			
(Dollars in Thousands) **Available for Sale**	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Estimated Market Value**
U.S. Government and agency	$ 7,448	$ 6	$ (158)	$ 7,296

	June 30, 2006			
Municipal obligations	17,471	67	(395)	17,143
Corporate obligations	16,059		(442)	15,617
Mortgage-backed securites	6,949	2	(204)	6,747
CMOs	16,330		(513)	15,817
Corporate preferred stock	1,800		(222)	1,578
Total securities available for sale	$66,057	$75	$(1,934)	$64,198
Held to Maturity				
Municipal obligations	$ 828	$14	$ (2)	$ 840
Mortgage-backed securites	190			190
Total securities held to maturity	$ 1,018	$14	$ (2)	$ 1,030

EAGLE BANCORP AND SUBSIDIARY
Notes to Consolidated Financial Statements
June 30, 2007 and 2006

NOTE 3: Securities - continued

The Company has not entered into any interest rate swaps, options, or futures contracts relating to investment securities.

Gross recognized gains on securities available-for-sale were $27,996 and $9,286 for the years ended June 30, 2007 and 2006, respectively. Gross recognized losses on securities available-for-sale were $32,332 and $9,893 for the years ended June 30, 2007 and 2006, respectively.

The amortized cost and estimated fair value of securities at June 30, 2007 by contractual maturity are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	June 30, 2007			
	Held to Maturity		Available for Sale	
(Dollars in Thousands)	Amortized Cost	Estimated Market Value	Amortized Cost	Estimated Market Value
Due in one year or less	$150	$150	$ 6,953	$ 6,868
Due from one to five years	411	414	9,276	9,101
Due from five to ten years	265	271	3,483	3,385
Due after ten years			19,023	18,640
	826	835	38,735	37,994
Mortgage-backed	95	95	8,107	7,872
CMOs			17,408	17,075
Corporate preferred stock			2,000	1,833
Total	$921	$930	$66,250	$64,774

Maturities of securities do not reflect repricing opportunities present in adjustable rate securities.

At June 30, 2007 and 2006, securities with a carrying value of $24,452,665 and $9,055,000, respectively, were pledged to secure public deposits and for other purposes required or permitted by law.

EAGLE BANCORP AND SUBSIDIARY
Notes to Consolidated Financial Statements
June 30, 2007 and 2006

NOTE 3: Securities - continued

The following table discloses, as of June 30, 2007 and 2006, the Company s investment securities that have been in a continuous unrealized-loss position for less than 12 months and those that have been in a continuous unrealized loss position for 12 or more months:

	June 30, 2007			
	Less than 12 months		12 months or longer	
(Dollars in Thousands)	Estimated Market Value	Gross Unrealized Losses	Estimated Market Value	Gross Unrealized Losses
U.S. Government and agency	$	$	$ 2,820	$ 52
Municipal obligations	12,338	369	4,023	159
Corporate obligations	4,075	75	9,548	149
Mortgage-backed & CMOs	6,617	183	15,292	392
Corporate preferred stock	380	20	1,453	147
Total	$23,410	$647	$33,136	$899

The table above shows the Company s investment gross unrealized losses and fair values, aggregated by investment category and length of time that the individual securities have been in a continuous unrealized loss position at June 30, 2007 and 2006. 168 and 180 securities are in an unrealized loss position as of June 30, 2007 and 2006, respectively.

Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Bank to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

EAGLE BANCORP AND SUBSIDIARY
Notes to Consolidated Financial Statements
June 30, 2007 and 2006

NOTE 3: Securities - continued

At June 30, 2007, sixty U.S. Government and agency securities and municipal obligations have unrealized losses with aggregate depreciation of less than 3% from the Company s amortized cost basis. These unrealized losses are principally due to rising interest rates. In analyzing an issuer s financial condition, management considers whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred, and industry analysts reports. As management has the ability to hold debt securities until maturity, or for the foreseeable future if classified as available for sale, no declines are deemed to be other than temporary.

At June 30, 2007, eighty-eight mortgage backed and CMO securities have unrealized losses with aggregate depreciation of 3% from the Company s cost basis. These unrealized losses are principally due to rising interest rates. No credit issues have been identified that cause management to believe the declines in market value are other than temporary. In analyzing the issuer s financial condition, management considers industry analysts reports, financial performance and projected target prices of investment analysts within a one-year time frame. As

management has the ability to hold debt securities until maturity, or for the foreseeable future if classified as available for sale, no declines are deemed to be other than temporary.

At June 30, 2007, sixteen corporate obligations have unrealized losses with aggregate depreciation of 2% from the Company s cost basis. These unrealized losses are principally due to rising interest rates. No credit issues have been identified that cause management to believe the declines in market value are other than temporary. In analyzing the issuer s financial condition, management considers industry analysts reports, financial performance and projected target prices of investment analysts within a one-year time frame. As management has the ability to hold debt securities until maturity, or for the foreseeable future if classified as available for sale, no declines are deemed to be other than temporary.

At June 30, 2007, four corporate preferred stocks have unrealized losses with aggregate depreciation of 8% from the Company s cost basis. These unrealized losses are principally due to rising interest rates. No credit issues have been identified that cause management to believe the declines in market value are other than temporary. In analyzing the issuer s financial condition, management considers industry analysts reports, financial performance and projected target prices of investment analysts within a one-year time frame. As management has the ability to hold these securities for the foreseeable future, no declines are deemed to be other than temporary.

NOTE 4: Loans

A summary of the balances of loans follow:

	June 30,	
	2007	**2006**
(Dollars in Thousands)		
First mortgage loans:		
Residential mortgage (1 4 family)	$ 81,958	$ 75,913
Commercial real estate	25,621	18,648
Real estate construction	8,253	6,901
Other loans:		
Home equity	24,956	20,191
Consumer	11,438	11,820
Commercial	6,366	7,861
Subtotal	158,592	141,334
Less: Allowance for loan losses	(518)	(535)
Deferred loan fees, net	66	59
Total loans, net	$ 158,140	$ 140,858

Loans net of related allowance for loan losses on which the accrual of interest has been discontinued were $21,470 and $345,000 at June 30, 2007 and 2006, respectively. Interest income not accrued on these loans and cash interest income was immaterial for the years ended June 30, 2007 and 2006. The allowance for loan losses on nonaccrual loans as of June 30, 2007 and 2006 was $35,509 and $31,488, respectively. The Company expects to collect all amounts due on nonaccrual loans, including interest accrued at contractual rates. Accordingly, there are no loans considered impaired at June 30, 2007 and 2006. As of June 30, 2007 and 2006, the Company had $191,000 and $144,000, respectively, of loans past due greater than ninety days that were still accruing interest.

The following is a summary of changes in the allowance for loan losses:

	June 30,	
	2007	**2006**

	June 30,	
(Dollars in Thousands)		
Balance at beginning of period	$535	$573
Reclassification to repossessed property reserve		(15)
Provision for loan losses		
Loans charged off	(29)	(48)
Recoveries of loans previously charged off	12	25
Balance at end of period	$518	$535

NOTE 4: Loans - continued

Loans are granted to directors and officers of the Company in the ordinary course of business. Such loans are made in accordance with policies established for all loans of the Company, except that directors, officers, and employees may be eligible to receive discounts on loan origination costs.

Loans receivable from directors and senior officers of the Company at June 30, 2007 and 2006, were $152,901and $135,172, respectively. During the year ended June 30, 2007, total principal additions amounted to $51,433, and total principal payments amounted to $69,162. Interest income from these loans was $8,905 and $11,136 for the years ended June 30, 2007 and 2006, respectively.

NOTE 5: Mortgage Servicing Rights

The Company is servicing loans for the benefit of others totaling approximately $194,624,000 and $197,773,000 at June 30, 2007 and 2006, respectively. Servicing loans for others generally consists of collecting mortgage payments, maintaining escrow accounts, disbursing payments to investors, and foreclosure processing.

Custodial escrow balances maintained in connection with the foregoing loan servicing, and included in demand deposits, were approximately $1,946,000 and $1,518,000 at June 30, 2007 and 2006, respectively.

The following is a summary of activity in mortgage servicing rights and the valuation allowance:

	Years Ended June 30,	
	2007	2006
(Dollars in Thousands)		
Mortgage servicing rights		
Balance at beginning of period	$1,722	$1,903
Mortgage servicing rights capitalized	211	174
Amortization of mortgage servicing rights	(305)	(355)
Balance at end of period	1,628	1,722
Valuation allowance		
Balance at beginning of period		46
Provision (credited) to operations		(46)
Balance at end of period		
Net mortgage servicing rights	$1,628	$1,722

The fair values of these rights were $2,114,000 and $2,043,000 at June 30, 2007 and June 30, 2006, respectively. The fair value of servicing rights was determined using discount rates ranging from 10% to 18%, prepayment speeds ranging from 111% to 329%, depending on stratification of the specific right. The fair value was also adjusted for the affect of potential past dues and foreclosures.

NOTE 6: Premises and Equipment

A summary of the cost and accumulated depreciation of premises and equipment follows:

	June 30,	
	2007	**2006**
(Dollars in Thousands)		
Land, buildings, and improvements	$ 8,094	$ 7,991
Furniture and equipment	4,231	4,042
	12,325	12,033
Accumulated depreciation	(6,519)	(6,071)
	$ 5,806	$ 5,962

Depreciation expense totaled $482,580 and $509,170 for the years ended June 30, 2007 and 2006, respectively.

NOTE 7: Deposits

Deposits are summarized as follows:

	June 30,	
	2007	**2006**
(Dollars in Thousands)		
Noninterest checking	$ 13,694	$ 12,575
Interest bearing checking (0.21%, 0.20%)	30,953	29,571
Passbook savings (0.65%, 0.65%)	22,521	24,438
Money market accounts (2.12%, 1.93%)	23,292	29,129
Time certificates of deposits (2007 2.71% 5.35%, 2006 2.13% 5.07%)	89,187	78,629
	$179,647	$174,342

The weighted average cost of funds was 2.64% and 2.05% at June 30, 2007 and 2006, respectively.

June 30, 2007 and 2006

NOTE 7: Deposits - continued

At June 30, 2007, the scheduled maturities of time deposits are as follows:

(Dollars in Thousands)	
Within one year	$74,365
One to two years	13,499
Two to three years	930
Three to four years	384
Thereafter	9
Total	$89,187

Interest expense on deposits is summarized as follows:

	Years Ended June 30,	
	2007	**2006**
(Dollars in Thousands)		
Checking	$ 64	$ 55
Passbook savings	151	164
Money market accounts	525	492
Time certificates of deposits	3,451	2,300
	$4,191	$3,011

Effective April 1, 2006 FDIC insurance increased to $250,000 for qualified retirement accounts. For nonqualified retirement accounts, the coverage remains at $100,000. At June 30, 2007 and 2006, the Company held $34,859,000 and $31,403,000, respectively, in non-retirement deposit accounts that included balances in excess of $100,000 or more. At June 30, 2007 and 2006, the Company held $275,000 and $276,000, respectively, in qualified retirement deposit accounts that included balances in excess of $250,000. Deposit amounts above $100,000, and $250,000 for retirement accounts may not be insured by the FDIC, depending upon the underlying ownership of the account.

At June 30, 2007 and 2006, the Company reclassified $21,322 and $20,260, respectively, in overdrawn deposits as loans.

Directors and senior officers deposit accounts at June 30, 2007 and 2006, were $289,049 and $543,063, respectively.

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EAGLE BANCORP AND SUBSIDIARY
Notes to Consolidated Financial Statements
June 30, 2007 and 2006

NOTE 8: Advances from the Federal Home Loan Bank and other borrowings

Advances from the Federal Home Loan Bank of Seattle and other borrowings mature as follows: June 30,

	June 30,	
	2007	**2006**
(Dollars in Thousands)		

	June 30,	
Within one year	$ 2,000	$ 16,371
One to two years	2,000	2,000
Two to three years	7,000	2,000
Three to four years		2,000
Four to five years	19,000	
Thereafter		
Total	$ 30,000	$ 22,371

Federal Home Loan Advances

The advances are due at maturity, with the exception of a $5,000,000 advance that is callable at the FHLB of Seattle s option. This advance was called on August 1, 2007. The advances are subject to prepayment penalties. The interest rates on advances are fixed, with the exception of one advance which is adjustable (tied to the three month LIBOR). The advances are collateralized by investment securities pledged to the FHLB of Seattle and a blanket pledge of the Bank s 1-4 family residential mortgage portfolio. The carrying value of the securities collateralized for these advances was $5,281,282 as of June 30, 2007. At June 30, 2007 and 2006, the Company exceeded the collateral requirements of the FHLB. The Company s investment in FHLB stock is also pledged as collateral on these advances. The total FHLB funding line available to the Company at June 30, 2007, was 30% of total Bank assets, or approximately $72,091,000. The balance of advances was $16,000,000 and $22,371,000 at June 30, 2007 and 2006, respectively.

Other Borrowings

The Bank had $14,000,000 in structured repurchase agreements with PNC Financial Service Group, Inc. (PNC) at June 30, 2007. These agreements are collateralized by corporate and municipal securities. The carrying value of these securities was $17,214,907 as of June 30, 2007. These agreements include terms, under certain conditions, which allow PNC to exercise a call option.

Federal Funds Purchased

During the year the Bank obtained a $6,000,000 Federal Funds line of credit with PNC. The balance was $3,800,000 at June 30, 2007.

For all borrowings the weighted average interest rate for advances at June 30, 2007 and 2006 was 4.90% and 4.96% respectively. The weighted average amount outstanding was $29,071,000 and $12,665,000 for the years ended June 30, 2007 and 2006, respectively.

The maximum amount outstanding at any month-end was $36,695,185 and $22,602,000 during the years ended June 30, 2007 and 2006, respectively.

NOTE 9: Subordinated Debentures

On September 28, 2005, the Company completed the private placement of $5,155,000 in subordinated debentures to Eagle Bancorp Statutory Trust I (the Trust). The Trust funded the purchase of the subordinated debentures through the sale of trust preferred securities to First Tennessee Bank, N.A. with a liquidation value of $5,155,000. Using interest payments made by the Company on the debentures, the Trust began paying quarterly dividends to preferred security holders on December 15, 2005. The annual percentage rate of the interest payable on the subordinated debentures and distributions payable on the preferred securities is fixed at 6.02% until December 15, 2010 then becomes variable at 3-Month LIBOR plus 1.42%. Dividends on the preferred securities are cumulative and the Trust may defer the payments for up to five years. The preferred securities mature in December 15, 2035 unless the Company elects and obtains regulatory approval to accelerate the maturity date to as early as December 15, 2010.

For the years ended June 30, 2007 and June 30, 2006, interest expense on the subordinated debentures was $309,000 and 235,000, respectively.

Subordinated debt may be included in regulatory Tier 1 capital subject to a limitation that such amounts not exceed 25% of Tier 1 capital. The remainder of subordinated debt is included in Tier II capital. There is no limitation for inclusion of subordinated debt in total risk-based capital and, as such, all subordinated debt was included in total risk-based capital.

NOTE 10: Legal Contingencies

Various legal claims also arise from time to time in the normal course of business which, in the opinion of management, will have no material effect on the Company s financial statements.

NOTE 11: Income Taxes

The components of the Company s income tax provision are as follows:

	Years Ended June 30,	
	2007	**2006**
(Dollars in Thousands)		
Current		
U.S. federal	$492	$531
Montana	154	143
	646	674
Deferred		
U.S. federal	(76)	(37)
Montana	(16)	(8)
	(92)	(45)
Total	$554	$629

EAGLE BANCORP AND SUBSIDIARY
Notes to Consolidated Financial Statements
June 30, 2007 and 2006

NOTE 11: Income Taxes - continued

The nature and components of deferred tax assets and liabilities, which are a component of other assets in 2007 and 2006 in the accompanying statement of financial condition, are as follows:

	June 30,	
	2007	**2006**
(Dollars in Thousands)		
Deferred tax assets:		
Deferred compensation	$323	$ 307
Loans receivable	57	56
Securities available for sale	548	702
Other	23	18
Total deferred tax assets	951	1,083
Deferred tax liabilities:		
Premises and equipment	175	227
Deferred loan fees	12	22

	June 30,	
FHLB stock	490	490
Unrealized gain on hedging	7	6
Other		17
Total deferred tax liabilities	684	762
Net deferred tax asset	$267	$ 321

The Company believes, based upon the available evidence, that all deferred tax assets will be realized in the normal course of operations. Accordingly, these assets have not been reduced by a valuation allowance.

A reconciliation of the Company s effective income tax provision to the statutory federal income tax rate is as follows:

	Years Ended June 30,	
	2007	**2006**
(Dollars in Thousands)		
Federal income taxes at the statutory rate of 34%	$ 793	$ 821
State income taxes	138	135
Nontaxable income	(333)	(312)
Other, net	(44)	(15)
Income tax expense	$ 554	$ 629
Effective tax rate	23.8%	26.1%

EAGLE BANCORP AND SUBSIDIARY
Notes to Consolidated Financial Statements
June 30, 2007 and 2006

NOTE 11: Income Taxes - continued

Prior to January 1, 1987, the Company was allowed a special bad debt deduction limited generally in the current year to 32% (net of preference tax) of otherwise taxable income and subject to certain limitations based on aggregate loans and savings account balances at the end of the year. If the amounts that qualified as deductions for federal income tax purposes are later used for purposes other than for bad debt losses, they will be subject to federal income tax at the then current corporate rate. Retained earnings include approximately $915,000 at June 30, 2007 and 2006, for which federal income tax has not been provided.

NOTE 12: Comprehensive Income

Comprehensive income represents the sum of net income and items of other comprehensive income that are reported directly in stockholders equity, such as the change during the period in the after-tax net unrealized gain or loss on securities available-for-sale.

The Company's other comprehensive income (loss) is summarized as follows for the years ended June 30:

	2007	**2006**
(Dollars in Thousands)		
Net unrealized holding gain or loss arising during the year:		

	2007	2006
Available for sale securities, net of related income tax (benefit) expense of $144 and $(480), respectively	$239	$(788)
Forward delivery commitments, net of related income tax (benefit) expense of $(1) and $(5), respectively	2	(7)
Reclassification adjustment for net realized gain included in net income, net of related income tax expense (benefit) of $(2) and $0, respectively	(2)	
Other comprehensive (loss) income	$239	$(795)

NOTE 13: Supplemental Cash Flow Information

	Years Ended June 30,	
	2007	2006
(Dollars in Thousands)		
Supplemental Cash Flow Information		
Cash paid during the year for interest	$6,018	$3,948
Cash paid during the year for income taxes	531	640
Non-Cash Investing Activities		
Decrease (increase) in market value of securities available for sale	$ (382)	$1,265
Mortgage servicing rights capitalized	211	174
ESOP shares released	149	150

NOTE 14: Regulatory Capital Requirements

The Bank is subject to various regulatory capital requirements administered by federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Bank s financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank s assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank s capital amounts and classifications are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of tangible and core capital (as defined in the regulations) to total adjusted assets (as defined), and of risk-based capital (as defined) to risk-weighted assets (as defined). Management believes, as of June 30, 2007 and 2006, that the Bank meets all capital adequacy requirements to which it is subject.

The most recent notification from the Office of Thrift Supervision (OTS) (as of June 4, 2007) categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well-capitalized, the Bank must maintain minimum tangible, core, and risk-based ratios as set forth in the table below. The Bank s actual capital amounts (in thousands) and ratios are presented in the table below:

NOTE 14: Regulatory Capital Requirements - continued

(Dollars in Thousands)	Actual		Minimum Capital Requirement		Minimum To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**
June 30, 2007:						
Total Risk-based Capital to Risk Weighted Assets						
Consolidated	$ 30,382	17.30%	$ 14,048	8.00%	$ N/A	N/A
Bank	25,797	14.78	13,967	8.00	17,459	10.00
Tier I Capital to						
Risk Weighted Assets						
Consolidated	29,899	17.03	7,024	4.00	N/A	N/A
Bank	25,314	14.50	6,984	4.00	21,691	6.00
Tier I Capital to						
Adjusted Total Assets						
Consolidated	29,899	12.15	7,375	3.00	N/A	N/A
Bank	25,314	10.48	7,246	3.00	12,076	5.00
Tangible Capital to						
Adjusted Total Assets						
Consolidated	29,899	12.15	3,687	1.50	N/A	N/A
Bank	25,314	10.48	3,623	1.50	N/A	N/A
June 30, 2006:						
Total Risk-based Capital to Risk Weighted Assets						
Consolidated	29,212	17.93	13,035	8.00	N/A	N/A
Bank	25,590	15.79	12,961	8.00	16,202	10.00
Tier I Capital to						
Risk Weighted Assets						
Consolidated	28,554	17.52	6,518	4.00	N/A	N/A
Bank	25,087	15.48	6,481	4.00	9,721	6.00
Tier I Capital to						
Adjusted Total Assets						
Consolidated	28,554	12.52	6,481	3.00	N/A	N/A
Bank	25,087	11.16	6,742	3.00	11,237	5.00
Tangible Capital to						
Adjusted Total Assets						
Consolidated	28,554	12.52	3,420	1.50	N/A	N/A
Bank	25,087	11.16	3,371	1.50	N/A	N/A

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NOTE 14: Regulatory Capital Requirements - continued

A reconciliation of the Bank s capital (in thousands) determined by generally accepted accounting principles to capital defined for regulatory purposes, is as follows:

	June 30,	
	2007	**2006**
(Dollars in Thousands)		
Capital determined by generally accepted accounting principles	$24,595	$24,144
Unrealized loss on securities available-for-sale	826	1,091
Unrealized loss on equity securities	(96)	(138)
Unrealized gain on forward delivery commitments	(11)	(10)
Tier I (core) capital	25,314	25,087
General allowance for loan losses	483	503
Total risk based capital	$25,797	$25,590

Dividend Limitations

Under OTS regulations that became effective April 1, 1999, savings associations such as the Bank generally may declare annual cash dividends up to an amount equal to net income for the current year plus net income retained for the two preceding years. Dividends in excess of such amount require OTS approval. The Bank has paid dividends totaling $1,716,904 and $1,433,000 to the Company during the years ended June 30, 2007, and 2006, respectively. The Company had paid four quarterly dividends of $0.22 per share to its shareholders for the year ended June 30, 2007, and four quarterly dividends of $0.20 per share to its shareholders for the year ended June 30, 2006.

Liquidation Rights

All depositors who had liquidation rights with respect to the Bank as of the effective date of the Reorganization continue to have such rights solely with respect to the Mutual Holding Company, as long as they continue to hold deposit accounts with the Bank. In addition, all persons who become depositors of the Bank subsequent to the Reorganization will have liquidation rights with respect to the Mutual Holding Company.

NOTE 15: Related Party Transactions

The Bank has contracted with a subsidiary of a company which is partially owned by one of the Company s directors. The Bank paid $21,885 during the year ended June 30, 2007 for support services, and an additional $94,056 for computer hardware and software used by the Bank for its computer network. For the year ended June 30, 2006, expenditures were $33,500 for support services and $20,454 for computer hardware and software.

During the current fiscal year the Bank also made a construction loan, in the normal course of lending, to this same affiliated entity for the construction of an office building. At June 30, 2007 $1,489,097 had been disbursed.

NOTE 16: Employee Benefits

Profit Sharing Plan

The Company provides a noncontributory profit sharing plan for eligible employees who have completed one year of service. The amount of the Company s annual contribution, limited to a maximum of 15% of qualified employees salaries, is determined by the Board of Directors. Profit sharing expense was $148,730 and $145,230 for the years ended June 30, 2007 and 2006, respectively.

The Company s profit sharing plan includes a 401(k) feature. At the discretion of the Board of Directors, the Company may match up to 50% of participants contributions up to a maximum of 4% of participants salaries. For the years ended June 30, 2007 and 2006, the Company s match totaled $38,439 and $39,484, respectively.

Deferred Compensation Plans

The Company has entered into deferred compensation contracts with current key employees. The contracts provide fixed benefits payable in equal annual installments upon retirement. The Company purchased life insurance contracts that may be used to fund the payments. The charge to expense is based on the present value computations of anticipated liabilities. For the years ended June 30, 2007 and 2006, the total expense was $93,646 and $92,159, respectively. The Company has recorded a liability for the deferred compensation plan of $858,433 and $813,050 at June 30, 2007 and 2006, respectively, which is included in the balance of accrued expenses and other liabilities.

Employee Stock Ownership Plan

The Company has established an ESOP for eligible employees who meet certain age and service requirements. At inception the ESOP borrowed $368,048 from Eagle Bancorp and used the funds to purchase 46,006 shares of common stock in the offering. The Bank makes periodic contributions to the ESOP sufficient to satisfy the debt service requirements of the loan that has a ten-year term and bears interest at 8%. The ESOP uses these contributions, and any dividends received by the ESOP on unallocated shares, to make principal and interest payments on the loan.

Shares purchased by the ESOP are held in a suspense account by the plan trustee until allocated to participant accounts. Shares released from the suspense account are allocated to participants on the basis of their relative compensation in the year of allocation. Participants become vested in the allocated shares over a period not to exceed seven years. Any forfeited shares are allocated to other participants in the same proportion as contributions.

Total ESOP expenses of $134,713 and $134,832 were recognized in fiscal 2007 and 2006, respectively, for 4,600 shares committed to be released to participants during the years ended June 30, 2007 and 2006 with respect to the plan years ending December 31, 2006 and 2005. The cost of the 11,506 ESOP shares ($92,048 at June 30, 2007) that have not yet been allocated or committed to be released to participants is deducted from stockholders equity. The fair value of these shares was approximately $376,250 at that date.

NOTE 16: Employee Benefits - continued

Stock Incentive Plan

The Company adopted the Stock Incentive Plan (the Plan) on October 19, 2000. The Plan provides for different types of awards including stock options, restricted stock and performance shares. Under the Plan, 23,000 shares of restricted stock were granted to directors and certain officers during fiscal 2001. These shares of restricted stock vest in equal installments over five years beginning one year from the grant date.

During fiscal 2007 and 2006, 0 and 4,600 shares vested, respectively and were removed from treasury stock resulting in compensation expense of $0 and $26,450, respectively.

There were no stock options granted under the Plan as of June 30, 2007.

NOTE 17: Financial Instruments and Off-Balance-Sheet Activities

All financial instruments held or issued by the Company are held or issued for purposes other than trading. In the ordinary course of business, the Company enters into off-balance-sheet financial instruments consisting of commitments to extend credit and forward delivery commitments for the sale of whole loans to the secondary market.

Commitments to extend credit In response to marketplace demands, the Company routinely makes commitments to extend credit for fixed rate and variable rate loans with or without rate lock guarantees. When rate lock guarantees are made to customers, the Company becomes subject to market risk for changes in interest rates that occur between the rate lock date and the date that a firm commitment to purchase the loan is made by a secondary market investor.

Generally, as interest rates increase, the market value of the loan commitment goes down. The opposite effect takes place when interest rates decline.

Commitments to extend credit are agreements to lend to a customer as long as the borrower satisfies the Company s underwriting standards and related provisions of the borrowing agreements. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. The Company uses the same credit policies in making commitments to extend credit as it does for on-balance-sheet instruments. Collateral is required for substantially all loans, and normally consists of real property. The Company s experience has been that substantially all loan commitments are completed or terminated by the borrower within 3 to 12 months.

The notional amount of the Company s commitments to extend credit at fixed and variable interest rates were approximately $5,823,000 and $3,326,000 at June 30, 2007 and 2006, respectively. Fixed rate commitments are extended at rates ranging from 4.75% to 8.25% and 5.00% to 7.90% at June 30, 2007 and 2006, respectively. The Company has lines of credit representing credit risk of approximately $36,092,000 and $29,793,000 at June 30, 2007 and 2006, respectively, of which approximately $18,047,000 and $14,263,000 had been drawn at June 30, 2007 and 2006, respectively. The Company has credit cards issued representing credit risk of approximately $624,000 and $596,000 at June 30, 2007 and 2006, respectively, of which approximately $23,000 and $21,000 had been drawn at June 30, 2007 and 2006, respectively. The Company has letters of credits issued representing credit risk of approximately $1,532,000 and $1,226,000 at June 30, 2007 and 2006, respectively.

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EAGLE BANCORP AND SUBSIDIARY
Notes to Consolidated Financial Statements
June 30, 2007 and 2006

NOTE 17: Financial Instruments and Off-Balance-Sheet Activities- continued

Forward delivery commitments The Company uses mandatory sell forward delivery commitments to sell whole loans. These commitments are also used as a hedge against exposure to interest-rate risks resulting from rate locked loan origination commitments on certain mortgage loans held-for-sale. Gains and losses in the items hedged are deferred and recognized in other comprehensive income until the commitments are completed. At the completion of the commitments the gains and losses are recognized in the Company s income statement

As of June 30, 2007 and 2006, the Company had entered into commitments to deliver approximately $1,201,000 and $918,000 respectively, in loans to various investors, all at fixed interest rates ranging from 2.75% to 6.50% and 5.00% to 6.50%, at June 30, 2007 and 2006, respectively. The Company had approximately $18,000 and $15,000 of gains deferred as a result of the forward delivery commitments entered into as of June 30, 2007 and 2006, respectively. The total amount of the gain is expected to be taken into income within the next twelve months.

The Company did not have any gains or losses reclassified into earnings as a result of the ineffectiveness of its hedging activities. The Company considers its hedging activities to be highly effective.

The Company did not have any gains or losses reclassified into earnings as a result of the discontinuance of cash flow hedges because it was probable that the original forecasted transaction would not occur by the end of the originally specified time frame as of June 30, 2007.

The Company has no other off-balance-sheet arrangements or transactions with unconsolidated, special purpose entities that would expose the Company to liability that is not reflected on the face of the financial statements.

NOTE 18: Fair Value of Financial Instruments

The estimated fair value amounts of financial instruments have been determined by the Company using available market information and appropriate valuation methodologies. However, considerable judgment is necessarily required to interpret data to develop the estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Company could realize in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value

amounts.

EAGLE BANCORP AND SUBSIDIARY
Notes to Consolidated Financial Statements
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NOTE 18: Fair Value of Financial Instruments - continued

	June 30,			
	2007		2006	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
(Dollars in Thousands)				
Financial Assets:				
Cash and cash equivalents	$ 3,069	$ 3,069	$ 2,871	$ 2,871
Securities available-for-sale	64,774	64,774	64,198	64,198
Securities held-to-maturity	921	930	1,018	1,030
FHLB stock	1,315	1,315	1,315	1,315
Mortgage loans held-for-sale	1,175	1,175	918	918
Loans receivable, net	158,140	157,883	140,858	139,720
Mortgage servicing rights	1,628	2,114	1,722	2,043
Cash value of life insurance	5,764	5,764	5,230	5,230
Financial Liabilities:				
Deposits	90,460	90,460	95,713	95,713
Time certificates of deposit	89,187	88,144	78,629	77,125
Advances from the FHLB	30,000	29,717	22,371	22,216
Subordinated debentures	5,155	5,007	5,155	4,451

The following methods and assumptions were used by the Company in estimating the fair value of the following classes of financial instruments.

Cash and interest-bearing accounts The carrying amounts approximate fair value due to the relatively short period of time between the origination of these instruments and their expected realization.

Investment securities and stock in the FHLB The fair value of investment securities is estimated based on bid quotations received from securities dealers. The fair value of stock in the FHLB approximates redemption value.

Loans receivable and mortgage loans held-for-sale Fair values are estimated by stratifying the loan portfolio into groups of loans with similar financial characteristics. Loans are segregated by type such as real estate, commercial, and consumer, with each category further segmented into fixed and adjustable rate interest terms.

For mortgage loans, including loans held-for-sale, the Company uses the secondary market rates in effect for loans that have similar characteristics. The fair value of other fixed rate loans is calculated by discounting scheduled cash flows through the anticipated maturities adjusted for prepayment estimates. Adjustable interest rate loans are assumed to approximate fair value because they generally reprice within the short term.

EAGLE BANCORP AND SUBSIDIARY
Notes to Consolidated Financial Statements
June 30, 2007 and 2006

NOTE 18: Fair Value of Financial Instruments - continued

Fair values are adjusted for credit risk based on assessment of risk identified with specific loans, and risk adjustments on the remaining portfolio based on credit loss experience.

Assumptions regarding credit risk are judgmentally determined using specific borrower information, internal credit quality analysis, and historical information on segmented loan categories for non-specific borrowers.

Mortgage servicing rights Fair values are estimated by stratifying the mortgage servicing portfolio into groups of loans with similar financial characteristics, such as loan type, interest rate, and expected maturity. The Company obtains market survey data estimates and bid quotations from secondary market investors who regularly purchase mortgage servicing rights. Assumptions regarding loan payoffs are determined using historical information on segmented loan categories for nonspecific borrowers.

Cash surrender value of life insurance The carrying amount for cash surrender value of life insurance approximates fair value as policies are recorded at redemption value.

Deposits and time certificates of deposit The fair value of deposits with no stated maturity, such as checking, passbook, and money market, is equal to the amount payable on demand. The fair value of time certificates of deposit is based on the discounted value of contractual cash flows. The discount rate is estimated using the rates currently offered for deposits of similar maturities.

Advances from the FHLB & Subordinated Debentures The fair value of the Company s advances and debentures are estimated using discounted cash flow analysis based on the interest rate that would be effective June 30, 2007, if the borrowings repriced according to their stated terms.

NOTE 19: Condensed Parent Company Financial Statements

Set forth below is the condensed statements of financial condition as of June 30, 2007 and 2006, of Eagle Bancorp together with the related condensed statements of income and cash flows for the years ended June 30, 2007 and 2006.

EAGLE BANCORP AND SUBSIDIARY
Notes to Consolidated Financial Statements
June 30, 2007 and 2006

NOTE 19: Condensed Parent Company Financial Statements - continued

Condensed Statements of Financial Condition
(Dollars in Thousands)

	2007	2006
Assets		
Cash and cash equivalents	$ 90	$ 315
Securities available for sale	4,108	2,778
Investment in Eagle Bancorp Statutory Trust I	155	155
Investment in American Federal Savings Bank	24,596	24,145
Other assets	307	320
Total assets	$29,256	$27,713
Liabilities and stockholders equity		
Accounts payable and accrued expenses	13	13
Long-term subordinated debt	5,155	5,155

	2007	2006
Stockholders Equity	24,088	22,545
Total liabilities and stockholders equity	$29,256	$27,713

Condensed Statements of Income
(Dollars in Thousands)

	2007	2006
Interest income	$ 162	$ 88
Interest expense	(311)	(257)
Noninterest expense	(123)	(114)
Loss before income taxes	(272)	(283)
Income tax benefit	(149)	(135)
Loss before equity in undistributed earnings of American Federal Savings Bank	(123)	(148)
Equity in undistributed earnings of American Federal Savings Bank	1,901	1,933
Net income	$1,778	$1,785

EAGLE BANCORP AND SUBSIDIARY
Notes to Consolidated Financial Statements
June 30, 2007 and 2006

NOTE 19: Condensed Parent Company Financial Statements - continued

Condensed Statements of Cash Flow
(Dollars in Thousands)

	2007	2006
Cash flows from operating activities		
Net income	$ 1,778	$ 1,785
Adjustments to reconcile net income to net cash used in operating activities:		
Equity in undistributed earnings of American Federal Savings Bank	(1,901)	(1,933)
Restricted stock awards		53
Other adjustments, net	10	(158)
Net cash used in operating activities	(113)	(253)
Cash flows from investing activities		
Cash contribution from American Federal Savings Bank	1,717	1,433
Activity in available for sale securities		
Sales		
Maturities, prepayments and calls	30	34
Purchases	(1,382)	(2,795)
Investment in Eagle Bancorp Statutory Trust I		(155)
Net cash provided by (used in) investing activities	365	(1,483)
Cash flows from financing activities		
ESOP payments and dividends	146	152

	2007	2006
Payments to purchase treasury stock	(238)	(554)
Net changes in notes payable advances		(2,500)
Proceeds from subordinated debentures		5,155
Dividends paid	(386)	(359)
Net cash (used in) provided by financing activities	(478)	1,894
Net change in cash and cash equivalents	(226)	158
Cash and cash equivalents at beginning of period	316	157
Cash and cash equivalents at end of period	$ 90	$ 315

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EAGLE BANCORP AND SUBSIDIARY
Notes to Consolidated Financial Statements
June 30, 2007 and 2006

NOTE 20: Quarterly Results of Operations (Unaudited)

The following is a condensed summary of quarterly results of operations for the years ended June 30, 2007 and 2006:

	Year ended June 30, 2007			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
(Dollars in Thousands, except per share data)				
Interest and dividend income	$2,994	$3,102	$3,260	$3,288
Interest expense	1,340	1,472	1,532	1,615
Net interest income	1,654	1,630	1,728	1,673
Non interest income	537	592	544	588
Non interest expense	1,616	1,661	1,660	1,677
Income before income tax expense	575	561	612	584
Income tax expense	153	100	159	142
Net income	$ 422	$ 461	$ 453	$ 442
Comprehensive income (loss)	$ 670	$ 55	$ 156	$ (642)
Basic earnings per common share	$ 0.39	$ 0.43	$ 0.42	$ 0.41
Diluted earnings per common share	$ 0.35	$ 0.38	$ 0.37	$ 0.37

	Year ended June 30, 2006			
Interest and dividend income	$2,438	$2,586	$2,661	$2,814
Interest expense	768	896	981	1,140
Net interest income	1,670	1,690	1,680	1,674
Non interest income	643	517	474	531
Non interest expense	1,592	1,637	1,634	1,602
Income before income tax expense	721	570	520	603
Income tax expense	222	125	117	165
Net income	$ 499	$ 445	$ 403	$ 438

	Year ended June 30, 2007			
Comprehensive loss	$ (183)	$ (226)	$ (33)	$ (353)
Basic earnings per common share	$ 0.46	$ 0.41	$ 0.37	$ 0.41
Diluted earnings per common share	$ 0.41	$ 0.37	$ 0.33	$ 0.36

NOTE 21: Subsequent Events

The Board announced on July 19, 2007 the declaration of a cash dividend of $0.24 per share for the fourth quarter. It is payable August 24, 2007 to shareholders of record at the close of business August 3, 2007. Eagle Financial MHC, Eagle Bancorp s mutual holding company, has waived its right to receive dividends on the 648,493 shares of Eagle Bancorp that Eagle Financial MHC holds.

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SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the registrant causes this report to be signed on its behalf by the undersigned, thereunto duly authorized.

EAGLE BANCORP
/s/ Larry A. Dreyer
Larry A. Dreyer
Chief Executive Officer

In accordance with the Exchange Act, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signatures	Title	Date
/s/ Larry A. Dreyer Larry A. Dreyer	Chief Executive Officer Director (Principal Executive Officer)	9/14/07
/s/ Peter J. Johnson Peter J. Johnson	President	9/14/07
/s/ Clinton J. Morrison Clinton J. Morrison	Senior Vice President and Chief Financial Officer	9/14/07
/s/ Robert L. Pennington Robert L. Pennington	Chairman	9/14/07
/s/ Charles G. Jacoby Charles G. Jacoby	Vice Chairman	9/14/07
/s/ Don O. Campbell Don O. Campbell	Director	9/14/07

Signatures	Title	Date
/s/ Lynn E. Dickey Lynn E. Dickey	Director	9/14/07
/s/ James A. Maierle James A. Maierle	Director	9/14/07
/s/ Thomas J. McCarvel Thomas J. McCarvel	Director	9/14/07

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