WAKE FOREST BANCSHARES INC
Form 10QSB
May 12, 2008

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FORM 10-QSB

þ **QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended March 31, 2008

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from __________ to __________

Commission file number 000-25999

Wake Forest Bancshares, Inc.

(Exact name of small business issuer as specified in its charter)

United States of America	56-2131079
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

302 South Brooks Street
Wake Forest, North Carolina 27587
(Address of principal executive offices)
(919)-556-5146
(Issuer s telephone number)
N/A
(Former name, former address and former fiscal year, if changed since last report)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No o

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

State the number of shares outstanding of each of the issuer s classes of common equity, as of the latest practicable date: As of May 1, 2008 there were issued and outstanding 1,158,628 shares of the Issuer s common stock, $.01 par value

Transitional Small Business Disclosure Format: Yes o No þ

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Item 1. Financial Statements

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WAKE FOREST BANCSHARES, INC.
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
March 31, 2008 and September 30, 2007

	March 31, 2008 (Unaudited)	September 30, 2007 *
ASSETS		
Cash and short-term cash investments	$ 22,170,900	$ 25,828,500
Investment securities:		
Available for sale, at estimated market value	1,763,200	1,999,900
FHLB stock	195,200	191,400
Loans receivable, net of loan loss allowances of $1,234,750 at March 31, 2008 and $1,187,550 at September 30, 2007	80,602,650	76,172,100
Accrued interest receivable	238,900	265,350
Foreclosed assets, net	1,470,250	1,003,800
Property and equipment, net	369,100	357,350
Bank owned life insurance	1,163,500	1,141,350
Deferred income taxes, net	505,150	390,650
Prepaid expenses and other assets	146,050	47,300
Total Assets	$ 108,624,900	$ 107,397,700
LIABILITIES AND STOCKHOLDERS EQUITY		
Deposits	$ 86,695,750	$ 85,659,150
Accrued interest on deposits	53,600	64,750
Accrued expenses and other liabilities	855,800	924,950
Dividends payable	104,700	99,750
Redeemable common stock held by the ESOP net of unearned ESOP shares	429,350	465,550
Total Liabilities	88,139,200	87,214,150
Stockholders equity:		
Preferred stock, authorized 1,000,000 shares, none issued		
Common stock, par value $ .01, authorized 5,000,000 shares, issued 1,253,948 shares at March 31, 2008 and September 30, 2007	12,550	12,550
Additional paid-in capital	5,779,500	5,779,500
Accumulated other comprehensive income	158,200	305,000
Retained earnings, substantially restricted	16,030,700	15,555,950
Less: Common stock in treasury, at cost, 95,320 shares at March 31, 2008 and 93,955 shares at September 30, 2007	(1,495,250)	(1,469,450)
Total stockholders equity	20,485,700	20,183,550
Total liabilities and stockholders equity	$ 108,624,900	$ 107,397,700

See Notes to Consolidated Financial Statements.

* Derived from Audited Consolidated Financial Statements.

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WAKE FOREST BANCSHARES, INC.
CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)
Three Months Ended March 31, 2008 and 2007

	2008	2007
Interest and dividend income:		
Loans	$ 1,378,550	$ 1,586,500
Investment securities	24,850	6,950
Short-term cash investments	237,200	334,050
Total interest income	1,640,600	1,927,500
Interest expense:		
Interest on deposits	872,900	907,750
Total interest expense	872,900	907,750
Net interest income before provision for loan losses	767,700	1,019,750
Provision for loan losses	(30,000)	(37,500)
Net interest income after provision for loan losses	737,700	982,250
Noninterest income:		
Service charges and fees	19,200	14,500
Secondary market fee income		6,150
Other	11,600	10,450
	30,800	31,100
Noninterest expense:		
Compensation and benefits	189,800	217,750
Occupancy	14,800	11,050
Federal insurance and operating assessments	12,300	11,950
Data processing	29,000	31,800
REO provisions and expense	3,750	10,150
Other operating expense	79,350	100,550
	329,000	383,250
Income before income taxes	439,500	630,100
Income taxes	156,850	218,550
Net income	$ 282,650	$ 411,550

Basic earnings per common share	$	0.24	$	0.35
Diluted earnings per common share	$	0.24	$	0.35
Dividends per common share	$	0.20	$	0.19

See Notes to Consolidated Financial Statements.

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WAKE FOREST BANCSHARES, INC.
CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)
Six Months Ended March 31, 2008 and 2007

	2008	2007
Interest and dividend income:		
Loans	$ 2,907,700	$ 3,216,450
Investment securities	49,100	13,950
Short-term cash investments	534,500	668,500
Total interest income	3,491,300	3,898,900
Interest expense:		
Interest on deposits	1,823,000	1,801,800
Total interest expense	1,823,000	1,801,800
Net interest income before provision for loan losses	1,668,300	2,097,100
Provision for loan losses	(70,000)	(92,500)
Net interest income after provision for loan losses	1,598,300	2,004,600
Noninterest income:		
Service charges and fees	36,450	30,750
Secondary market fee income		6,150
Other	23,000	21,350
	59,450	58,250
Noninterest expense:		
Compensation and benefits	379,500	425,050
Occupancy	26,400	24,800
Federal insurance and operating assessments	24,400	23,400
Data processing	56,100	57,900
REO provisions and expense	8,550	40,200
Other operating expense	154,750	191,700
	649,700	763,050
Income before income taxes	1,008,050	1,299,800
Income taxes	359,750	456,700
Net income	$ 648,300	$ 843,100
Basic earnings per common share	$ 0.56	$ 0.73

Diluted earnings per common share	$	0.56	$	0.73
Dividends per common share	$	0.40	$	0.38

See Notes to Consolidated Financial Statements.

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WAKE FOREST BANCSHARES, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)
Three and Six Months Ended March 31, 2008 and 2007

	2008	2007
For the Three Months Ended March 31:		
Net income	$ 282,650	$ 411,550
Other comprehensive (loss), net of tax:		
Unrealized (losses) on securities:		
Unrealized holding (losses) arising during period	(30,850)	(42,500)
Less: reclassification adjustments for (losses) included in net income		
Other comprehensive (loss)	(30,850)	(42,500)
Comprehensive income	$ 251,800	$ 369,050

	2008	2007
For the Six Months Ended March 31:		
Net income	$ 648,300	$ 843,100
Other comprehensive income (loss), net of tax:		
Unrealized gains (losses) on securities:		
Unrealized holding gains (losses) arising during period	(146,800)	(34,600)
Less: reclassification adjustments for gains (losses) included in net income		
Other comprehensive income (loss)	(146,800)	(34,600)
Comprehensive income	$ 501,500	$ 808,500

See Notes to Consolidated Financial Statements.

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WAKE FOREST BANCSHARES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
Six Months Ended March 31, 2008 and 2007

	2008	2007
Net income	$ 648,300	843,100
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	23,400	27,500
Provision for loan losses	70,000	92,500
Deferred income taxes	(24,650)	(50,400)
Increase in cash surrender value of life insurance	(22,150)	(20,150)
Loss on sale of foreclosed assets	400	
Changes in assets and liabilities:		
Prepaid expenses and other assets	(98,750)	(42,750)
Accrued interest receivable	26,450	13,250
Accrued interest on deposits	(11,150)	(19,650)
Accrued expenses and other liabilities	(69,150)	73,200
Net cash provided by operating activities	542,700	916,600
Cash Flows From Investing Activities:		
Net increase in loans receivable	(5,063,550)	(1,162,950)
Redemption of FHLB stock		6,200
Purchase of FHLB stock	(3,800)	
Capital additions to foreclosed assets	(13,400)	
Proceeds from sale of foreclosed assets	109,550	
Purchase of property and equipment	(35,150)	
Net cash used in investing activities	(5,006,350)	(1,156,750)
Cash Flows From Financing Activities:		
Net increase in deposits	1,036,600	2,878,900
Proceeds from exercise of stock options		86,900
Additions to paid in capital from tax effect from exercise of of stock options		27,000
Repurchase of common stock for the Treasury	(25,800)	(54,200)
Dividends paid	(204,750)	(188,100)
Net cash provided by financing activities	806,050	2,750,500
Net increase (decrease) in cash and cash equivalents	(3,657,600)	2,510,350
Cash and cash equivalents:		
Beginning	25,828,500	23,818,900
Ending	$ 22,170,900	$ 26,329,250
Supplemental Disclosure of Cash Flow Information:		
Cash payments of interest	$ 1,834,150	$ 1,821,450

Cash payment of income taxes	$ 454,000	$ 510,000
Supplemental Disclosure of Noncash transactions:		
Decrease in ESOP put option credited to retained earnings	$ 36,200	$ 33,900
Transfer of loans to foreclosed assets	$ 563,000	$ 75,100
Decrease in unrealized gain on investment securities, net of tax	$ (146,800)	$ (34,600)

See Notes to Consolidated Financial Statements.

Wake Forest Bancshares, Inc.
Notes to Consolidated Financial Statements

Note 1. Nature of Business

Wake Forest Bancshares, Inc. (the Company) is located in Wake Forest, North Carolina and is the parent stock holding company of Wake Forest Federal Savings and Loan Association (the Association or Wake Forest Federal), its only subsidiary. The Company conducts no business other than holding all of the stock in the Association, investing dividends received from the Association, repurchasing its common stock from time to time, and distributing dividends on its common stock to its shareholders. The Association s principal activities consist of obtaining deposits and providing mortgage credit to customers in its primary market area, the counties of Wake and Franklin, North Carolina. The Company s and the Association s primary regulator is the Office of Thrift Supervision (OTS) and its deposits are insured by the Federal Deposit Insurance Corporation (FDIC).

Note 2. Organizational Structure

The Company is majority owned by the Wake Forest Bancorp, M.H.C., (the MHC) a mutual holding company. Members of the MHC consist of depositors and certain borrowers of the Association, who have the sole authority to elect the board of directors of the MHC for as long as it remains in mutual form. Initially, the MHC s principal assets consisted of 635,000 shares of the Association s common stock (now converted to the Company s common stock) and $100,000 in cash received from the Association as initial capital. Prior to 2003 (see Note 4), the MHC received its proportional share of dividends declared and paid by the Association (now the Company), and such funds are invested in deposits with the Association. The MHC, which by law must own in excess of 50% of the stock of the Company, currently has an ownership interest of 54.8% of the Company. The mutual holding company is registered as a savings and loan holding company and is subject to regulation, examination, and supervision by the OTS.

The Company was formed on May 7, 1999 solely for the purpose of becoming a savings and loan holding company and had no prior operating history. The formation of the Company had no impact on the operations of the Association or the MHC. The Association continues to operate at the same location and is subject to all the rights, obligations and liabilities of the Association which existed immediately prior to the formation of the Company. The Board of Directors of the Association capitalized the Company with $100,000. Future capitalization of the Company will depend upon dividends declared by the Association based on future earnings, or the raising of additional capital by the Company through a future issuance of securities, debt or by other means. The Board of Directors of the Company has no present plans or intentions with respect to any future issuance of securities or debt at this time.

Note 3. Basis of Presentation

The accompanying unaudited consolidated financial statements (except for the consolidated statement of financial condition at September 30, 2007, which is derived from audited consolidated financial statements) have been prepared in accordance with generally accepted accounting principles for interim financial information and Regulation S-B. Accordingly, they do not include all of the information required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (none of which were other than normal recurring accruals) necessary for a fair presentation of the financial position and results of operations for the periods presented have been included. The results of operations for the three and six month periods ended March 31, 2008 are not necessarily indicative of the results of operations that may be expected for the Company s fiscal year ending September 30, 2008. The accounting policies followed are as set forth in Note 1 of the Notes to Consolidated Financial Statements in the Company s September 30, 2007 Annual Report to Stockholders.

Note 4. Dividends Declared

On March 17, 2008, the Board of Directors of the Company declared a cash dividend of $0.20 a share for stockholders of record as of March 31, 2008 and payable on April 10, 2008. The dividends declared were accrued and reported as dividends payable in the March 31, 2008 Consolidated Statement of Financial Condition. Wake Forest Bancorp, Inc., the mutual holding company, waived the receipt of the dividend declared by the Company this quarter.

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Wake Forest Bancshares, Inc.
Notes to Consolidated Financial Statements

Note 5. Earnings Per Share

Basic earnings per share amounts are based on the weighted average shares of common stock outstanding. Diluted earnings per share assumes the conversion, exercise or issuance of all potential common stock instruments such as options, warrants and convertible securities, unless the effect is to reduce a loss or increase earnings per share. This presentation has been adopted for all periods presented. There were no adjustments required to net income for any period in the computation of diluted earnings per share. The reconciliation of weighted average shares outstanding for the computation of basic and diluted earnings per share for the three and six month periods ended March 31, 2008 and 2007 is presented below.

For the Three Months Ended March 31:	2008	2007
Weighted average shares outstanding for Basic EPS	1,159,379	1,161,906
Plus incremental shares from assumed issuances of shares pursuant to stock option and stock award plans		1,368
Weighted average shares outstanding for diluted EPS	1,159,379	1,163,274

For the Six Months Ended March 31:	2008	2007
Weighted average shares outstanding for Basic EPS	1,159,685	1,159,703
Plus incremental shares from assumed issuances of shares pursuant to stock option and stock award plans		1,776
Weighted average shares outstanding for diluted EPS	1,159,685	1,161,479

Note 6. New Accounting Standard

In July 2006, the FASB issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN No. 48). FIN No. 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with SFAS No. 109, *Accounting for Income Taxes*. FIN No. 48 prescribes a recognition threshold and measurement approach for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN No. 48 also provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition issues.

FIN No. 48 establishes a two-step process for evaluation of tax positions. The first step is recognition, under which the enterprise determines whether it is more likely than not that a tax position will be sustained upon examination, including resolution of any related appeals or litigation processes, based on the technical merits of the position. The enterprise is required to presume the position will be examined by the appropriate taxing authority that has full knowledge of all relevant information. The second step is measurement, under which a tax position that meets the more-likely-than-not recognition threshold is measured to determine the amount of benefit to recognize in the financial statements. The tax position is measured at the largest amount of benefit that is greater than 50% likely of being realized upon ultimate settlement. The cumulative effect of adopting FIN No. 48 is required to be reported as an adjustment to the opening balance of retained earnings (or other appropriate components of equity) for that fiscal year. FIN No. 48 is effective for the Company s current fiscal year and its adoption had no impact on Company s consolidated financial statements.

Note 7. Future Reporting Requirements

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 157, *Fair Value Measurements*, which enhances existing guidance for measuring assets and liabilities using fair value. SFAS No. 157 provides a single definition of fair value, together with a framework for measuring it, and requires additional disclosures about the use of fair value to measure assets and liabilities. SFAS

No. 157 emphasizes that fair value is a market-based measurement and establishes a fair value hierarchy with the highest priority being quoted market prices in active markets. While SFAS No. 157 does not add any new fair value measurements, it may change certain current practices. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and for interim periods within those fiscal years. The Company does not expect the adoption of SFAS No. 157 will have a material impact on its consolidated financial statements.

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Notes to Consolidated Financial Statements

Note 7. Future Reporting Requirements (Continued)

In February 2007, the FASB issued SFAS No. 159 *The Fair Value Option for Financial Assets and Financial Liabilities*. SFAS No. 159 provides an option to measure eligible financial instruments at fair value at specified election dates. Unrealized gains and losses on specific financial assets and liabilities that are designated to be carried at fair value will be recognized in earnings thereafter. The fair value option may be applied instrument by instrument, is irrevocable and may only be applied to entire instruments, not to portions of instruments. The provisions of SFAS No. 159 are effective for fiscal years beginning after November 15, 2007. The Company does not currently plan to adopt SFAS No. 159.

The Emerging Issues Task Force (EITF) reached a consensus at its September 2006 meeting regarding EITF 06-4, *Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements*. EITF 06-4 requires the recognition of a liability and related compensation costs for endorsement split-dollar life insurance policies that provide a benefit to an employee that extends to postretirement periods. The Company has policies that fall within the scope of EITF 06-4. EITF 06-4 is effective for fiscal years beginning after December 15, 2007 and can be applied by either a change in accounting principle through a cumulative-effect adjustment to retained earnings as of the beginning of the year of adoption or a change in accounting principle through a retrospective application to all prior periods. The Company is currently evaluating the impact of EITF 06-4 on its consolidated financial statements.

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Wake Forest Bancshares, Inc.
Management s Discussion and Analysis of Financial Condition
and Results of Operations

Forward Looking Statements

Information set forth below contains various forward-looking statements within the meaning of Section 27A of the Securities and Exchange Act of 1933 and Section 21E of the Securities Exchange Act of 1934, which statements represent the Company s judgment concerning the future and are subject to risks and uncertainties that could cause the Company s actual operating results to differ materially. Such forward-looking statements can be identified by the use of forward-looking terminology, such as may , will , expect , anticipate , estimate , believe , or continue , or thereof or other variations thereof or comparable terminology. The Company cautions that such forward-looking statements are further qualified by important factors that could cause the Company s actual operating results to differ materially from those in the forward-looking statements, as well as the factors set forth in the Company s periodic reports and other filings with the SEC.

Comparison of Financial Condition at September 30, 2007 and March 31, 2008

Total assets increased by $1.2 million to $108.6 million at March 31, 2008 from $107.4 million at September 30, 2007. The increase in total assets during the six month period ended March 31, 2008 was funded primarily from an increase in deposits of approximately $1.0 million and cash generated from internal operating activities during the same period. Due to adequate levels of current liquidity, deposits were priced to meet competition and retain certain accounts but not to aggressively attract additional funds. The Company attempts to maintain a certain level of liquidity to fund loan growth and to provide a cushion for its construction loan commitments. During the current quarter, cash and short term cash investments decreased by approximately $3.7 million.

Net loans receivable increased by $4.4 million to $80.6 million at March 31, 2008 from $76.2 million at September 30, 2007. The increase during the current six month period occurred primarily because of a $1.5 million increase in the Company s construction loan portfolio, which typically expands during early spring and throughout the summer months, and a $3.0 million increase in the Company s commercial real estate portfolio. The increase in the Company s commercial real estate portfolio occurred because of two large loan originations that closed during March 2008 and which were secured by a couple of industrial warehouses located in the area. The residential market in the Company s primary lending area remains sluggish when compared to the same periods a year earlier and both re-sales and newly constructed homes remain on the market for longer periods of time. New home starts are considerably less during the current six month period when compared to the same time period a year ago. The Company s local real estate market experienced significant growth over the last five years, primarily due to an influx of newcomers from outside the area. Although the Company s markets have not experienced a drop in home prices like many areas of the country, local real estate markets are impacted by newcomers unable to purchase homes here until they are able to sell residences elsewhere.

In addition, questions about the strength of the economy combined with tighter credit standards associated with the sub-prime fall-out have slowed the residential real estate markets significantly both locally and nationwide. Population growth and employment expansion across a wide spectrum of the local economic base combined with moderate interest rate levels will ultimately determine whether loan demand can be revived. Assuming local economic conditions improve, management believes that the long-term fundamentals of its lending markets provide potential for future loan growth. However, there can be no assurances that such loan demand can or will materialize in the near future.

Investment securities decreased by $232,900 to $1,958,400 at March 31, 2008 from $2,191,300 at September 30, 2007. The decrease is attributable to a $274,700 unrealized loss in the Company s investment in FHLMC stock offset by $38,000 increase in unrealized appreciation in the Company s bond portfolio during the past six months and a required $3,800 purchase of FHLB stock during the same period. The Company has held its FHLMC investment for many years and considers it to be a long term investment. The Company has very little cost basis in the stock and retains an approximately $198,000 unrealized gain in the stock at March 31, 2008. The FHLMC stock has recently declined due to the issues surrounding sub-prime lending and the market for mortgage-backed securities. The Company also has an investment of $1.5 million in FHLB bonds.

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Wake Forest Bancshares, Inc.
Management s Discussion and Analysis of Financial Condition
and Results of Operations

Comparison of Financial Condition at September 30, 2007 and March 31, 2008 (Continued)

The Company generally maintains higher levels of short term liquidity in order to minimize interest rate risk, to fund construction loan commitments, and due to the relatively minor differential in current investment rates available on extended maturities. As a result, the Company has not been actively involved in the buying and selling securities but has been purchasing FDIC insured bank certificates of deposit generally with maturities up to one year to protect against downward interest rate risk. The Company s portfolio of bank certificates of deposit amounted to $13.3 million at March 31, 2008. These bank certificates of deposit investments are typically acquired at interest rates of 1.00% to 1.50% higher than most debt securities currently available for terms much longer than a year.

The Company had no borrowings outstanding during the period because its current level of liquidity was sufficient to fund lending and other cash commitments. The Company has recorded a liability of $429,350 at March 31, 2008 for the ESOP put option which represents the potential liability owed to participants based on the current market value of the Company s stock if all participants were to request the balance of their account from the Company in cash instead of stock.

The Company has an ongoing stock repurchase program authorizing management to repurchase shares of its outstanding common stock. The repurchases are made through registered broker-dealers from shareholders in open market purchases at the discretion of management. The Company intends to hold the shares repurchased as treasury shares, and may utilize such shares to fund stock benefit plans or for any other general corporate purposes permitted by applicable law. At March 31, 2008 the Company had repurchased 95,320 shares of its common stock. The program continues until completed or terminated by the Board of Directors.

Retained earnings increased by $474,750 to $16.0 million at March 31, 2008 from $15.5 million at September 30, 2007. The increase is primarily attributable to the Company s earnings of $648,300 during the six month period ended March 31, 2008, reduced by $209,700 in dividends declared during the period and a $36,150 recovery of prior charges to retained earnings to reflect the change in the fair value of the ESOP shares subject to the put option. At March 31, 2008 the Company s capital amounted to $20.5 million, which as a percentage of total assets was 18.86%. The Company and the Association are both required to meet certain capital requirements as established by the OTS. At March 31, 2008, all capital requirements were met.

Asset Quality

The Company s level of non-performing loans, consisting of loans past due 90 days or more, amounted to $868,600 or 1.06% as a percentage of loans outstanding at March 31, 2008. At March 31, 2007, the Company had $637,850 in loans past due 90 days or more. Non-performing loans amounted to $595,650 or 0.77% as a percentage of loans outstanding at September 30, 2007. At March 31, 2008, non-performing loans consisted of three residential construction loans amounting to $613,950 and one land loan totaling $254,650. All three of the construction loans are with one builder and foreclosure proceedings have commenced on all three loans. Specific loss allowances amounting to $75,000 have been established at March 31, 2008 for these non-performing loans. All of the loans have been placed on non-accrual status.

Non-performing assets also includes real estate acquired through foreclosure. At March 31, 2008, foreclosed assets included three partially completed single family homes ($439,950) and one residential lot loan ($26,500). Two of the partially completed single family homes were transferred to foreclosed assets after having incurred $18,500 in loan charge-offs but are under contract and will be sold at very little additional gain or loss. At March 31, 2008 the Company believes that the remaining single family property and the residential lot have a fair value in excess of their recorded cost.

In addition, real estate acquired through foreclosure includes a commercial property ($1,003,800) which consisted of a convenience store and an adjacent tract of land, in total 3.81 acres located on a major highway outside of Wake Forest, North Carolina. While the commercial property s location is considered highly desirable, the Company decided that an environmental assessment was necessary to properly market the tract due to the historical uses of the property.

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Management s Discussion and Analysis of Financial Condition
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Comparison of Financial Condition at September 30, 2007 and March 31, 2008 (Continued)

Asset Quality (Continued)

Site assessment reports on the tract were filed with various state environmental agencies. Petroleum contamination and other trace elements consistent with operating a gas station and a truck maintenance facility over an extended period of time were found on parts of the property. The Company has obtained brownfields status for the site which should make the tract more attractive to prospective developers of the property. In addition, the Company obtained Trust Fund status for the site which will allow certain environmental cost to be reimbursed. Although the Company does not currently believe the contamination will have a significant detrimental effect on the potential development of the property, the agencies are assisting the Company in determining the extent of any required clean-up and ongoing monitoring steps that will be required. The Company has set aside $143,000 at March 31, 2008 for such testing and clean-up activities. At this time, the Company does not believe that the ongoing environmental costs will materially impact the value of the property. At March 31, 2008, the Company had entered into a contract to sell the commercial property which would result in very little gain or loss on its disposition.

The Company had $22,800 in loan charge-offs during the current quarter and six months ended March 31, 2008. The Company s loan loss allowance amounted to $1,234,750 at March 31, 2008 and management believes that it has sufficient allowances established to cover losses associated with its loan portfolio. The allowance for loan losses is established based upon probable losses that are estimated to have occurred through a provision for loan losses charged to earnings. During the past five years, the Association s loan portfolio has gradually trended towards a greater concentration of residential construction and land loans, which generally involve a greater degree of credit risk and collection issues. As a result, the Company has provided relatively higher levels of loan loss provisions and resulting allowances during this period than what has historically been considered necessary. The allowance for loan losses is evaluated on a regular basis by management.

The Company records provisions for loan losses based upon known problem loans and estimated deficiencies in the existing loan portfolio. The Company s methodology for assessing the appropriateness of the allowance for loan losses consists of two key components which are a specific allowance for identified problem or impaired loans under the provisions of Statement of Financial Accounting Standards (SFAS) No. 114, *Accounting by Creditors for Impairment of a Loan* , and a formula allowance for the remainder of the portfolio under the provisions of SFAS No. 5, *Accounting for Contingencies.* Because the Company only originates loans secured by real estate, specific problem loans are graded using the standard regulatory classifications and are evaluated for impairment under SFAS No. 114 based upon the collateral s fair value less estimated cost of disposal.

All other loans with unidentified impairment issues are pooled and segmented by major loan types (single-family residential properties, construction loans, commercial real estate, land, etc.). Loan loss rates for these categories are then generated by capturing historical loan losses net of recoveries over a five and ten year period, with added weight given to the more recent five year period. Qualitative factors that may affect loan collectibility such as geographical and lending concentrations, local economic conditions, and delinquency trends are also considered in determining the Company s best estimate of the range of credit losses. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

Although management believes it has established and maintained the allowance for loan losses at appropriate levels, future adjustments may be necessary if economic, real estate values and other conditions differ substantially from the current operating environment. In addition, regulatory examiners may require the Association to recognize adjustments to the allowance for loan losses based on their judgments about information available to them at the time of their examination.

Wake Forest Bancshares, Inc.
Management s Discussion and Analysis of Financial Condition
and Results of Operations

Comparison of Operating Results for the Three and Six Months Ended March 31, 2008 and 2007

General. Net income for the three month period ended March 31, 2008 was $282,650, or $128,900 less than the $411,550 earned during the same quarter in 2007. Net income for the six month period ended March 31, 2008 was $648,300, or $194,800 less than the $843,100 earned during the same period in 2007. As discussed below, changes in net interest income between the comparable periods were primarily responsible for the change in net income during the current quarter and six month period end March 31, 2008 when compared to the same periods a year earlier.

Interest income. Interest income decreased by $286,900 from $1,927,500 for the three months ended March 31, 2007 to $1,640,600 for the three months ended March 31, 2008. The decrease in interest income resulted from a 104 basis point decrease in the average yield on interest earning assets between the quarters. Interest income decreased by $407,600 from $3,898,900 for the six months ended March 31, 2007 to $3,491,300 for the six months ended March 31, 2008. The decrease in interest income resulted from a 72 basis point decrease in the average yield on interest earning assets between the six month periods. The Company s yield on interest earning assets was 6.26% and 6.56% for the quarter and six month period ended March 31, 2008; respectively, and 7.30% and 7.28% for the quarter and six month period ended March 31, 2007; respectively. The changes in yield occurred primarily due to fluctuations in market rates outstanding during the periods. A significant portion of the Company s assets have rates that are tied to prime or generally move in tandem with changes to prime, which in turn is directly influenced by Federal Reserve monetary policies and its interest rate movements. The Federal Reserve has lowered rates by 3.00% since September 2007 which has had a material impact on the Company s revenue stream.

Interest Expense. Interest expense decreased by $34,850 from $907,750 for the three months ended March 31, 2007 to $872,900 for the three months ended March 31, 2008. Interest expense increased by $21,200 from $1,801,800 for the six months ended March 31, 2007 to $1,823,000 for the six months ended March 31, 2008. The decrease in interest expense during the current quarter as compared to the same period a year earlier resulted primarily from a 33 basis point decrease in the Company s cost of funds. The increase in interest expense for the six month period ended March 31, 2008 as compared to the same period one year earlier was primarily due to a $620,000 increase in the average outstanding balance of deposits between the periods. The Company s cost of funds was 3.99% and 4.17% for the three and six month periods ended March 31, 2008; respectively, as compared to 4.32% and 4.28%, respectively, for the same periods a year earlier.

Net interest income. Net interest income decreased by $252,050 from $1,019,750 for the three months ended March 31, 2007 to $767,700 for the three months ended March 31, 2008. Net interest income decreased by $428,800 from $2,097,100 for the six months ended March 31, 2007 to $1,668,300 for the six months ended March 31, 2008. As explained above, the decrease in net interest income resulted primarily from declines in the Company s yields on its interest-earning assets during the three and six months ended March 31, 2008 as compared with the same periods one year earlier. The Company s net interest margin was 2.93% and 3.18% for the current quarter and six months ended March 31, 2008 versus 3.92% and 4.07% for the same quarter and six month period a year earlier.

Provision for loan losses. The Company provided $30,000 and $70,000 in loan loss provisions during the current quarter and six month period ended March 31, 2008; respectively, as compared to $37,500 and $92,500 during the three and six month periods; respectively, a year earlier. Provisions, which are charged to operations, and the resulting loan loss allowances are amounts the Company s management believes will be adequate to absorb losses that are estimated to have occurred in the portfolio. Loans are charged off against the allowance when management believes that uncollectibility is confirmed. Subsequent recoveries, if any, are credited to the allowance. The Association s loan portfolio has gradually trended towards a greater concentration of builder construction loans, land and land development loans, and commercial real estate loans which generally involve a greater degree of credit risk and collection issues. Also, many of these types of loans involve lending relationships which are larger than what the Company has traditionally maintained. As a result, the Company has provided relatively higher levels of loan loss provisions and resulting allowances during the last five years than what has historically been considered necessary.

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Non-interest income. The Company s non-interest income is primarily comprised on various fees and service charges on customer accounts, income from bank owned life insurance products, as well as security gains and fees earned from secondary market originations. The Company did not have any investment sales during any of the periods being reported upon. In addition, the Company has been originating residential mortgage loans for its own portfolio over the periods being reported upon and therefore very little secondary marketing income has been generated over those same periods.

Non-interest expense. Non-interest expense decreased by $54,250 to $329,000 for the three month period ended March 31, 2008 from $383,250 for the comparable quarter in 2007. Non-interest expense decreased by $113,350 to $649,700 for the six month period ended March 31, 2008 from $763,050 for the same period a year earlier.

Compensation and benefits decreased by $27,950 and $45,550 during the quarter and six months ended March 31, 2008 as compared to the same periods a year earlier due to the accrual of a lesser amount of employee bonuses for the current year. REO provisions and expense are primarily associated with environmental assessment activities for the Company s foreclosed tract on highway 98 outside of Wake Forest, North Carolina and were approximately $6,400 and $31,650 lower during the current quarter and six months ended March 31, 2008 versus the same periods a year earlier. The lower REO expense was primarily due to a lesser amount of assessment activities to the tract during the current year as compared to the same periods in 2007.

Other operating expense decreased by $21,200 and $36,950, respectively, during the three and six months ended March 31, 2008 as compared to the same periods a year ago primarily because the Company has been diligent in trimming various operating expenses when feasible, including reductions in certain data processing expense, employee and director expense, equipment expense, supplies expense, shareholder expense, and contribution expense. No other category of non-interest expense changed significantly between the periods.

Capital Resources and Liquidity

The term liquidity generally refers to an organization s ability to generate adequate amounts of funds to meet its needs for cash. More specifically for financial institutions, liquidity ensures that adequate funds are available to meet deposit withdrawals, fund loan and capital expenditure commitments, maintain reserve requirements, pay operating expenses, and provide funds for debt service, dividends to stockholders, and other institutional commitments. Funds are primarily provided through financial resources from operating activities, expansion of the deposit base, borrowings, through the sale or maturity of investments, the ability to raise equity capital, or maintenance of shorter term interest-earning deposits.

During the six month period ended March 31, 2008, cash and cash equivalents, a significant source of liquidity, decreased by approximately $3.7 million. The most significant use of cash during the six month period ended March 31, 2008 was a $5.1 million net increase in loans receivable. A net increase in customer deposits of $1.0 million and net cash provided by operating activities of $542,750 were the primary sources of cash during the current six month period. Given its excess liquidity and its ability to borrow from the Federal Home Loan Bank of Atlanta, the Company believes that it will have sufficient funds available to meet anticipated future loan commitments, unexpected deposit withdrawals, and other cash requirements.

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Off-Balance Sheet Transactions

In the normal course of business, the Association engages in a variety of financial transactions that, under generally accepted accounting principles, either are not recorded on the balance sheet or are recorded on the balance sheet in amounts that differ from the full contract or notional amounts. Primarily the Association is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, revolving lines of credit, and the undisbursed portion of construction loans. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amounts recognized in the statement of financial condition. The contract or notional amounts of those instruments reflect the extent of involvement the Association has in particular classes of financial instruments. The Association s exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit is represented by the contractual notional amount of those instruments. The Association uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments. At March 31, 2008, the Association had outstanding loan commitments amounting to approximately $902,600. The undisbursed portion of construction loans amounted to $9.4 million and unused lines of credit amounted to $3.7 million at March 31, 2008.

Critical Accounting Policies and Estimates

The accounting policies followed are as set forth in Note 1 of the Notes to Financial Statements in the Company s 2007 Annual Report on Form 10-KSB. The Company has not experienced any material change in its critical accounting policies since September 30, 2007. The Company s discussion and analysis of its financial condition and results of operations are based upon its consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires the Company to make estimates and judgments regarding uncertainties that affect the reported amounts of assets, liabilities, revenues and expenses. On an ongoing basis, the Company evaluates its estimates which are based upon historical experience and on other assumptions that are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. The Company considers the following accounting policies to be most critical in their potential effect on its financial position or results of operations:

Allowance for Loan Losses

The most critical estimate concerns the Company s allowance for loan losses. The Company records provisions for loan losses based upon known problem loans and estimated deficiencies in the existing loan portfolio. The Company s methodology for assessing the appropriations of the allowance for loan losses consists of two key components, which are a specific allowance for identified problem or impaired loans and a formula allowance for the remainder of the portfolio.

A loan is considered impaired when, based on current information and events, it is probable that the Association 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 of the circumstances surrounding the loan and the borrower, including the length of the 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. This evaluation is inherently subjective as it requires material estimates that may be susceptible to significant change.

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Critical Accounting Policies and Estimates (Continued)

The adequacy of the allowance is also reviewed by management based upon its evaluation of then-existing economic and business conditions affecting the key lending areas of the Company and other conditions, such as new loan products, collateral values, loan concentrations, changes in the mix and volume of the loan portfolio; trends in portfolio credit quality, including delinquency and charge-off rates; and current economic conditions that may affect a borrower s ability to repay. Although management believes it has established and maintained the allowance for loan losses at appropriate levels, future adjustments may be necessary if economic, real estate and other conditions differ substantially from the current operating environment.

Interest Income Recognition:

Interest on loans is included in income as earned based upon interest rates applied to unpaid principal. Interest is not accrued on loans 90 days or more past due unless the loans are adequately secured and in the process of collection. Interest is not accrued on other loans when management believes collection is doubtful. All loans considered impaired are non-accruing. Interest on non-accruing loans is recognized as payments are received when the ultimate collectibility of interest is no longer considered doubtful. When a loan is placed on non-accrual status, all interest previously accrued is reversed against current-period interest income.

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Wake Forest Bancshares, Inc.
March 31, 2008

Item 3. Controls and Procedures

Management, including the Company s Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company s disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(f) and 15d-15(e)) as of the end of the period covered by this report. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the disclosure controls and procedures were effective, in all material respects, to ensure that information required to be disclosed in the reports the Company files and submits under the Exchange Act is recorded, processed, summarized and reported as and when required.

There have been no changes in the Company s internal control over financial reporting identified in connection with the evaluation that occurred during the Company s last fiscal quarter that has materially affected, or that is reasonably likely to materially affect, the Company s internal control over financial reporting.

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Wake Forest Bancshares, Inc.

Part II. OTHER INFORMATION

Item 1. Legal Proceedings

The Company is not engaged in any material legal proceedings at the present time. Occasionally, the Association is a party to legal proceedings within the normal course of business wherein it enforces its security interest in loans made by it, and other matters of a similar nature.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

None

Item 3. Defaults Upon Senior Securities

None

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

On February 19, 2008, the annual meeting of stockholders was held to consider and vote upon the election of four directors of the Company and to ratify the appointment of Dixon Hughes PLLC as independent auditors for the Company s fiscal year ending September 30, 2008. All items were approved by the stockholders as shown below.

Vote concerning the election of directors of the Company:

	For	Against	Withheld	Total
Howard L. Brown	1,051,582		3,991	1,055,573
R.W. Wilkinson III	1,051,582		3,991	1,055,573
Robert C. White	1,051,582		3,991	1,055,573

Vote concerning ratification of Dixon Hughes PLLC as independent auditors for the year ending September 30, 2008:

For	Against	Abstained	Total
1,055,048	325	200	1,055,573

The foregoing matters are described in detail in the Company s proxy statement dated January 18, 2008 for the 2008 Annual Meeting of stockholders.

Item 5. Other Information

None

Item 6. Exhibits

a) Exhibit 31 Certification of Pursuant to 18 U.S.C. Section 1350, as adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

b) Exhibit 32 Certification of 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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SIGNATURES

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

	Wake Forest Bancshares, Inc.
Dated May 12, 2008	By: /s/ Robert C. White Robert C. White Chief Executive Officer and Chief Financial Officer

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EXHIBIT INDEX

Exhibit 31	Certification of Pursuant to 18 U.S.C. Section 1350, as adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
Exhibit 32	Certification of Pursuant to 18 U.S.C. Section 1350, as adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.