

OCEANFIRST FINANCIAL CORP  
Form 10-Q  
November 08, 2007  
Table of Contents

---

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, DC 20549

\_\_\_\_\_  
**FORM 10-Q**  
\_\_\_\_\_

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

For the quarterly period ended September 30, 2007

**.. 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 0-27428

\_\_\_\_\_  
**OceanFirst Financial Corp.**

(Exact name of registrant as specified in its charter)

\_\_\_\_\_  
**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**22-3412577**  
(I.R.S. Employer  
Identification No.)

**975 Hooper Avenue, Toms River, NJ**  
(Address of principal executive offices)

**08754-2009**  
(Zip Code)

Registrant's telephone number, including area code: (732)240-4500

Edgar Filing: OCEANFIRST FINANCIAL CORP - Form 10-Q

---

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer  Accelerated Filer  Non-accelerated Filer

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

As of November 6, 2007, there were 12,346,465 shares of the Registrant's Common Stock, par value \$.01 per share, outstanding.

---

**Table of Contents**

**OceanFirst Financial Corp.**

INDEX TO FORM 10-Q

|   | <b>PAGE</b> |
|---|-------------|
| <b><u>PART I. FINANCIAL INFORMATION</u></b>   |             |
| Item 1. Consolidated Financial Statements (Unaudited)   |             |
| <u>Consolidated Statements of Financial Condition as of September 30, 2007 and December 31, 2006</u>                    | 1           |
| <u>Consolidated Statements of Operations for the three and nine months ended September 30, 2007 and 2006</u>            | 2           |
| <u>Consolidated Statements of Changes in Stockholders' Equity for the nine months ended September 30, 2007 and 2006</u> | 3           |
| <u>Consolidated Statements of Cash Flows for the nine months ended September 30, 2007 and 2006</u>                      | 4           |
| <u>Notes to Unaudited Consolidated Financial Statements</u>   | 6           |
| Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>                    | 8           |
| Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>   | 16          |
| Item 4. <u>Controls and Procedures</u>  | 17          |
| <b><u>PART II. OTHER INFORMATION</u></b>  |             |
| Item 1. <u>Legal Proceedings</u>  | 17          |
| Item 1A. <u>Risk Factors</u>  | 17          |
| Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>  | 18          |
| Item 3. <u>Defaults Upon Senior Securities</u>  | 18          |
| Item 4. <u>Submission of Matters to a Vote of Security Holders</u>  | 18          |
| Item 5. <u>Other Information</u>  | 18          |
| Item 6. <u>Exhibits</u>   | 18          |
| <u>Signatures</u>   | 19          |

**Table of Contents****OceanFirst Financial Corp.****Consolidated Statements of Financial Condition**

(dollars in thousands, except per share amounts)

|  | September 30,<br>2007<br>(Unaudited) | December 31,<br>2006 |
|--|--------------------------------------|----------------------|
| <b>ASSETS</b>  |                                      |                      |
| Cash and due from banks  | \$ 29,456                            | \$ 32,204            |
| Investment securities available for sale   | 58,133                               | 82,384               |
| Federal Home Loan Bank of New York stock, at cost  | 22,040                               | 25,346               |
| Mortgage-backed securities available for sale  | 58,285                               | 68,369               |
| Loans receivable, net  | 1,678,937                            | 1,701,425            |
| Mortgage loans held for sale   | 3,244                                | 82,943               |
| Interest and dividends receivable  | 8,357                                | 8,083                |
| Real estate owned, net   | 433                                  | 288                  |
| Premises and equipment, net  | 17,372                               | 18,196               |
| Servicing asset  | 9,340                                | 9,787                |
| Bank Owned Life Insurance  | 38,087                               | 37,145               |
| Intangible Assets  | 23                                   | 1,114                |
| Other assets   | 13,123                               | 9,718                |
| <b>Total assets</b>  | <b>\$ 1,936,830</b>                  | <b>\$ 2,077,002</b>  |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>  |                                      |                      |
| Deposits   | \$ 1,310,941                         | \$ 1,372,328         |
| Securities sold under agreements to repurchase with retail customers   | 69,742                               | 50,982               |
| Securities sold under agreements to repurchase with the Federal Home Loan Bank   | 13,000                               | 34,000               |
| Federal Home Loan Bank advances  | 371,500                              | 430,500              |
| Other borrowings   | 27,500                               | 17,500               |
| Advances by borrowers for taxes and insurance  | 8,247                                | 7,743                |
| Other liabilities  | 12,329                               | 31,629               |
| <b>Total liabilities</b>   | <b>1,813,259</b>                     | <b>1,944,682</b>     |
| <b>Stockholders' equity:</b>   |                                      |                      |
| Preferred stock, \$.01 par value, 5,000,000 shares authorized, no shares issued  |                                      |                      |
| Common stock, \$.01 par value, 55,000,000 shares authorized, 27,177,372 shares issued and 12,341,915 and 12,262,307 shares outstanding at September 30, 2007 and December 31, 2006, respectively | 272                                  | 272                  |
| Additional paid-in capital   | 203,237                              | 201,936              |
| Retained earnings  | 154,317                              | 164,121              |
| Accumulated other comprehensive loss   | (2,704)                              | (470)                |
| Less: Unallocated common stock held by Employee Stock Ownership Plan   | (5,612)                              | (6,369)              |
| Treasury stock, 14,835,457 and 14,915,065 shares at September 30, 2007 and December 31, 2006, respectively   | (225,939)                            | (227,170)            |
| Common stock acquired by Deferred Compensation Plan  | 1,406                                | 1,457                |
| Deferred Compensation Plan Liability   | (1,406)                              | (1,457)              |
| <b>Total stockholders' equity</b>  | <b>123,571</b>                       | <b>132,320</b>       |

Edgar Filing: OCEANFIRST FINANCIAL CORP - Form 10-Q

|  |              |              |
|--|--------------|--------------|
| Total liabilities and stockholders' equity | \$ 1,936,830 | \$ 2,077,002 |
|--|--------------|--------------|

See accompanying Notes to Unaudited Consolidated Financial Statements.

**Table of Contents****OceanFirst Financial Corp.****Consolidated Statements of Operations**

(in thousands, except per share amounts)

|  | For the three months<br>ended September 30,<br>2007 |               | For the nine months<br>ended September 30,<br>2006 |               |
|--|---|---------------|--|---------------|
|  | (Unaudited)   |               | (Unaudited)  |               |
| <b>Interest income:</b>  |   |               |  |               |
| Loans  | \$ 25,945   | \$ 27,825     | \$ 79,528  | \$ 79,051     |
| Mortgage-backed securities   | 688   | 812           | 2,127  | 2,518         |
| Investment securities and other  | 1,590   | 1,679         | 5,494  | 5,102         |
| <b>Total interest income</b>   | <b>28,223</b>                                       | <b>30,316</b> | <b>87,149</b>                                      | <b>86,671</b> |
| <b>Interest expense:</b>   |   |               |  |               |
| Deposits   | 9,326   | 8,939         | 27,778   | 24,040        |
| Borrowed funds   | 6,066   | 6,918         | 19,431   | 18,343        |
| <b>Total interest expense</b>  | <b>15,392</b>                                       | <b>15,857</b> | <b>47,209</b>                                      | <b>42,383</b> |
| <b>Net interest income</b>   | <b>12,831</b>                                       | <b>14,459</b> | <b>39,940</b>                                      | <b>44,288</b> |
| Provision for loan losses  | 75  | 50            | 525  | 100           |
| <b>Net interest income after provision for loan losses</b>   | <b>12,756</b>                                       | <b>14,409</b> | <b>39,415</b>                                      | <b>44,188</b> |
| <b>Other income (loss):</b>  |   |               |  |               |
| Loan servicing income  | 126   | 136           | 356  | 408           |
| Fees and service charges   | 2,942   | 2,677         | 8,724  | 7,854         |
| Net gain (loss) and lower of cost or market adjustment on sales of loans and securities available for sale | 1,156   | 3,515         | (11,676)   | 8,474         |
| Net income (loss) from other real estate operations  | 8   | (60)          | 27   | (60)          |
| Income from Bank Owned Life Insurance  | 324   | 291           | 942  | 840           |
| Other  | 6   | 44            | 41   | 55            |
| <b>Total other income (loss)</b>   | <b>4,562</b>  | <b>6,603</b>  | <b>(1,586)</b>                                     | <b>17,571</b> |
| <b>Operating expenses:</b>   |   |               |  |               |
| Compensation and employee benefits   | 6,755   | 7,497         | 22,227   | 22,752        |
| Occupancy  | 1,569   | 1,244         | 4,028  | 3,564         |
| Equipment  | 543   | 767           | 1,631  | 1,975         |
| Marketing  | 359   | 531           | 1,046  | 1,230         |
| Federal deposit insurance  | 168   | 133           | 444  | 400           |
| Data processing  | 859   | 859           | 2,625  | 2,569         |
| General and administrative   | 2,357   | 2,483         | 8,430  | 7,735         |
| Goodwill impairment  |   |               | 1,014  |               |
| <b>Total operating expenses</b>  | <b>12,610</b>                                       | <b>13,514</b> | <b>41,445</b>                                      | <b>40,225</b> |
| <b>Income (loss) before provision (benefit) for income taxes</b>   | <b>4,708</b>  | <b>7,498</b>  | <b>(3,616)</b>                                     | <b>21,534</b> |
| Provision (benefit) for income taxes   | 1,582   | 2,592         | (1,597)  | 7,461         |

Edgar Filing: OCEANFIRST FINANCIAL CORP - Form 10-Q

|                                    |          |          |            |           |
|------------------------------------|----------|----------|------------|-----------|
| Net income (loss)                  | \$ 3,126 | \$ 4,906 | \$ (2,019) | \$ 14,073 |
| Basic earnings (loss) per share    | \$ 0.27  | \$ 0.43  | \$ (0.18)  | \$ 1.22   |
| Diluted earnings (loss) per share  | \$ 0.27  | \$ 0.42  | \$ (0.18)  | \$ 1.18   |
| Average basic shares outstanding   | 11,561   | 11,465   | 11,522     | 11,567    |
| Average diluted shares outstanding | 11,643   | 11,689   | 11,522     | 11,880    |

See accompanying Notes to Unaudited Consolidated Financial Statements.

**Table of Contents****OceanFirst Financial Corp.****Consolidated Statements of****Changes in Stockholders' Equity (Unaudited)**

(in thousands, except per share amounts)

|  | Common<br>Stock | Additional<br>Paid-In<br>Capital | Retained<br>Earnings | Accumulated<br>Other<br>Comprehensive<br>Loss | Employee<br>Stock<br>Ownership<br>Plan | Treasury<br>Stock | Common Stock<br>Acquired<br>by<br>Deferred<br>Compensation<br>Plan | Deferred<br>Compensation<br>Plan<br>Liability | Total      |
|--|-----------------|----------------------------------|----------------------|---|--|-------------------|--|---|------------|
| Balance at<br>December 31, 2005                                | \$ 272          | \$ 197,621                       | \$ 164,613           | \$ (1,223)                                    | \$ (7,472)                             | \$ (215,027)      | \$ 1,383   | \$ (1,383)                                    | \$ 138,784 |
| Comprehensive<br>income:                                       |                 |                                  |                      |   |  |                   |  |   |            |
| Net income   |                 |                                  | 14,073               |   |  |                   |  |   | 14,073     |
| Other comprehensive<br>income:                                 |                 |                                  |                      |   |  |                   |  |   |            |
| Unrealized gain on<br>securities (net of tax<br>expense \$244) |                 |                                  |                      | 354   |  |                   |  |   | 354        |
| Total comprehensive<br>income                                  |                 |                                  |                      |   |  |                   |  |   | 14,427     |
| Stock award  |                 | 278                              |                      |   |  |                   |  |   | 278        |
| Tax benefit of stock<br>plans                                  |                 | 2,035                            |                      |   |  |                   |  |   | 2,035      |
| Purchase 669,604<br>shares of common<br>stock                  |                 |                                  |                      |   |  | (15,288)          |  |   | (15,288)   |
| Allocation of ESOP<br>stock                                    |                 |                                  |                      |   | 827                                    |                   |  |   | 827        |
| ESOP adjustment  |                 | 1,385                            |                      |   |  |                   |  |   | 1,385      |
| Cash dividend \$.60 per<br>share                               |                 |                                  | (6,897)              |   |  |                   |  |   | (6,897)    |
| Exercise of stock<br>options                                   |                 |                                  | (3,720)              |   |  | 5,179             |  |   | 1,459      |
| Purchase of stock for<br>the deferred<br>compensation plan     |                 |                                  |                      |   |  |                   | 134  | (134)   |            |
| Balance at<br>September 30, 2006                               | \$ 272          | \$ 201,319                       | \$ 168,069           | \$ (869)                                      | \$ (6,645)                             | \$ (225,136)      | \$ 1,517   | \$ (1,517)                                    | \$ 137,010 |
| Balance at<br>December 31, 2006                                | \$ 272          | \$ 201,936                       | \$ 164,121           | \$ (470)                                      | \$ (6,369)                             | \$ (227,170)      | \$ 1,457   | \$ (1,457)                                    | \$ 132,320 |

Edgar Filing: OCEANFIRST FINANCIAL CORP - Form 10-Q

|  |    |       |     |         |    |         |    |         |         |           |
|--|----|-------|-----|---------|----|---------|----|---------|---------|-----------|
| Comprehensive loss:  |    |       |     |         |    |         |    |         |         |           |
| Net loss   |    |       |     |         |    |         |    |         |         | (2,019)   |
| Other comprehensive loss:                                  |    |       |     |         |    |         |    |         |         |           |
| Unrealized loss on securities (net of tax benefit \$1,543) |    |       |     |         |    |         |    |         | (2,234) | (2,234)   |
| Total comprehensive loss                                   |    |       |     |         |    |         |    |         |         | (4,253)   |
| Stock awards   |    | 354   |     |         |    |         |    |         |         | 354       |
| Treasury stock allocated to restricted stock plan          |    | (295) | (3) |         |    | 298     |    |         |         |           |
| Tax benefit of stock plans                                 |    | 337   |     |         |    |         |    |         |         | 337       |
| Purchase 49,701 shares of common stock                     |    |       |     |         |    |         |    |         | (1,112) | (1,112)   |
| Allocation of ESOP stock                                   |    |       |     |         |    | 757     |    |         |         | 757       |
| ESOP adjustment  |    | 905   |     |         |    |         |    |         |         | 905       |
| Cash dividend \$.60 per share                              |    |       |     |         |    |         |    |         | (6,784) | (6,784)   |
| Exercise of stock options                                  |    |       |     |         |    |         |    |         | 2,045   | 1,047     |
| Sale of stock for the deferred compensation plan           |    |       |     |         |    |         |    |         | (51)    | 51        |
| Balance at September 30, 2007                              | \$ | 272   | \$  | 203,237 | \$ | 154,317 | \$ | (2,704) | \$      | (5,612)   |
|  | \$ |       | \$  |         | \$ |         | \$ |         | \$      | (225,939) |
|  | \$ |       | \$  |         | \$ |         | \$ |         | \$      | 1,406     |
|  | \$ |       | \$  |         | \$ |         | \$ |         | \$      | (1,406)   |
|  | \$ |       | \$  |         | \$ |         | \$ |         | \$      | 123,571   |

See accompanying Notes to Unaudited Consolidated Financial Statements.

**Table of Contents****OceanFirst Financial Corp.****Consolidated Statements of Cash Flows**

(dollars in thousands)

|  | For the nine months |                 |
|--|---------------------|-----------------|
|  | ended September 30, |                 |
|  | 2007                | 2006            |
|  | (Unaudited)         |                 |
| Cash flows from operating activities:  |                     |                 |
| Net (loss) income  | \$ (2,019)          | \$ 14,073       |
| Adjustments to reconcile net (loss) income to net cash provided by (used in) operating activities: |                     |                 |
| Depreciation and amortization of premises and equipment  | 1,486               | 1,531           |
| Amortization of ESOP   | 757                 | 827             |
| ESOP adjustment  | 905                 | 1,385           |
| Stock award  | 354                 | 278             |
| Amortization of servicing asset  | 1,648               | 1,509           |
| Amortization and impairment of intangible assets   | 1,091               | 77              |
| Net premium amortization in excess of discount accretion on securities                             | 81                  | 194             |
| Net amortization of deferred costs and discounts on loans  | 729                 | 506             |
| Provision for loan losses  | 525                 | 100             |
| Lower of cost or market write-down on loans held for sale  | 9,400               |                 |
| Provision for repurchased loans  | 3,760               |                 |
| Net loss on write-off of fixed assets  | 21                  |                 |
| Net loss on sale of real estate owned  | (11)                | 99              |
| Net gain on sales of loans and securities  | (1,484)             | (8,474)         |
| Loans repurchased  | (1,012)             |                 |
| Proceeds from sales of mortgage loans held for sale  | 352,373             | 514,441         |
| Mortgage loans originated for sale   | (281,342)           | (537,480)       |
| Increase in value of Bank Owned Life Insurance   | (942)               | (840)           |
| Increase in interest and dividends receivable  | (274)               | (1,277)         |
| Increase in other assets   | (1,862)             | (627)           |
| (Decrease) increase in other liabilities   | (12,453)            | 11,761          |
| <b>Total adjustments</b>   | <b>73,750</b>       | <b>(15,990)</b> |
| <b>Net cash provided by (used in) operating activities</b>   | <b>71,731</b>       | <b>(1,917)</b>  |
| Cash flows from investing activities:  |                     |                 |
| Net decrease (increase) in loans receivable  | 15,880              | (60,892)        |
| Loans repurchased  | (14,128)            |                 |
| Proceeds from sales of loans repurchased   | 8,666               |                 |
| Proceeds from maturities or calls of investment securities available for sale                      | 20,780              | 2,584           |
| Purchase of investment securities available for sale   | (681)               | (748)           |
| Proceeds from sale of investment securities available for sale                                     |                     | 437             |
| Proceeds from sale of mortgage-backed securities available for sale                                |                     | 6,241           |
| Purchase of mortgage-backed securities available for sale  |                     | (6,439)         |
| Principal payments on mortgage-backed securities available for sale                                | 10,378              | 13,480          |
| Decrease (increase) in Federal Home Loan Bank of New York stock                                    | 3,306               | (2,842)         |
| Net proceeds (disbursements) from sales and acquisition of real estate owned                       | 638                 | (39)            |
| Purchases of premises and equipment  | (683)               | (3,135)         |

Edgar Filing: OCEANFIRST FINANCIAL CORP - Form 10-Q

|   |        |           |
|---|--------|-----------|
| Net cash provided by (used in) investing activities | 44,156 | (51,353)  |
|   |        | Continued |

**Table of Contents****OceanFirst Financial Corp.****Consolidated Statements of Cash Flows (Continued)**

(dollars in thousands)

|  | <b>For the nine months</b> |                    |
|--|----------------------------|--------------------|
|  | <b>ended September 30,</b> | <b>2006</b>        |
|  | <b>2007</b>                | <b>(Unaudited)</b> |
| <b>Cash flows from financing activities:</b>   |                            |                    |
| (Decrease) increase in deposits  | \$ (61,387)                | \$ 15,170          |
| Increase (decrease) in short-term borrowings   | 3,760                      | (3,939)            |
| Repayments of securities sold under agreements to repurchase with the Federal Home Loan Bank |                            | (10,000)           |
| Proceeds from Federal Home Loan Bank advances  | 20,000                     | 190,000            |
| Repayments of Federal Home Loan Bank advances  | (85,000)                   | (127,000)          |
| Proceeds from other borrowings   | 10,000                     | 12,500             |
| Increase in advances by borrowers for taxes and insurance                                    | 504                        | 1,089              |
| Exercise of stock options  | 1,047                      | 1,459              |
| Dividends paid   | (6,784)                    | (6,897)            |
| Purchase of treasury stock   | (1,112)                    | (15,288)           |
| Tax benefit of stock plans   | 337                        | 2,035              |
| <b>Net cash (used in) provided by financing activities</b>                                   | <b>(118,635)</b>           | <b>59,129</b>      |
| <b>Net (decrease) increase in cash and due from banks</b>                                    | <b>(2,748)</b>             | <b>5,859</b>       |
| <b>Cash and due from banks at beginning of period</b>  | <b>32,204</b>              | <b>31,108</b>      |
| <b>Cash and due from banks at end of period</b>  | <b>\$ 29,456</b>           | <b>\$ 36,967</b>   |
| <b>Supplemental Disclosure of Cash Flow Information:</b>                                     |                            |                    |
| <b>Cash paid during the period for:</b>  |                            |                    |
| Interest   | \$ 47,590                  | \$ 41,689          |
| Income taxes   | 227                        | 3,947              |
| <b>Non cash activities:</b>  |                            |                    |
| Transfer of loans receivable to real estate owned  | 772                        | 70                 |
| Transfer of securities sold under agreements to repurchase to advances                       | 21,000                     | 15,000             |

See accompanying Notes to Unaudited Consolidated Financial Statements.

**Table of Contents****OceanFirst Financial Corp.****Notes To Unaudited Consolidated Financial Statements****Note 1. Summary of Significant Accounting Policies**

The accompanying unaudited consolidated financial statements include the accounts of OceanFirst Financial Corp. (the Company) and its wholly-owned subsidiary, OceanFirst Bank (the Bank) and its wholly-owned subsidiaries, Columbia Home Loans, LLC, OceanFirst REIT Holdings, LLC, and OceanFirst Services, LLC. At September 30, 2007 most of the operations of Columbia Home Loans, LLC were discontinued.

The interim consolidated financial statements reflect all normal and recurring adjustments which are, in the opinion of management, considered necessary for a fair presentation of the financial condition and results of operations for the periods presented. The results of operations for the three and nine months ended September 30, 2007 are not necessarily indicative of the results of operations that may be expected for all of 2007.

Certain information and note disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted, pursuant to the rules and regulations of the Securities and Exchange Commission (the SEC).

These unaudited consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company's Annual Report to Stockholders on Form 10-K for the year ended December 31, 2006.

Certain amounts previously reported have been reclassified to conform to the current period's classification.

**Earnings per Share**

The following reconciles shares outstanding for basic and diluted earnings per share for the three and nine months ended September 30, 2007 and 2006 (in thousands):

|  | <b>Three months ended</b> |                      | <b>Nine months ended</b> |                      |
|--|---------------------------|----------------------|--------------------------|----------------------|
|  | <b>September 30,</b>      | <b>September 30,</b> | <b>September 30,</b>     | <b>September 30,</b> |
|  | <b>2007</b>               | <b>2006</b>          | <b>2007</b>              | <b>2006</b>          |
| Weighted average shares issued net of Treasury shares                            | 12,329                    | 12,345               | 12,317                   | 12,481               |
| Less: Unallocated ESOP shares  | (681)                     | (804)                | (710)                    | (837)                |
| Unallocated incentive award shares and shares held by deferred compensation plan | (87)                      | (76)                 | (85)                     | (77)                 |
| Average basic shares outstanding   | 11,561                    | 11,465               | 11,522                   | 11,567               |
| Add: Effect of dilutive securities:  |                           |                      |                          |                      |
| Stock options  | 15                        | 150                  |                          | 240                  |
| Incentive awards and shares held by deferred compensation plan                   | 67                        | 74                   |                          | 73                   |
| Average diluted shares outstanding   | 11,643                    | 11,689               | 11,522                   | 11,880               |

For the three months ended September 30, 2007 and 2006, 1,408,000 and 924,000, respectively, antidilutive stock options were excluded from earnings per share calculations. For the nine months ended September 30, 2007 and 2006, 1,312,000 and 659,000, respectively, antidilutive stock options were excluded from earnings per share calculations. In addition, for the nine months ended September 30, 2007, 113,000 antidilutive potential shares of common stock have been excluded from the calculation of average diluted shares outstanding, as the Company incurred a net loss for the period.

**Comprehensive Income (Loss)**

For the three month periods ended September 30, 2007 and 2006, total comprehensive income, representing net income plus or minus the change in unrealized gains or losses on securities available for sale amounted to \$1,224,000 and \$5,598,000, respectively. For the nine months ended September 30, 2007 and 2006 total comprehensive (loss) income amounted to \$(4,253,000) and \$14,427,000.



**Table of Contents****Note 2. Loans Receivable, Net**

Loans receivable, net at September 30, 2007 and December 31, 2006 consisted of the following (in thousands):

|   | September 30, 2007  | December 31, 2006   |
|---|---------------------|---------------------|
| Real estate:                                  |                     |                     |
| One-to-four family                            | \$ 1,104,566        | \$ 1,231,716        |
| Commercial real estate, multi-family and land | 317,080             | 306,288             |
| Construction                                  | 14,172              | 13,475              |
| Consumer                                      | 209,232             | 190,029             |
| Commercial                                    | 46,532              | 49,693              |
| <b>Total loans</b>                            | <b>1,691,582</b>    | <b>1,791,201</b>    |
| Loans in process                              | (3,883)             | (2,318)             |
| Deferred origination costs, net               | 5,169               | 5,723               |
| Allowance for loan losses                     | (10,687)            | (10,238)            |
| <b>Total loans, net</b>                       | <b>1,682,181</b>    | <b>1,784,368</b>    |
| Less: Mortgage loans held for sale            | 3,244               | 82,943              |
| <b>Loans receivable, net</b>                  | <b>\$ 1,678,937</b> | <b>\$ 1,701,425</b> |

**Note 3. Reserve for Repurchased Loans**

An analysis of the reserve for repurchased loans for the three and nine months ended September 30, 2007 follows (in thousands). There was no balance in the reserve at September 30, 2006. The reserve is included in other liabilities in the accompanying statement of financial condition.

|  | Three months ended    | Nine months ended  |
|--|-----------------------|--------------------|
|  | September 30,<br>2007 | September 30, 2007 |
| Balance at beginning of period             | \$ 5,397              | \$ 9,600           |
| (Recovery) provision charged to operations | (200)                 | 3,760              |
| Loss on loans repurchased                  | (2,444)               | (10,607)           |
| <b>Balance at end of period</b>            | <b>\$ 2,753</b>       | <b>\$ 2,753</b>    |

The reserve for repurchased loans is established to provide for expected losses related to outstanding loan repurchase requests and additional repurchase requests which may be received on loans previously sold to investors. In establishing the reserve for repurchased loans, the Company considered all types of sold loans, however, the actual types of loans which resulted in loss estimates included subprime loans with 100% financing, all other subprime loans and a small amount of ALT-A loans. At September 30, 2007, the Company utilized \$15.1 million to repurchase loans from investors of which \$12.2 million were subsequently resold. Also, at September 30, 2007 the Company had unresolved loan repurchase requests of \$618,000.

**Note 4. Deposits**

The major types of deposits at September 30, 2007 and December 31, 2006 were as follows (in thousands):

Edgar Filing: OCEANFIRST FINANCIAL CORP - Form 10-Q

| <u>Type of Account</u>    | September 30, 2007 | December 31, 2006 |
|---------------------------|--------------------|-------------------|
| Non-interest-bearing      | \$ 113,488         | \$ 114,950        |
| Interest-bearing checking | 442,195            | 408,666           |
| Money market deposit      | 86,442             | 105,571           |
| Savings                   | 193,872            | 200,544           |
| Time deposits             | 474,944            | 542,597           |
|                           | \$ 1,310,941       | \$ 1,372,328      |

**Table of Contents****Note 5. Recent Accounting Pronouncements**

In February 2007, the Financial Accounting Standards Board ( FASB ) issued Statement of Financial Accounting Standards ( SFAS ) No. 159, The Fair Value Option for Financial Assets and Financial Liabilities . SFAS No. 159 permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. The statement is effective as of the beginning of an entity s first fiscal year that begins after November 15, 2007 with early adoption permitted as of the beginning of a fiscal year that begins on or before November 15, 2007. The Company does not expect the adoption of statement No. 159 to have a material impact on its financial statements.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements. This Statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This Statement applies under other accounting pronouncements that require or permit fair value measurements, the FASB having previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. Accordingly, this Statement does not require any new fair value measurements. The Statement is effective for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. The Company does not expect the adoption of Statement No. 157 to have a material impact on its financial statements.

In June 2006, the FASB issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes. The interpretation clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with FASB Statement 109

Accounting for Income Taxes. This Interpretation presents a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The Company adopted the Interpretation effective January 1, 2007. The adoption of Interpretation No. 48 did not have a material impact on the Company s financial statements.

In March 2006, the FASB issued SFAS No. 156, Accounting for Servicing of Financial Assets. SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, establishes, among other things, the accounting for all separately recognized servicing assets and servicing liabilities. SFAS No. 156 amends Statement 140 to require that all separately recognized servicing assets and servicing liabilities be initially measured at fair value, if practicable. This Statement permits, but does not require, the subsequent measurement of separately recognized servicing assets and servicing liabilities at fair value. An entity that uses derivative instruments to mitigate the risks inherent in servicing assets and servicing liabilities is required to account for those derivative instruments at fair value. Under this Statement, an entity can elect subsequent fair value measurement to account for its separately recognized servicing assets and servicing liabilities. By electing that option, an entity may simplify its accounting because this Statement permits income statement recognition of the potential offsetting changes in fair value of those servicing assets and servicing liabilities and derivative instruments in the same accounting period. The Company adopted the Statement effective January 1, 2007. The adoption of SFAS No. 156 did not have a material impact on the Company s financial statements.

**Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations**  
**Critical Accounting Policies**

Note 1 to the Company s Audited Consolidated Financial Statements for the year ended December 31, 2006 included in the Company s Annual Report on Form 10-K for the year ended December 31, 2006, as supplemented by this report, contains a summary of significant accounting policies. Various elements of these accounting policies, by their nature, are inherently subject to estimation techniques, valuation assumptions and other subjective assessments. Certain assets are carried in the consolidated statements of financial condition at fair value or the lower of cost or fair value. Policies with respect to the methodologies used to determine the allowance for loan losses, the reserve for repurchased loans, the valuation of Mortgage Servicing Rights and judgments regarding securities impairment are the most critical accounting policies because they are important to the presentation of the Company s financial condition and results of operations, involve a higher degree of complexity and require management to make difficult and subjective judgments which often require assumptions or estimates about highly uncertain matters. The use of different judgments, assumptions and estimates could result in material differences in the results of operations or financial condition. These critical accounting policies and their application are reviewed periodically and, at least annually, with the Audit Committee of the Board of Directors.

---

**Table of Contents****Summary**

The Company's results of operations are primarily dependent on net interest income, which is the difference between the interest income earned on interest-earning assets, such as loans and investments, and the interest expense on interest-bearing liabilities, such as deposits and borrowings. The Company also generates non-interest income such as income from loan sales, loan servicing, loan originations, merchant credit card services, deposit accounts, the sale of alternative investments, trust and asset management services and other fees. The Company's operating expenses primarily consist of compensation and employee benefits, occupancy and equipment, marketing, data processing and general and administrative expenses. The Company's results of operations are also significantly affected by general economic and competitive conditions, particularly changes in market interest rates, government policies and actions of regulatory agencies.

During the second quarter, the Board of Directors of the Bank decided to discontinue most of the operations of Columbia Homes Loans, LLC, the Bank's mortgage banking subsidiary. During the third quarter, the Bank decided to completely shutter all of Columbia's loan origination activity by discontinuing the two remaining small loan production offices. The Bank is retaining Columbia's loan servicing portfolio. Columbia originated a full product line of residential mortgage loans including the origination of subprime mortgage loans. These subprime loans were ordinarily sold to investors in the normal course of business. The loan sale agreements generally required Columbia to repurchase certain loans previously sold in the event of an early payment default, generally defined as the failure by the borrower to make a payment within a designated period early in the loan term. Columbia may also be required to repurchase a loan in the event of a breach to a representation or warranty. Columbia experienced early payment defaults primarily related to subprime mortgage loans with 100% financing relative to the value of the underlying property. During the first quarter of 2007, Columbia originated \$38.2 million in subprime loans of which \$8.7 million were loans with 100% financing. In March 2007, the Company discontinued the origination of all subprime loans. A reserve was established to account for Columbia's potential obligation to repurchase loans. In establishing the reserve for repurchased loans, the Company considered all types of sold loans, however, the actual types of loans which resulted in loss estimates included subprime loans with 100% financing, all other subprime loans and a small amount of ALT-A loans. As a result of the analysis of the reserve for repurchased loans at September 30, 2007, the Company recognized a reversal of the provision for repurchased loans of \$200,000 for the quarter ended September 30, 2007. For the nine months ended September 30, 2007, the provision for repurchased loans was \$3.8 million which is included as part of the gain (loss) on sale of loans. Columbia also maintained an inventory of loans held for sale. These loans were originated for sale to investors, however, a large amount of subprime loans remained unsold at March 31, 2007 due to a significant decline in liquidity in the subprime loan market during the first quarter of 2007, primarily related to changes in investor product specifications. The loans were initially underwritten to the specifications of particular investors and were generally intended to be sold in bulk. When the investors' product specifications changed, there was an absence of traditional buyers for these loans creating the significant decline in liquidity in the subprime loan market. During the second quarter of 2007, Columbia closed on a bulk sale of subprime loans with a stated principal balance of \$42.6 million for which Columbia recognized a loss on sale, net of reserves, of \$1.3 million. Additionally, included in the loss on sale of loans for the nine months ended September 30, 2007, is a charge of \$9.4 million incurred by Columbia to reduce loans held for sale to their current fair market value. There was no lower of cost or market value charge for the quarter ended September 30, 2007. At September 30, 2007, Columbia was holding subprime loans with a gross principal balance of \$7.2 million and a carrying value, net of reserves and lower of cost or market adjustment, of \$4.4 million.

The interest rate yield curve began the year in an inverted position and generally remained flat to inverted through most of the second quarter when longer-term rates rose and the interest rate yield curve had a modest upward slope. During the third quarter shorter-term rates began to decline resulting in a continued upward slope to the interest rate yield curve. The flat to inverted yield curve experienced throughout most of 2006 and through the beginning of 2007 has generally had a negative impact on the Bank's results of operations and net interest margin as interest-earning assets, both loans and securities, are priced against longer-term indices, while interest-bearing liabilities, primarily deposits and borrowings, are priced against shorter-term indices. The Bank has generally not repriced all core deposits (defined as all deposits other than time deposits) at the same pace as market increases in short-term interest rates. Any upward repricing of core deposits would likely have a negative impact on the Bank's results of operations and net interest margin. Conversely, a prolonged steepening to the yield curve may have a small positive impact on the Bank's results of operations and net interest margin in the latter part of 2007 and into 2008.

**Table of Contents****Analysis of Net Interest Income**

Net interest income represents the difference between income on interest-earning assets and expense on interest-bearing liabilities. Net interest income depends upon the relative amounts of interest-earning assets and interest-bearing liabilities and the interest rate earned or paid on them.

The following tables set forth certain information relating to the Company for the three and nine months ended September 30, 2007 and 2006. The yields and costs are derived by dividing income or expense by the average balance of assets or liabilities, respectively, for the periods shown except where noted otherwise. Average balances are derived from average daily balances. The yields and costs include certain fees which are considered adjustments to yields.

|  | FOR THE QUARTERS ENDED SEPTEMBER 30, |           |  |              |           |                |
|--|--------------------------------------|-----------|--|--------------|-----------|----------------|
|  | 2007                                 |           |  | 2006         |           |                |
|  | AVERAGE                              |           | AVERAGE                                  | AVERAGE      |           | AVERAGE        |
|  | BALANCE                              | INTEREST  | YIELD/<br>COST<br>(Dollars in thousands) | BALANCE      | INTEREST  | YIELD/<br>COST |
| <b>Assets</b>  |                                      |           |  |              |           |                |
| Interest-earnings assets:                            |                                      |           |  |              |           |                |
| Interest-earning deposits and short-term investments | \$ 17,191                            | \$ 217    | 5.05%                                    | \$ 8,960     | \$ 117    | 5.22%          |
| Investment securities (1)                            | 62,836                               | 895       | 5.70                                     | 83,917       | 1,212     | 5.78           |
| FHLB stock   | 22,432                               | 478       | 8.52                                     | 25,940       | 350       | 5.40           |
| Mortgage-backed securities (1)                       | 60,539                               | 688       | 4.55                                     | 74,679       | 812       | 4.35           |
| Loans receivable, net (2)                            | 1,696,679                            | 25,945    | 6.12                                     | 1,806,060    | 27,825    | 6.16           |
| Total interest-earning assets                        | 1,859,677                            | 28,223    | 6.07                                     | 1,999,556    | 30,316    | 6.06           |
| Non-interest-earning assets                          | 102,284                              |           |  | 99,144       |           |                |
| Total assets   | \$ 1,961,961                         |           |  | \$ 2,098,700 |           |                |
| <b>Liabilities and Stockholders Equity</b>           |                                      |           |  |              |           |                |
| Interest-bearing liabilities:                        |                                      |           |  |              |           |                |
| Transaction deposits                                 | \$ 727,233                           | 3,837     | 2.11                                     | \$ 703,986   | 3,039     | 1.73           |
| Time deposits  | 488,688                              | 5,489     | 4.49                                     | 557,093      | 5,900     | 4.24           |
| Total  | 1,215,921                            | 9,326     | 3.07                                     | 1,261,079    | 8,939     | 2.84           |
| Borrowed funds                                       | 489,662                              | 6,066     | 4.96                                     | 567,003      | 6,918     | 4.88           |
| Total interest-bearing liabilities                   | 1,705,583                            | 15,392    | 3.61                                     | 1,828,082    | 15,857    | 3.47           |
| Non-interest-bearing deposits                        | 116,895                              |           |  | 124,998      |           |                |
| Non-interest-bearing liabilities                     | 16,834                               |           |  | 12,896       |           |                |
| Total liabilities                                    | 1,839,312                            |           |  | 1,965,976    |           |                |
| Stockholders equity                                  | 122,649                              |           |  | 132,724      |           |                |
| Total liabilities and stockholders equity            | \$ 1,961,961                         |           |  | \$ 2,098,700 |           |                |
| Net interest income                                  |                                      | \$ 12,831 |  |              | \$ 14,459 |                |
| Net interest rate spread (3)                         |                                      |           | 2.46%                                    |              |           | 2.59%          |

Edgar Filing: OCEANFIRST FINANCIAL CORP - Form 10-Q

|                         |       |       |
|-------------------------|-------|-------|
| Net interest margin (4) | 2.76% | 2.89% |
|-------------------------|-------|-------|

|  | FOR THE NINE MONTHS ENDED SEPTEMBER 30, |                     |   |                    |                     |                           |
|--|---|---------------------|---|--------------------|---------------------|---------------------------|
|  | 2007                                    |                     |   | 2006               |                     |                           |
|  | AVERAGE<br>BALANCE                      | AVERAGE<br>INTEREST | AVERAGE<br>YIELD/<br>COST<br>(Dollars in thousands) | AVERAGE<br>BALANCE | AVERAGE<br>INTEREST | AVERAGE<br>YIELD/<br>COST |
| <b>Assets</b>  |   |                     |   |                    |                     |                           |
| Interest-earning assets:                             |   |                     |   |                    |                     |                           |
| Interest-earning deposits and short-term investments | \$ 11,212                               | \$ 430              | 5.11%   | \$ 8,706           | \$ 315              | 4.82%                     |
| Investment securities (1)                            | 69,980                                  | 3,661               | 6.98  | 84,480             | 3,880               | 6.12                      |
| FHLB stock   | 24,575                                  | 1,403               | 7.61  | 24,289             | 907                 | 4.98                      |
| Mortgage-backed securities (1)                       | 63,912                                  | 2,127               | 4.44  | 79,506             | 2,518               | 4.22                      |
| Loans receivable, net (2)                            | 1,743,488                               | 79,528              | 6.08  | 1,751,643          | 79,051              | 6.02                      |
| Total interest-earning assets                        | 1,913,167                               | 87,149              | 6.07  | 1,948,624          | 86,671              | 5.93                      |
| Non-interest-earning assets                          | 101,345                                 |                     |   | 96,516             |                     |                           |
| Total assets   | \$ 2,014,512                            |                     |   | \$ 2,045,140       |                     |                           |
| <b>Liabilities and Stockholders Equity</b>           |   |                     |   |                    |                     |                           |
| Interest-bearing liabilities:                        |   |                     |   |                    |                     |                           |
| Transaction deposits                                 | \$ 723,194                              | 11,116              | 2.05  | \$ 717,194         | 8,544               | 1.59                      |
| Time deposits  | 501,697                                 | 16,662              | 4.43  | 531,557            | 15,496              | 3.89                      |
| Total  | 1,224,891                               | 27,778              | 3.02  | 1,248,751          | 24,040              | 2.57                      |
| Borrowed funds                                       | 529,584                                 | 19,431              | 4.89  | 526,266            | 18,343              | 4.65                      |
| Total interest-bearing liabilities                   | 1,754,475                               | 47,209              | 3.59  | 1,775,017          | 42,383              | 3.18                      |
| Non-interest-bearing deposits                        | 115,299                                 |                     |   | 124,508            |                     |                           |
| Non-interest-bearing liabilities                     | 19,153                                  |                     |   | 11,563             |                     |                           |
| Total liabilities                                    | 1,888,927                               |                     |   | 1,911,088          |                     |                           |
| Stockholders equity                                  | 125,585                                 |                     |   | 134,052            |                     |                           |
| Total liabilities and stockholders equity            | \$ 2,014,512                            |                     |   | \$ 2,045,140       |                     |                           |
| Net interest income                                  |   | \$ 39,940           |   |                    | \$ 44,288           |                           |
| Net interest rate spread (3)                         |   |                     | 2.48%   |                    |                     | 2.75%                     |
| Net interest margin (4)                              |   |                     | 2.78%   |                    |                     | 3.03%                     |

- (1) Amounts are recorded at average amortized cost.
- (2) Amount is net of deferred loan fees, undisbursed loan funds, discounts and premiums and estimated loss allowances and includes loans held for sale and non-performing loans.
- (3) Net interest rate spread represents the difference between the annualized yield on interest-earning assets and the annualized cost of interest-bearing liabilities.
- (4) Net interest margin represents annualized net interest income divided by average interest-earning assets.

---

**Table of Contents**

**Comparison of Financial Condition at September 30, 2007 and December 31, 2006**

Total assets at September 30, 2007 were \$1.937 billion, a decrease of \$140.2 million, compared to \$2.077 billion at December 31, 2006.

Investment and mortgage-backed securities available for sale decreased \$34.3 million to \$116.4 million at September 30, 2007 as compared to \$150.8 million at December 31, 2006 due to calls of investment securities and repayment of mortgage-backed securities. Loans receivable, net decreased by \$22.5 million to a balance of \$1.679 billion at September 30, 2007, compared to a balance of \$1.701 billion at December 31, 2006. Increases of \$7.6 million in commercial and commercial real estate loans and \$19.2 million in consumer loans were more than offset by a decline in one-to-four family mortgage loans. Mortgage loans held for sale decreased \$79.7 million to a balance of \$3.2 million at September 30, 2007 compared to a balance of \$82.9 million at December 31, 2006. The decrease was reflective of the discontinuance of most of Columbia's mortgage banking operations.

Deposit balances decreased \$61.4 million to \$1.311 billion at September 30, 2007 from \$1.372 billion at December 31, 2006 as the Bank maintained its disciplined pricing relating to certificates of deposit. Total Federal Home Loan Bank borrowings decreased by \$80.0 million to \$384.5 million at September 30, 2007 as compared to \$464.5 million at December 31, 2006 due to lower asset balances. Additionally, during the quarter ended June 30, 2007, the Company issued \$10.0 million of debt in the form of Trust Preferred Securities which is included in other borrowings.

Stockholders' equity at September 30, 2007 decreased to \$123.6 million, compared to \$132.3 million at December 31, 2006. The Company repurchased 49,701 shares of common stock during the nine months ended September 30, 2007 at a total cost of \$1.1 million. Stockholders' equity was further reduced by the net loss, the cash dividend and an increase in accumulated other comprehensive loss.

**Comparison of Operating Results for the Three and Nine Months Ended September 30, 2007 and September 30, 2006**

**General**

Net income for the three months ended September 30, 2007 was \$3.1 million, or \$.27 per diluted share, as compared to \$4.9 million, or \$.42 per diluted share, for the corresponding prior year period. For the nine months ended September 30, 2007, the net loss was \$2.0 million, or \$.18 per diluted share, as compared to net income of \$14.1 million, or \$1.18 per diluted share, for the corresponding prior year period.

**Interest Income**

Interest income for the three and nine months ended September 30, 2007 was \$28.2 million and \$87.1 million, respectively, compared to \$30.3 million and \$86.7 million, respectively, for the three and nine months ended September 30, 2006. The yield on interest-earning assets increased to 6.07% for both the three and nine months ended September 30, 2007 as compared to 6.06% and 5.93%, respectively, for the same prior year periods. Average interest-earning assets decreased by \$139.9 million and \$35.5 million, respectively, for the three and nine months ended September 30, 2007 as compared to the same prior year periods partly reflective of the discontinuance of most of Columbia's mortgage banking operations.

**Interest Expense**

Interest expense for the three and nine months ended September 30, 2007 was \$15.4 million and \$47.2 million, respectively, compared to \$15.9 million and \$42.4 million, respectively, for the three and nine months ended September 30, 2006. The cost of interest-bearing liabilities increased to 3.61% and 3.59%, respectively, for the

**Table of Contents**

three and nine months ended September 30, 2007, as compared to 3.47% and 3.18%, respectively, in the same prior year periods. Average interest-bearing liabilities decreased by \$122.5 million and \$20.5 million, respectively, for the three and nine months ended September 30, 2007 as compared to the same prior year periods.

**Net Interest Income**

Net interest income for the three and nine months ended September 30, 2007 decreased to \$12.8 million and \$39.9 million, respectively, as compared to \$14.5 million and \$44.3 million, respectively, in the same prior year periods. The net interest margin decreased to 2.76% and 2.78%, respectively, for the three and nine months ended September 30, 2007 from 2.89% and 3.03%, respectively, in the same prior year periods. The slope of the interest rate yield curve caused the increase in the cost of interest-bearing liabilities to outpace the increase in the yield on interest-earning assets.

**Provision for Loan Losses**

For the three and nine months ended September 30, 2007, the Bank's provision for loan losses was \$75,000 and \$525,000, respectively, compared to \$50,000 and \$100,000, respectively, in the same prior year periods. Non-performing loans increased to \$9.2 million at September 30, 2007 from \$4.5 million at December 31, 2006. The non-performing loan total includes \$887,000 of repurchased one-to-four family and consumer loans and \$3.3 million of one-to-four family and consumer loans previously held-for-sale, which were previously written down to their fair market value, which included an assessment of each loan's potential credit impairment. As a result, these loans do not currently require an adjustment to the allowance for loan losses. Loans receivable, net declined modestly during the first nine months of 2007 and net charge-offs for the three and nine months ended September 30, 2007 were \$7,000 and \$76,000, respectively. The increase in the provision for loan losses was primarily due to the increase in non-performing loans.

**Other Income (Loss)**

Other income (loss) decreased to income of \$4.6 million and a loss of \$1.6 million, respectively, for the three and nine months ended September 30, 2007, compared to income of \$6.6 million and \$17.6 million, respectively, for the same prior year periods. The net gain (loss) on the sale of loans was a gain of \$1.2 million and a loss of \$11.7 million, respectively, for the three and nine months ended September 30, 2007 as compared to a net gain of \$3.5 million and \$8.5 million, respectively, for the three and nine months ended September 30, 2006. The decrease in the gain on sale is partly due to the decision to discontinue most operations of Columbia. For the three months ended September 30, 2007, the gain on the sale of loans benefited from a \$200,000 reduction to the reserve for repurchased loans. The net loss on the sale of loans for the nine months ended September 30, 2007 includes a loss of \$1.3 million on the bulk sale of subprime loans and lower of cost or market charges of \$9.4 million taken by Columbia to reduce loans held for sale to their current fair market value. Also included in the net loss on the sale of loans for the nine months ended September 30, 2007 is a \$3.8 million charge to increase the reserve for repurchased loans.

Fees and service charges increased \$265,000, or 9.9%, and \$870,000, or 11.1%, respectively, for the three and nine months ended September 30, 2007, as compared to the same prior year periods primarily related to increases in fees generated from trust services and deposit accounts.

**Operating Expenses**

Operating expenses were \$12.6 million and \$41.4 million, respectively, for the three and nine months ended September 30, 2007, as compared to \$13.5 million and \$40.2 million, respectively, in the same prior year periods. The decrease in operating expenses for the three months ended September 30, 2007 as compared to the corresponding prior year period was due to the discontinuation of most of the operations at Columbia and lower ESOP expense. These reductions were partly offset by the cost of new branches, higher professional fees and total severance costs at Columbia of \$101,000. Total severance costs for the nine months ended September 30, 2007 amounted to \$879,000. Additionally, occupancy expense for the three and nine months ended September 30, 2007 includes a \$375,000 charge for lease termination costs at Columbia. Additionally, included in operating expenses for the nine months ended September 30, 2007 is \$1.0 million representing the write-off of the previously established goodwill on the August 2000 acquisition of Columbia.

---

## **Table of Contents**

### Provision (benefit) for Income Taxes

Income tax expense (benefit) was an expense of \$1.6 million and a benefit of \$1.6 million, respectively, for the three and nine months ended September 30, 2007, as compared to an expense of \$2.6 million and \$7.5 million, respectively, for the same prior year periods.

### **Liquidity and Capital Resources**

The Company's primary sources of funds are deposits, principal and interest payments on loans and mortgage-backed securities, proceeds from the sale of loans, FHLB and other borrowings and, to a lesser extent, investment maturities. While scheduled amortization of loans is a predictable source of funds, deposit flows and mortgage prepayments are greatly influenced by general interest rates, economic conditions and competition. The Company has other sources of liquidity if a need for additional funds arises, including lines of credit and FHLB advances.

At September 30, 2007 the Company had outstanding overnight borrowings from the FHLB of \$27.5 million as compared to \$42.5 million in overnight borrowings at December 31, 2006. The Company utilizes the overnight line to fund short-term liquidity needs. The Company had total FHLB borrowings, including overnight borrowings, of \$384.5 million at September 30, 2007, a decrease from \$464.5 million at December 31, 2006.

The Company's cash needs for the nine months ended September 30, 2007 were primarily satisfied by principal payments on loans and mortgage-backed securities, maturities or calls of investment securities, proceeds from the sale of mortgage loans held for sale and the issuance of debt in the form of trust preferred securities. The cash was principally utilized for loan originations and repurchases, to fund deposit outflows and reduce Federal Home Loan Bank borrowings. For the nine months ended September 30, 2006, the cash needs of the Company were primarily satisfied by principal payments on loans and mortgage-backed securities, increased deposits and borrowings, and proceeds from the sale of mortgage loans held for sale. The cash provided was principally used for the origination of loans and the repurchase of common stock.

In the normal course of business, the Company routinely enters into various off-balance sheet commitments, primarily relating to the origination and sale of loans. At September 30, 2007, outstanding commitments to originate loans totaled \$62.1 million; outstanding unused lines of credit totaled \$188.6 million; and outstanding commitments to sell loans totaled \$11.0 million. The Company expects to have sufficient funds available to meet current commitments arising in the normal course of business.

Time deposits scheduled to mature in one year or less totaled \$422.8 million at September 30, 2007. Based upon historical experience management estimates that a significant portion of such deposits will remain with the Company.

Under the Company's stock repurchase programs, shares of OceanFirst Financial Corp. common stock may be purchased in the open market and through other privately-negotiated transactions, from time-to-time, depending on market conditions. The repurchased shares are held as treasury stock for general corporate use. For the nine months ended September 30, 2007, the Company purchased 49,701 shares of common stock at a total cost of \$1.1 million compared with purchases of 669,604 shares for the nine months ended September 30, 2006 at a total cost of \$15.3 million. At September 30, 2007, there were 489,062 shares remaining to be repurchased under the existing stock repurchase program. Cash dividends declared and paid during the first nine months of 2007 were \$6.8 million, a decrease from \$6.9 million in the same prior year period. On October 17, 2007, the Board of Directors declared a quarterly cash dividend of twenty cents (\$.20) per common share. The dividend is payable on November 16, 2007 to stockholders of record at the close of business on November 2, 2007.

The primary sources of liquidity for OceanFirst Financial Corp., the holding company of OceanFirst Bank, are capital distributions from the banking subsidiary and the issuance of debt instruments. For the first nine months of 2007, OceanFirst Financial Corp. received no dividend payments from OceanFirst Bank. The Office of Thrift Supervision (OTS) has previously notified the Bank that it does not object to the payment of capital dividends, so long as the Bank remains well capitalized after each capital distribution, and also maintains a tier one core leverage ratio above 6.0% and a total risk-based capital ratio above 10.5% after each capital distribution. The Bank's tier one core leverage ratio and total risk-based capital ratio at September 30, 2007 were 6.9% and 10.9%, respectively. Applicable Federal law or the OTS, may further limit the amount of capital distributions OceanFirst

**Table of Contents**

Bank may make. OceanFirst Financial Corp. s ability to continue to pay dividends and repurchase stock is partly dependent upon capital distributions from OceanFirst Bank and may be adversely affected by the Bank s current capital constraints. The Company raised \$10.0 million during the second quarter of 2007 from the issuance of trust preferred securities. The trust preferred securities carry a floating rate of 175 basis points over 3 month LIBOR and adjust quarterly. Accrued interest is due quarterly with principal due at the maturity date of September 1, 2037. At September 30, 2007, OceanFirst Financial Corp. held \$6.4 million in cash and \$6.3 million in investment securities available for sale. Additionally, OceanFirst Financial Corp. has an available line of credit for up to \$4.0 million.

At September 30, 2007, the Bank exceeded all of its regulatory capital requirements with tangible capital of \$134.0 million, or 6.9% of total adjusted assets, which is above the required level of \$29.1 million or 1.5%; core capital of \$134.0 million or 6.9% of total adjusted assets, which is above the required level of \$58.1 million, or 3.0%; and risk-based capital of \$144.3 million, or 10.9% of risk-weighted assets, which is above the required level of \$105.5 million or 8.0%. The Bank is considered a well-capitalized institution under the Office of Thrift Supervision s Prompt Corrective Action Regulations.

**Off-Balance-Sheet Arrangements and Contractual Obligations**

In the normal course of operations, the Company engages in a variety of financial transactions that, in accordance with generally accepted accounting principles, are not recorded in the financial statements. These transactions involve, to varying degrees, elements of credit, interest rate, and liquidity risk. Such transactions are used for general corporate purposes or for customer needs. Corporate purpose transactions are used to help manage credit, interest rate, and liquidity risk or to optimize capital. Customer transactions are used to manage customers requests for funding. These financial instruments and commitments include unused consumer lines of credit and commitments to extend credit. The Company also has outstanding commitments to sell loans amounting to \$11.0 million.

The following table shows the contractual obligations of the Company by expected payment period as of September 30, 2007 (in thousands):

| Contractual Obligation                     | Total      | Less than  |            |           | More than |
|--|------------|------------|------------|-----------|-----------|
|  |            | One year   | 1-3 years  | 3-5 years | 5 years   |
| Debt Obligations                           | \$ 481,742 | \$ 198,242 | \$ 218,000 | \$ 38,000 | \$ 27,500 |
| Commitments to Originate Loans             | \$ 62,060  | \$ 62,060  |            |           |           |
| Commitments to Fund Unused Lines of Credit | \$ 188,559 | \$ 188,559 |            |           |           |

Debt obligations include borrowings from the FHLB, Securities Sold under Agreements to Repurchase and other borrowings. The borrowings have defined terms and, under certain circumstances, \$40.0 million of the borrowings are callable at the option of the lender.

Commitments to originate loans and commitments to fund unused lines of credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since some of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company s exposure to credit risk is represented by the contractual amount of the instruments.

**Table of Contents****Non-Performing Assets**

The following table sets forth information regarding the Company's non-performing assets consisting of non-accrual loans and Real Estate Owned ( REO ). It is the policy of the Company to cease accruing interest on loans 90 days or more past due or in the process of foreclosure.

|  | September 30,<br>2007  | December 31,<br>2006 |
|--|------------------------|----------------------|
|  | (dollars in thousands) |                      |
| Non-accrual loans:   |                        |                      |
| Real estate One-to-four family                                     | \$ 6,144               | \$ 2,703             |
| Commercial Real Estate   | 1,739                  | 286                  |
| Consumer   | 414                    | 281                  |
| Commercial   | 865                    | 1,255                |
| Total non-performing loans   | 9,162                  | 4,525                |
| REO, net   | 433                    | 288                  |
| Total non-performing assets  | \$ 9,595               | \$ 4,813             |
| Allowance for loan losses as a percent of total loans receivable   | .63%                   | .57%                 |
| Allowance for loan losses as percent of total non-performing loans | 116.64                 | 226.25               |
| Non-performing loans as a percent of total loans receivable        | .54                    | .25                  |
| Non-performing assets as a percent of total assets                 | .50                    | .23                  |

The non-performing loan total includes \$887,000 of repurchased one-to-four family and consumer loans and \$3.3 million of one-to-four family and consumer loans previously held for sale, which were previously written down to their fair market value. The commercial real estate category includes an \$883,000 relationship for the construction of townhouses which has experienced sales delays. The Company also classifies assets in accordance with certain regulatory guidelines. At September 30, 2007 the Company had \$10.2 million designated as Special Mention, \$11.9 million classified as Substandard and \$105,000 classified as Doubtful as compared to \$18.2 million, \$8.2 million and \$185,000, respectively, designated as Special Mention and classified as Substandard and Doubtful at December 31, 2006. The largest Substandard relationship at September 30, 2007 is comprised of two loans totaling \$2.2 million for a start-up business for which operating revenue is not currently supporting the debt obligation. The loans are current as to payments. The largest Special Mention relationship at September 30, 2007 comprised several credit facilities to a large, real estate agency with an aggregate balance of \$4.4 million which was current as to payments, but criticized due to declining revenue and net income of the borrower. The loans are secured by commercial real estate and corporate assets and the personal guarantee of the principals. Included in the Substandard and Doubtful categories are all of the non-performing loans noted above.

**Private Securities Litigation Reform Act Safe Harbor Statement**

In addition to historical information, this quarterly report contains certain forward-looking statements which are based on certain assumptions and describe future plans, strategies and expectations of the Company. These forward-looking statements are generally identified by use of the words believe, expect, intend, anticipate, estimate, project, or similar expressions. The Company's ability to predict results or the actual future plans or strategies is inherently uncertain. Factors which could have a material adverse effect on the operations of the Company and the subsidiaries include, but are not limited to, changes in interest rates, general economic conditions, legislative/regulatory changes, monetary and fiscal policies of the U.S. Government, including policies of the U.S. Treasury and the Board of Governors of the Federal Reserve System, the quality or composition of the loan or investment portfolios, demand for loan products, deposit flows, competition, demand for financial services in the Company's market area and accounting principles and guidelines. These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on statements. The Company does not undertake - and specifically disclaims any obligation - to publicly release the result of any revisions which may be made to any forward-looking

**Table of Contents**

statements to reflect events or circumstances after the date of such statements or to reflect the occurrence of anticipated or unanticipated events. Further description of the risks and uncertainties to the business are included in Item 1, Business and Item 1A, Risk Factors of the Company's 2006 Form 10-K.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

The Company's interest rate sensitivity is monitored through the use of an interest rate risk ( IRR ) model. The following table sets forth the amounts of interest-earning assets and interest-bearing liabilities outstanding at September 30, 2007 which were anticipated by the Company, based upon certain assumptions, to reprice or mature in each of the future time periods shown. At September 30, 2007 the Company's one-year gap was negative 12.55% as compared to negative 0.80% at December 31, 2006.

| At June 30, 2007<br>(dollars in thousands)   | 3 Months<br>or Less | More than<br>3 Months<br>to<br>1 Year | More than<br>1 Year to<br>3 Years | More than<br>3 Years to<br>5 Years | More<br>than<br>5 Years | Total             |
|--|---------------------|---------------------------------------|-----------------------------------|------------------------------------|-------------------------|-------------------|
| <b>Interest-earning assets: (1)</b>  |                     |                                       |                                   |                                    |                         |                   |
| Interest-earning deposits and short-term investments                                     | \$ 2,942            | \$                                    | \$                                | \$                                 | \$                      | \$ 2,942          |
| Investment securities  | 54,953              | 295                                   |                                   |                                    | 7,333                   | 62,581            |
| FHLB stock   |                     |                                       |                                   |                                    | 22,040                  | 22,040            |
| Mortgage-backed securities   | 6,687               | 13,302                                | 26,471                            | 8,619                              | 3,217                   | 58,296            |
| Loans receivable (2)   | 253,724             | 330,642                               | 539,429                           | 272,709                            | 291,195                 | 1,687,699         |
| <b>Total interest-earning assets</b>   | <b>318,306</b>      | <b>344,239</b>                        | <b>565,900</b>                    | <b>281,328</b>                     | <b>323,785</b>          | <b>1,833,558</b>  |
| <b>Interest-bearing liabilities:</b>   |                     |                                       |                                   |                                    |                         |                   |
| Money market deposit accounts  | 3,936               | 11,808                                | 31,489                            | 39,209                             |                         | 86,442            |
| Savings accounts   | 10,670              | 26,172                                | 69,791                            | 87,239                             |                         | 193,872           |
| Interest-bearing checking accounts   | 155,432             | 40,965                                | 109,241                           | 136,557                            |                         | 442,195           |
| Time deposits  | 113,030             | 309,922                               | 41,270                            | 9,692                              | 1,030                   | 474,944           |
| FHLB advances  | 37,500              | 91,000                                | 205,000                           | 38,000                             |                         | 371,500           |
| Securities sold under agreements to repurchase   | 69,742              |                                       | 13,000                            |                                    |                         | 82,742            |
| Other borrowings   | 22,500              |                                       |                                   |                                    | 5,000                   | 27,500            |
| <b>Total interest-bearing liabilities</b>  | <b>412,810</b>      | <b>479,867</b>                        | <b>469,791</b>                    | <b>310,697</b>                     | <b>6,030</b>            | <b>1,679,195</b>  |
| <b>Interest sensitivity gap (3)</b>  | <b>\$ (94,504)</b>  | <b>\$ (135,628)</b>                   | <b>\$ 96,109</b>                  | <b>\$ (29,369)</b>                 | <b>\$ 317,755</b>       | <b>\$ 154,363</b> |
| <b>Cumulative interest sensitivity gap</b>   | <b>\$ (94,504)</b>  | <b>\$ (230,132)</b>                   | <b>\$ (134,023)</b>               | <b>\$ (163,392)</b>                | <b>\$ 154,363</b>       | <b>\$ 154,363</b> |
| <b>Cumulative interest sensitivity gap as a percent of total interest-earning assets</b> | <b>(5.15)%</b>      | <b>(12.55)%</b>                       | <b>(7.31)%</b>                    | <b>(8.91)%</b>                     | <b>8.42%</b>            | <b>8.42%</b>      |

- (1) Interest-earning assets are included in the period in which the balances are expected to be redeployed and/or repriced as a result of anticipated prepayments, scheduled rate adjustments, and contractual maturities.
  - (2) For purposes of the gap analysis, loans receivable includes loans held for sale and non-performing loans gross of the allowance for loan losses, unamortized discounts and deferred loan fees.
  - (3) Interest sensitivity gap represents the difference between interest-earning assets and interest-bearing liabilities.
- Additionally, the table below sets forth the Company's exposure to interest rate risk as measured by the change in net portfolio value ( NPV ) and net interest income under varying rate shocks as of September 30, 2007 and December 31, 2006. All methods used to measure interest rate

## Edgar Filing: OCEANFIRST FINANCIAL CORP - Form 10-Q

sensitivity involve the use of assumptions, which may tend to oversimplify the manner in which actual yields and costs respond to changes in market interest rates. The Company's interest rate sensitivity should be reviewed in conjunction with the financial statements and notes thereto contained in the Company's Annual Report for the year ended December 31, 2006.

| Change in Interest Rates in<br>Basis Points (Rate Shock)<br>(dollars in thousands) | September 30, 2007  |          |              |                     |          |  | December 31, 2006   |          |       |                     |          |
|--|---------------------|----------|--------------|---------------------|----------|--|---------------------|----------|-------|---------------------|----------|
|  | Net Portfolio Value |          |              | Net Interest Income |          |  | Net Portfolio Value |          | NPV   | Net Interest Income |          |
|  | Amount              | % Change | NPV<br>Ratio | Amount              | % Change |  | Amount              | % Change | Ratio | Amount              | % Change |
| 200  | \$ 129,056          | (26.3)%  | 7.1%         | \$ 49,849           | (8.4)%   |  | \$ 172,422          | (16.0)%  | 8.7%  | \$ 53,028           | (4.9)%   |
| 100  | 154,567             | (11.7)   | 8.2          | 52,443              | (3.6)    |  | 192,040             | (6.5)    | 9.5   | 54,748              | (1.9)    |
| Static   | 175,103             |          | 9.1          | 54,399              |          |  | 205,312             |          | 9.9   | 55,788              |          |
| (100)  | 183,784             | 5.0      | 9.4          | 55,110              | 1.3      |  | 206,157             | 0.4      | 9.8   | 55,431              | (0.6)    |
| (200)  | 175,944             | 0.5      | 9.0          | 53,240              | (2.1)    |  | 191,711             | (6.6)    | 9.1   | 52,490              | (5.9)    |

## **Table of Contents**

### **Item 4. Controls and Procedures**

The Company's management, including the Company's principal executive officer and principal financial officer, have evaluated the effectiveness of the Company's disclosure controls and procedures, as such term is defined in Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended, (the Exchange Act). Based upon their evaluation, the principal executive officer and principal financial officer concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures were effective. Disclosure controls and procedures are the controls and other procedures that are designed to ensure that the information required to be disclosed in the reports that the Company files or submits under the Exchange Act with the SEC (1) is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and (2) is accumulated and communicated to the Company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure.

At December 31, 2006, the Company's policies and procedures were not effective to provide for the proper evaluation and assessment of the adequacy of its reserve for repurchased loans at its mortgage banking subsidiary. Specifically, the Company lacked an effective process to ensure that the exercise of loan repurchase requests by purchasers of its loans were timely identified and incorporated properly in the analysis of its reserve for repurchased loans. This deficiency resulted in material misstatements in the Company's reserve for repurchased loans and amounts recorded as a gain on sales of loans at December 31, 2006 and resulted in more than a remote likelihood that a material misstatement of the Company's annual or interim consolidated financial statements would not be prevented or detected. These misstatements were corrected in the consolidated financial statements included in the December 31, 2006 Form 10-K.

During 2007, the Company implemented a remediation plan to address the material weakness in internal control over financial reporting which existed at December 31, 2006. To address the material weakness, during the first quarter of 2007, the Company enhanced its policies and procedures related to the quarterly evaluation of the adequacy of the reserve for repurchased loans. All repurchase requests received must be reported to a committee of senior officers of the Bank for evaluation and incorporation into the analysis of the reserve for repurchased loans. The Company proactively monitors the receipt of repurchase requests. Additionally, the Company's mortgage banking subsidiary modified its mortgage loan product menu to eliminate the origination of subprime loans. Furthermore, the Company has taken disciplinary action against certain officers of the mortgage banking subsidiary responsible for not following established policies and procedures. Finally, the Bank determined to discontinue most of the operations of Columbia while merging the remaining functions into the Bank's operations.

Except as described above, there were no changes in the Company's internal control over financial reporting during the quarter ended September 30, 2007 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## **PART II. OTHER INFORMATION**

### **Item 1. Legal Proceedings**

The Company is not engaged in any legal proceedings of a material nature at the present time. From time to time, the Company is a party to routine legal proceedings within the normal course of business. Such routine legal proceedings in the aggregate are believed by management to be immaterial to the Company's financial condition or results of operations.

### **Item 1A. Risk Factors**

No material change.

**Table of Contents****Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

Information regarding the Company's common stock repurchases for the three month period ended September 30, 2007 is as follows:

| Period                                       | Total Number of<br>Shares Purchased | Average price<br>Paid per Share | Total Number of<br>Shares Purchased as<br>Part of Publicly<br>Announced Plans or<br>Programs | Maximum Number of<br>Shares that May Yet<br>Be Purchased Under<br>the Plans or Programs |
|--|-------------------------------------|---------------------------------|--|---|
|  |                                     |                                 |  |   |
| July 1, 2007 through July 31, 2007           | 0                                   |                                 | 0  | 489,062   |
| August 1, 2007 through August 31, 2007       | 0                                   |                                 | 0  | 489,062   |
| September 1, 2007 through September 30, 2007 | 0                                   |                                 | 0  | 489,062   |

On July 19, 2006, the Company announced its intention to repurchase up to an additional 615,883 shares, or 5%, of its outstanding common stock.

**Item 3. Defaults Upon Senior Securities**

Not Applicable

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

Not Applicable

**Item 5. Other Information**

Not Applicable

**Item 6. Exhibits**

Exhibits:

- 3.1 Certificate of Incorporation of OceanFirst Financial Corp.\*
- 3.2 Bylaws of OceanFirst Financial Corp.\*\*
- 4.0 Stock Certificate of OceanFirst Financial Corp.\*
- 31.1 Rule 13a-14(a)/15d-14(c) Certification of Chief Executive Officer
- 31.2 Rule 13a-14(a)/15d-14(c) Certification of Chief Financial Officer
- 32.0 Section 1350 Certifications

\* Incorporated herein by reference into this document from the Exhibits to Form S-1, Registration Statement, effective May 13, 1996, as amended, Registration No. 33-80123.

Edgar Filing: OCEANFIRST FINANCIAL CORP - Form 10-Q

\*\* Incorporated herein by reference into this document from the Exhibit to Form 10-K, Annual Report, filed on March 25, 2003.

**Table of Contents**

**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.

OceanFirst Financial Corp.  
Registrant

DATE: November 8, 2007

/s/ John R. Garbarino  
John R. Garbarino  
Chairman of the Board, President

and Chief Executive Officer

DATE: November 8, 2007

/s/ Michael J. Fitzpatrick  
Michael J. Fitzpatrick  
Executive Vice President and

Chief Financial Officer

**Table of Contents**

Exhibit Index

| <b>Exhibit</b> | <b>Description</b>  | <b>Page</b> |
|----------------|---|-------------|
| 31.1           | Rule 13a-14(a)/15d-14(c) Certification of Chief Executive Officer | 21          |
| 31.2           | Rule 13a-14(a)/15d-14(c) Certification of Chief Financial Officer | 22          |
| 32.0           | Section 1350 Certifications                                       | 23          |