OCEANFIRST FINANCIAL CORP
Form 10-Q
November 10, 2008
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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, 2008

¨ **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	**22-3412577**
(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**Identification No.)**
975 Hooper Avenue, Toms River, NJ	**08754-2009**
(Address of principal executive offices)	**(Zip Code)**

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

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

Indicate 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 x Non-accelerated Filer ¨ Smaller Reporting Company ¨

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

As of November 5, 2008, there were 12,364,573 shares of the Registrant s Common Stock, par value $.01 per share, outstanding.

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OceanFirst Financial Corp.

Consolidated Statements of Financial Condition

(dollars in thousands, except per share amounts)

	September 30, 2008 (Unaudited)	December 31, 2007
ASSETS		
Cash and due from banks	$ 26,730	$ 27,547
Investment securities available for sale	45,309	57,625
Federal Home Loan Bank of New York stock, at cost	19,130	22,941
Mortgage-backed securities available for sale	43,487	54,137
Loans receivable, net	1,647,317	1,675,919
Mortgage loans held for sale	4,161	6,072
Interest and dividends receivable	6,896	6,915
Real estate owned, net	654	438
Premises and equipment, net	20,988	17,882
Servicing asset	7,658	8,940
Bank Owned Life Insurance	39,387	38,430
Other assets	14,541	10,653
Total assets	$ 1,876,258	$ 1,927,499
LIABILITIES AND STOCKHOLDERS EQUITY		
Deposits	$ 1,315,748	$ 1,283,790
Securities sold under agreements to repurchase with retail customers	67,682	69,807
Securities sold under agreements to repurchase with the Federal Home Loan Bank		12,000
Federal Home Loan Bank advances	323,500	393,000
Other borrowings	27,500	27,500
Advances by borrowers for taxes and insurance	8,088	7,588
Other liabilities	9,695	9,508
Total liabilities	1,752,213	1,803,193
Stockholders equity:		
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 12,364,573 and 12,346,465 shares outstanding at September 30, 2008 and December 31, 2007, respectively	272	272
Additional paid-in capital	204,040	203,532
Retained earnings	159,107	154,929
Accumulated other comprehensive loss	(8,710)	(3,211)
Less: Unallocated common stock held by Employee Stock Ownership Plan	(5,141)	(5,360)
Treasury stock, 14,812,799 and 14,830,907 shares at September 30, 2008 and December 31, 2007, respectively	(225,523)	(225,856)
Common stock acquired by Deferred Compensation Plan	982	1,307
Deferred Compensation Plan Liability	(982)	(1,307)
Total stockholders equity	124,045	124,306

Total liabilities and stockholders equity	$ 1,876,258	$ 1,927,499

See accompanying Notes to Unaudited Consolidated Financial Statements.

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OceanFirst Financial Corp.

Consolidated Statements of Operations

(in thousands, except per share amounts)

	For the three months ended September 30, 2008	2007	For the nine months ended September 30, 2008	2007
	(Unaudited)		(Unaudited)	
Interest income:				
Loans	$ 23,821	$ 25,945	$ 72,926	$ 79,528
Mortgage-backed securities	525	688	1,710	2,127
Investment securities and other	888	1,590	3,787	5,494
Total interest income	25,234	28,223	78,423	87,149
Interest expense:				
Deposits	6,256	9,326	20,827	27,778
Borrowed funds	4,348	6,066	14,469	19,431
Total interest expense	10,604	15,392	35,296	47,209
Net interest income	14,630	12,831	43,127	39,940
Provision for loan losses	400	75	1,175	525
Net interest income after provision for loan losses	14,230	12,756	41,952	39,415
Other income (loss):				
Loan servicing income	121	126	293	356
Fees and service charges	2,625	2,942	8,292	8,724
Net gain (loss) and lower of cost or market adjustment on sales of loans and securities available for sale	466	1,156	344	(11,676)
Net gain from other real estate operations	79	8	97	27
Income from Bank Owned Life Insurance	314	324	957	942
Other	2	6	13	41
Total other income (loss)	3,607	4,562	9,996	(1,586)
Operating expenses:				
Compensation and employee benefits	6,166	6,755	17,907	22,227
Occupancy	1,548	1,569	3,943	4,028
Equipment	468	543	1,433	1,631
Marketing	452	359	1,298	1,046
Federal deposit insurance	301	168	952	444
Data processing	779	859	2,375	2,625
General and administrative	2,549	2,357	7,357	8,430
Goodwill impairment				1,014
Total operating expenses	12,263	12,610	35,265	41,445
Income (loss) before provision (benefit) for income taxes	5,574	4,708	16,683	(3,616)
Provision (benefit) for income taxes	1,852	1,582	5,420	(1,597)

Net income (loss)	$ 3,722	$ 3,126	$ 11,263	$ (2,019)
Basic earnings (loss) per share	$ 0.32	$ 0.27	$ 0.97	$ (0.18)
Diluted earnings (loss) per share	$ 0.32	$ 0.27	$ 0.96	$ (0.18)
Average basic shares outstanding	11,678	11,561	11,661	11,522
Average diluted shares outstanding	11,751	11,643	11,722	11,522

See accompanying Notes to Unaudited Consolidated Financial Statements.

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OceanFirst Financial Corp.

Consolidated Statements of

Changes in Stockholders Equity (Unaudited)

(in thousands, except per share amounts)

	Common Stock	**Additional Paid-In Capital**	**Retained Earnings**	**Accumulated Other Comprehensive Loss**	**Employee Stock Ownership Plan**	**Treasury Stock**	**Common Stock Acquired by Deferred Compensation Plan**	**Deferred Compensation Plan Liability**	**Total**
Balance at December 31, 2006	$ 272	$ 201,936	$ 164,121	$ (470)	$ (6,369)	$ (227,170)	$ 1,457	$ (1,457)	$ 132,320
Comprehensive loss:									
Net loss			(2,019)						(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			(998)			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
Balance at December 31, 2007	$ 272	$ 203,532	$ 154,929	$ (3,211)	$ (5,360)	$ (225,856)	$ 1,307	$ (1,307)	$ 124,306

Comprehensive income:									
Net income			11,263						11,263
Other comprehensive loss:									
Unrealized loss on securities (net of tax benefit $3,277)				(6,085)					(6,085)
Reclassification adjustment for losses included in net income (net of tax benefit $316)				586					586
Total comprehensive income									5,764
Stock awards		431							431
Treasury stock allocated to restricted stock plan		(172)	(24)			196			
Allocation of ESOP stock					219				219
ESOP adjustment		249							249
Cash dividend - $.60 per share			(7,025)						(7,025)
Exercise of stock options			(36)			137			101
Sale of stock for the deferred compensation plan							(325)	325	
Balance at September 30, 2008	$ 272	$ 204,040	$ 159,107	$ (8,710)	$ (5,141)	$ (225,523)	$ 982	$ (982)	$ 124,045

See accompanying Notes to Unaudited Consolidated Financial Statements.

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OceanFirst Financial Corp.

Consolidated Statements of Cash Flows

(dollars in thousands)

	For the nine months ended September 30, 2008	2007
	(Unaudited)	
Cash flows from operating activities:		
Net income (loss)	$ 11,263	$ (2,019)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization of premises and equipment	1,276	1,486
Amortization of ESOP	219	757
ESOP adjustment	249	905
Stock award	431	354
Amortization of servicing asset	1,590	1,648
Amortization and impairment of intangible assets		1,091
Net premium amortization in excess of discount accretion on securities	32	81
Net amortization of deferred costs and discounts on loans	727	729
Provision for loan losses	1,175	525
Lower of cost or market write-down on loans held for sale		9,400
Net gain on sale of real estate owned	(164)	(11)
(Recovery) provision for repurchased loans	(211)	3,760
Net loss on write-off of fixed assets		21
Net gain on sales of loans and securities	(133)	(1,484)
Loans repurchased		(1,012)
Proceeds from sales of mortgage loans held for sale	79,220	352,373
Mortgage loans originated for sale	(76,582)	(281,342)
Increase in value of Bank Owned Life Insurance	(957)	(942)
Decrease (increase) in interest and dividends receivable	19	(274)
Increase in other assets	(929)	(1,862)
Increase (decrease) in other liabilities	1,405	(12,453)
Total adjustments	7,367	73,750
Net cash provided by operating activities	18,630	71,731
Cash flows from investing activities:		
Net decrease in loans receivable	25,520	15,880
Loans repurchased	(968)	(14,128)
Proceeds from sales of loans repurchased		8,666
Proceeds from maturities or calls of investment securities available for sale	300	20,780
Proceeds from sale of investment securities available for sale	3,122	
Purchases of investment securities available for sale	(937)	(681)
Principal payments on mortgage-backed securities available for sale	11,089	10,378
Decrease in Federal Home Loan Bank of New York stock	3,811	3,306
Proceeds from sales of real estate owned	1,089	638
Purchases of premises and equipment	(4,382)	(683)
Net cash provided by investing activities	38,644	44,156

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OceanFirst Financial Corp.

Consolidated Statements of Cash Flows (Continued)

(dollars in thousands)

	For the nine months ended September 30, 2008	2007
	(Unaudited)	
Cash flows from financing activities:		
Increase (decrease) in deposits	$ 31,958	$ (61,387)
(Decrease) increase in short-term borrowings	(37,625)	3,760
Repayments of securities sold under agreements to repurchase with the Federal Home Loan Bank	(12,000)	
Proceeds from Federal Home Loan Bank advances	57,000	20,000
Repayments of Federal Home Loan Bank advances	(91,000)	(85,000)
Proceeds from other borrowings		10,000
Increase in advances by borrowers for taxes and insurance	500	504
Exercise of stock options	101	1,047
Dividends paid	(7,025)	(6,784)
Purchase of treasury stock		(1,112)
Tax benefit of stock plans		337
Net cash used in financing activities	(58,091)	(118,635)
Net decrease in cash and due from banks	(817)	(2,748)
Cash and due from banks at beginning of period	27,547	32,204
Cash and due from banks at end of period	$ 26,730	$ 29,456
Supplemental Disclosure of Cash Flow Information:		
Cash paid during the period for:		
Interest	$ 35,718	$ 47,590
Income taxes	4,529	227
Non cash activities:		
Transfer of loans receivable to real estate owned	1,141	772
Transfer of securities sold under agreements to repurchase to advances		21,000

See accompanying Notes to Unaudited Consolidated Financial Statements.

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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. The operations of Columbia Home Loans, LLC (Columbia) were shuttered in late 2007.

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, 2008 are not necessarily indicative of the results of operations that may be expected for all of 2008.

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, 2007.

Earnings per Share

The following reconciles shares outstanding for basic and diluted earnings per share for the three and nine months ended September 30, 2008 and 2007 (in thousands):

	Three months ended September 30,		Nine months ended September 30,	
	2008	2007	2008	2007
Weighted average shares issued net of Treasury shares	12,365	12,329	12,359	12,317
Less: Unallocated ESOP shares	(614)	(681)	(623)	(710)
Unallocated incentive award shares and shares held by deferred compensation plan	(73)	(87)	(75)	(85)
Average basic shares outstanding	11,678	11,561	11,661	11,522
Add: Effect of dilutive securities:				
Stock options	27	15	12	
Incentive awards and shares held by deferred compensation plan	46	67	49	
Average diluted shares outstanding	11,751	11,643	11,722	11,522

For the three months ended September 30, 2008 and 2007, 1,200,000 and 1,408,000, respectively, antidilutive stock options were excluded from earnings per share calculations. For the nine months ended September 30, 2008 and 2007, 1,267,000 and 1,312,000, 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, 2008 and 2007, total comprehensive income, representing net income plus or minus the change in unrealized gains or losses on securities available for sale amounted to $1,685,000 and $1,224,000, respectively. For the nine month periods ended September 30, 2008 and 2007, total comprehensive income (loss) amounted to $5,764,000 and $(4,253,000), respectively.

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Note 2. Loans Receivable, Net

Loans receivable, net at September 30, 2008 and December 31, 2007 consisted of the following (in thousands):

	September 30, 2008	December 31, 2007
Real estate:		
One-to-four family	$ 1,052,411	$ 1,084,687
Commercial real estate, multi-family and land	328,711	326,707
Construction	7,889	10,816
Consumer	215,291	213,282
Commercial	55,982	54,279
Total loans	1,660,284	1,689,771
Loans in process	(2,795)	(2,452)
Deferred origination costs, net	5,207	5,140
Allowance for loan losses	(11,218)	(10,468)
Total loans, net	1,651,478	1,681,991
Less: Mortgage loans held for sale	4,161	6,072
Loans receivable, net	$ 1,647,317	$ 1,675,919

An analysis of the allowance for loan losses for the three and nine months ended September 30, 2008 and 2007 is as follows (in thousands):

	Three months ended September 30,		Nine months ended September 30,	
	2008	2007	2008	2007
Balance at beginning of period	$ 10,919	$ 10,619	$ 10,468	$ 10,238
Provision charged to operations	400	75	1,175	525
Charge-offs	(104)	(14)	(641)	(84)
Recoveries	3	7	216	8
Balance at end of period	$ 11,218	$ 10,687	$ 11,218	$ 10,687

Note 3. Reserve for Repurchased Loans

An analysis of the reserve for repurchased loans for the three and nine months ended September 30, 2008 and 2007 follows (in thousands). The reserve is included in other liabilities in the accompanying statements of financial condition.

	Three months ended September 30,		Nine months ended September 30,	
	2008	2007	2008	2007
Balance at beginning of period	$ 1,705	$ 5,397	$ 2,398	$ 9,600
(Recovery) provision charged to operations	(50)	(200)	(211)	3,760
Loss on loans repurchased	(475)	(2,444)	(1,007)	(10,607)
Balance at end of period	$ 1,180	$ 2,753	$ 1,180	$ 2,753

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 primarily included subprime loans with 100% financing and all other subprime loans and, to a lesser extent, ALT-A and prime loans. At September 30, 2008, there was one unresolved prime loan repurchase request outstanding which is subject to an arbitration proceeding.

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Note 4. Deposits

The major types of deposits at September 30, 2008 and December 31, 2007 were as follows (in thousands):

	September 30, 2008	December 31, 2007
Type of Account		
Non-interest-bearing	$ 111,604	$ 103,656
Interest-bearing checking	534,835	454,666
Money market deposit	83,563	84,287
Savings	205,636	187,095
Time deposits	380,110	454,086
	$ 1,315,748	$ 1,283,790

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 Company adopted the statement effective January 1, 2008. The adoption of SFAS No. 159 did not have a material impact on the Company s financial statements as the Company did not choose to measure any additional financial instruments or certain other items at fair value.

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 Company adopted the statement effective January 1, 2008. The adoption of SFAS No. 157 did not have a material impact on the Company s operations. In February 2008, Financial Accounting Standards Board Staff Position (FSP) No. 157-2, Effective Date of FASB Statement No. 157 was issued. FSP No. 157-2 delayed the application of SFAS No. 157 for non-financial assets and non-financial liabilities until January 1, 2009. In October 2008, FSP No. 157-3 Determining the Fair Value of a Financial Asset When the Market for that Asset Is Not Active was issued which clarifies the applications of SFAS No. 157 in a market that is not active.

In June 2007, the Emerging Issues Task Force (EITF) of the FASB issued EITF 06-11 which provides guidance on how an entity should recognize the income tax benefit received on dividends that are (a) paid to employees holding equity-classified nonvested shares, equity-classified nonvested share units, or equity-classified outstanding share options and (b) charged to retained earnings under SFAS No. 123(R). The Company adopted EITF 06-11 effective January 1, 2008. The adoption of EITF 06-11 did not have a material impact on the Company s financial statements.

In June 2008, EITF 03-6-1 was issued which addresses whether instruments granted in share-based payment transactions are participating securities prior to vesting and, therefore, need to be included in the earnings allocation in computing earnings per share. EITF 03-6-1 is effective for financial statements issued for fiscal years beginning after December 15, 2008. The adoption of EITF 03-6-1 is not expected to have a material impact on the Company s financial statements.

Note 6. Fair Value Measurements

SFAS No. 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. A fair market measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability or in the absence of a principal market, the most advantageous market for the asset or liability. The price in the principal (or the most advantageous) market used to measure the fair value of the asset or liability shall not be adjusted for transaction costs. An orderly transaction is a transaction that assumes

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exposure to the market for a period prior to the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets and liabilities; it is not a forced transaction. Market participants are buyers and sellers in the principal market that are (i) independent, (ii) knowledgeable, (iii) able to transact and (iv) willing to transact.

SFAS No. 157 requires the use of valuation techniques that are consistent with the market approach, the income approach and/or the cost approach. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets and liabilities. The income approach uses valuation techniques to convert future amounts, such as cash flows or earnings, to a single present amount on a discounted basis. The cost approach is based on the amount that currently would be required to replace the service capacity of an asset (replacement costs). Valuation techniques should be consistently applied. Inputs to valuation techniques refer to the assumptions that market participants would use in pricing the asset or liability. Inputs may be observable, meaning those that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from independent sources, or unobservable, meaning those that reflect the reporting entity s own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. In that regard, SFAS No. 157 establishes a fair value hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

Level 1 Inputs Unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.

Level 2 Inputs Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (for example, interest rates, volatilities, prepayment speeds, loss severities, credit risks and default rates) or inputs that are derived principally from or corroborated by observable market data by correlations or other means.

Level 3 Inputs Significant unobservable inputs that reflect an entity s own assumptions that market participants would use in pricing the assets or liabilities.

A description of the valuation methodologies used for assets and liabilities measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below.

In general, fair value is based upon quoted market prices, where available. If such quoted market prices are not available, fair value is based upon internally developed models that primarily use, as inputs, observable market-based parameters. Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. While management believes the Company s valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

Securities Available for Sale Securities classified as available for sale are reported at fair value utilizing Level 1 and Level 2 inputs. Most of the Company s investment and mortgage-backed securities are fixed income instruments that are not quoted on an exchange, but are bought and sold in active markets. Prices for these instruments are obtained through third party pricing vendors or security industry sources that actively participate in the buying and selling of securities. Prices obtained from these sources include market quotations and matrix pricing. Matrix pricing is a mathematical technique used principally to value certain securities without relying exclusively on quoted prices for the specific securities, but comparing the securities to benchmark or comparable securities.

The following table summarizes financial assets and financial liabilities measured at fair value on a recurring basis as of September 30, 2008, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value (dollars in thousands):

	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
Securities available for sale	$ 741	$ 88,055	$	$ 88,796

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Certain financial assets and financial liabilities are measured at fair value on a non-recurring basis, that is, the instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment). Financial assets and liabilities measured at fair value on a non-recurring basis were not significant as of September 30, 2008.

SFAS No. 157 will be applicable to certain non-financial assets and non-financial liabilities measured at fair value on a recurring and non-recurring basis, such as real estate owned, beginning January 1, 2009.

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, 2007 included in the Company s Annual Report on Form 10-K for the year ended December 31, 2007, 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.

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 2008, short-term interest rates declined and the interest rate yield curve steepened as compared to 2007. The changing interest rate environment has generally had a positive impact on the Bank s results of operations and net interest margin. Interest-earning assets, both loans and securities, are generally priced against longer-term indices, while interest-bearing liabilities, primarily deposits and borrowings, are generally priced against shorter-term indices. Also during 2008, there has been a general weakening of the overall economy coupled with continued concern surrounding the housing market. These conditions have had an adverse impact on the Bank s results of operations as non-performing loans and the provision for loan losses have increased.

The Company incurred a net loss for the nine months ended September 30, 2007 due to losses at Columbia, the Company s mortgage banking subsidiary, relating to the origination of subprime loans. In March 2007, Columbia discontinued the origination of all subprime loans and in September 2007, the Bank discontinued all loan origination activity at Columbia. At September 30, 2008, the Bank was still holding subprime loans with a gross principal balance of $5.6 million and a carrying value, net of reserves and lower of cost or market adjustment, of $3.5 million and ALT-A loans with a gross principal balance of $7.3 million and a carrying value, net of reserves and lower of cost or market adjustment, of $6.3 million.

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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, 2008 and 2007. 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 THREE MONTHS ENDED SEPTEMBER 30,					
	2008			2007		
	AVERAGE BALANCE	INTEREST	AVERAGE YIELD/ COST	AVERAGE BALANCE	INTEREST	AVERAGE YIELD/ COST
	(Dollars in thousands)					
Assets						
Interest-earning assets:						
Interest-earning deposits and short-term investments	$ 13,123	$ 43	1.31%	$ 17,191	$ 217	5.05%
Investment securities (1)	60,379	524	3.47	62,836	895	5.70
FHLB stock	19,019	321	6.75	22,432	478	8.52
Mortgage-backed securities (1)	44,984	525	4.67	60,539	688	4.55
Loans receivable, net (2)	1,636,707	23,821	5.82	1,696,679	25,945	6.12
Total interest-earning assets	1,774,212	25,234	5.69	1,859,677	28,223	6.07
Non-interest-earning assets	91,203			102,284		
Total assets	$ 1,865,415			$ 1,961,961		
Liabilities and Stockholders Equity						
Interest-bearing liabilities:						
Transaction deposits	$ 799,671	3,299	1.65	$ 727,233	3,837	2.11
Time deposits	392,893	2,957	3.01	488,688	5,489	4.49
Total	1,192,564	6,256	2.10	1,215,921	9,326	3.07
Borrowed funds	417,873	4,348	4.16	489,662	6,066	4.96
Total interest-bearing liabilities	1,610,437	10,604	2.63	1,705,583	15,392	3.61
Non-interest-bearing deposits	113,303			116,895		
Non-interest-bearing liabilities	18,050			16,834		
Total liabilities	1,741,790			1,839,312		
Stockholders equity	123,625			122,649		
Total liabilities and stockholders equity	$ 1,865,415			$ 1,961,961		
Net interest income		$ 14,630			$ 12,831	
Net interest rate spread (3)			3.06%			2.46%
Net interest margin (4)			3.30%			2.76%

	FOR THE NINE MONTHS ENDED SEPTEMBER 30,					
	2008			2007		
	AVERAGE BALANCE	INTEREST	AVERAGE YIELD/ COST	AVERAGE BALANCE	INTEREST	AVERAGE YIELD/ COST
	(Dollars in thousands)					
Assets						