KAMAN CORP
Form 10-Q
August 02, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 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 **June 29, 2007**

OR

o Transition Report Pursuant To Section 13 or 15(d) of the Securities Exchange Act of 1934 for the
Transition Period From ___ to ___

Commission File No. 0-1093

KAMAN CORPORATION

(Exact name of registrant as specified in its charter)

Connecticut (State or other jurisdiction of incorporation or organization)	06-0613548 (I.R.S. Employer Identification No.)

1332 Blue Hills Avenue
Bloomfield, Connecticut 06002
(Address of principal executive offices)

(860) 243-7100
Registrant's telephone number, including area code

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 [ ]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes [ ] No [X]

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of August 2, 2007:

Common Stock	24,519,521

Part I – Financial Information

Item 1. Financial Statements:

Condensed Consolidated Balance Sheets
(In thousands) (Unaudited)

	June 29, 2007		December 31, 2006	
Assets:				
Current assets:				
Cash and cash equivalents		$ 12,902		$ 12,720
Accounts receivable, net		216,684		189,328
Inventories		241,563		231,350
Income taxes receivable		2,056		-
Deferred income taxes		28,722		25,425
Other current assets		18,691		19,097
Total current assets		520,618		477,920
Property, plant & equip., at cost	174,365		168,875	
Less accumulated depreciation and amortization	119,062		114,710	
Net property, plant & equipment		55,303		54,165
Goodwill		58,095		56,833
Other intangible assets, net		19,108		19,264
Deferred income taxes		15,417		14,000
Other assets, net		9,964		8,231
Total assets		$ 678,505		$ 630,413
Liabilities and Shareholders' Equity:				
Current liabilities:				
Notes payable		$ 442		$ -
Current portion of long-term debt		523		1,551
Accounts payable - trade		98,253		95,059
Accrued salaries and wages		22,634		26,129
Accrued pension costs		8,725		2,965
Accrued contract losses		11,477		11,542
Advances on contracts		9,964		10,215
Other accruals and payables		39,619		42,661
Income taxes payable		-		8,215
Total current liabilities		191,637		198,337
Long-term debt, excl. current portion		107,135		72,872
Other long-term liabilities		61,199		62,643
Commitments and contingencies				

Shareholders' equity	318,534	296,561
Total liabilities and shareholders’ equity	$ 678,505	$ 630,413

See accompanying notes to condensed consolidated financial statements.

Condensed Consolidated Statements of Operations
(In thousands except per share amounts)
(Unaudited)

	For the Three Months Ended		For the Six Months Ended	
	June 29, 2007	June 30, 2006	June 29, 2007	June 30, 2006
Net sales	$ 319,953	$ 292,967	$ 637,271	$ 589,604
Costs and expenses:				
Cost of sales	231,774	212,462	459,963	427,754
Selling, general and administrative expense	71,472	67,008	143,571	137,082
Net gain on sale of assets	(56)	(43)	(14)	(56)
Other operating income	(724)	(452)	(1,256)	(823)
Interest expense, net	1,625	1,630	3,143	2,888
Other expense, net	260	303	218	563
	304,351	280,908	605,625	567,408
Earnings before income taxes	15,602	12,059	31,646	22,196
Income tax expense	(5,543)	(4,573)	(11,512)	(8,790)
Net earnings	10,059	7,486	20,134	13,406
Net earnings per share:				
Basic	0.41	0.31	0.83	0.56
Diluted	0.40	0.31	0.81	0.55
Average shares outstanding:				
Basic	24,285	24,031	24,213	23,984
Diluted	25,210	24,880	25,157	24,883
Dividends declared per share	$ 0.125	$ 0.125	$ 0.25	$ 0.25

See accompanying notes to condensed consolidated financial statements.

Condensed Consolidated Statements of Cash Flows
(In thousands except share and per share amounts) (Unaudited)

	For the Six Months Ended June 29, 2007	June 30, 2006
Cash flows from operating activities:		
Net earnings	$ 20,134	$ 13,406
Depreciation and amortization	5,718	5,165
Change in allowance for doubtful accounts	(688)	(219)
Net (gain) loss on sale of assets	(14)	(56)
Stock compensation expense	2,157	1,627
Deferred income taxes	(4,986)	2,423
Changes in assets and liabilities, excluding effects of acquisitions/divestitures:		
Accounts receivable	(26,025)	(23,623)
Inventories	(9,198)	(1,260)
Income taxes receivable	(2,056)	-
Other current assets	768	(448)
Accounts payable	8,612	(13,093)
Accrued contract losses	(65)	(6,217)
Advances on contracts	(251)	(3,857)
Accrued expenses and payables	(7,943)	(9,836)
Income taxes payable	(7,711)	(3,230)
Pension liabilities	2,432	4,913
Other long-term liabilities	3,565	187
Cash provided by (used in) operating activities	(15,551)	(34,118)
Cash flows from investing activities:		
Proceeds from sale of assets	194	461
Expenditures for property, plant & equipment	(6,799)	(5,046)
Acquisition of businesses including earn out adjustment	(1,793)	(362)
Other, net	(2,228)	(1,742)
Cash provided by (used in) investing activities	(10,626)	(6,689)
Cash flows from financing activities:		
Net borrowings (repayments) under revolving credit agreements	36,143	38,410
Debt repayment	(1,543)	(1,827)
Net change in book overdraft	(5,834)	7,820
Proceeds from exercise of employee stock plans	2,829	2,010
Dividends paid	(6,056)	(5,985)
Debt issuance costs	(150)	-
Windfall tax benefit	464	200
Other	96	151
Cash provided by (used in) financing activities	25,949	40,779
Net increase (decrease) in cash and cash equivalents	(228)	(28)
Effect of exchange rate changes on cash and cash equivalents	410	353

Cash and cash equivalents at beginning of period		12,720		12,998
Cash and cash equivalents at end of period	$	12,902	$	13,323

Supplemental Disclosure: Non-cash financing activity for the first half of 2007 and 2006 includes the conversion of 975 and 276 debentures with a total value of $975 and $276 into 41,731 and 11,801 shares of common stock, respectively, issued from treasury.

See accompanying notes to condensed consolidated financial statements.

Notes to Condensed Consolidated Financial Statements
(In thousands except share and per share amounts) (Unaudited)

1. Basis of Presentation

The December 31, 2006 condensed consolidated balance sheet amounts have been derived from the previously audited consolidated balance sheet of Kaman Corporation and subsidiaries. In the opinion of management, the balance of the condensed financial information reflects all adjustments which are necessary for a fair presentation of the company's financial position, results of operations and cash flows for the interim periods presented and are of a normal recurring nature, unless otherwise disclosed in this report. Certain amounts in the prior period condensed consolidated financial statements have been reclassified to conform to current year presentation. The statements should be read in conjunction with the consolidated financial statements and notes included in the company's Form 10-K (as amended) for the year ended December 31, 2006. The results of operations for the interim period presented are not necessarily indicative of trends or of results to be expected for the entire year.

The company has a calendar year-end; however, its first three fiscal quarters follow a 13-week convention, with each quarter ending on a Friday. The second quarter for 2007 and 2006 ended on June 29, 2007 and June 30, 2006, respectively.

Recently Issued Accounting Pronouncements
In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" (SFAS 159), including an amendment to Statement of Financial Accounting Standards No. 115. Under SFAS 159, entities may elect to measure specified financial instruments and warranty and insurance contracts at fair value on a contract-by-contract basis, with changes in fair value recognized in earnings each reporting period. The election, called the fair value option, will enable entities to achieve an offsetting accounting effect for changes in fair value of certain related assets and liabilities without having to apply complex hedge accounting provisions. SFAS 159 is effective as of the beginning of a company's first fiscal year that begins after November 15, 2007. The company is still in the process of evaluating the impact that adoption of SFAS 159 will have on our future consolidated financial statements.

On January 1, 2007, the company adopted FASB Interpretation No. 48 ("FIN 48"), "Accounting for Uncertainty in Income Taxes." The cumulative effect of the adoption of FIN 48 was a decrease of $415 in the liability for unrecognized tax benefits and a corresponding increase to retained earnings. The total liability for unrecognized tax benefits upon adoption was $5,118, including interest and penalties of $1,152. Included in unrecognized tax benefits upon adoption were items approximating $1,500 that, if recognized, would favorably affect the company's effective tax rate in future periods.

During the second quarter of 2007, the liability for unrecognized tax benefits was reduced by $373 to reflect payments in settlements with tax authorities, with no impact to the company's effective tax rate. The company does not anticipate that total unrecognized tax benefits will change significantly within the next twelve months. The company files tax returns in numerous U.S. and foreign jurisdictions, with returns subject to examination for varying periods, but generally back to and including 2003. It is the company's policy to record interest and penalties on unrecognized tax benefits as income taxes.

Cash Flow Items
Cash payments for interest were $3,141 and $2,886 for the six months ended June 29, 2007 and June 30, 2006, respectively. Cash payments for income taxes, net of refunds, for the comparable periods were $19,949 and $9,260, respectively.

Comprehensive Income

Comprehensive income was $22,670 and $13,913 for the six months ended June 29, 2007 and June 30, 2006, 2006, respectively. The changes to net earnings used to determine comprehensive income are comprised of foreign currency translation adjustments and net changes in pension and post-retirement benefit plan unrecognized gains and losses as a result of the adoption of SFAS No. 158, “Employers’ Accounting for Defined Benefit Pension and Other Postretirement Plans,” as of December 31, 2006.

Sale of Product Line Assets

The company has entered into an agreement with DSE, Inc., former owner of the Dayron operation, under which DSE will purchase the 40mm production line assets, including principally equipment and inventory. The sale price is approximately $4,500 plus the value of inventory and the transaction, which is subject to customary closing conditions, is expected to occur on or before December 31, 2007.

2. Accounts Receivable, net

Accounts receivable consist of the following:

		June 29, 2007		December 31, 2006
Trade receivables	$	105,564	$	97,752
U.S. Government contracts:				
Billed		38,010		26,938
Costs and accrued profit – not billed		6,814		4,544
Commercial and other government contracts:				
Billed		26,650		21,479
Costs and accrued profit – not billed		42,323		41,968
Less allowance for doubtful accounts		(2,677)		(3,353)
Total	$	216,684	$	189,328

Included in commercial and other government contracts – not billed as of December 31, 2006 was $41,295 related to the production contract for the Australian SH-2G(A) program for the Helicopters segment. Of this balance, $41,016 remained unbilled as of June 29, 2007. A total of $279 was billed during the first half of 2007 all of which has been collected to date. Based upon the terms of the existing contract, the company estimates that approximately $1,000 of the currently unbilled amount will be billed after June 29, 2008. If the company performs additional work scope for the customer pursuant to currently proposed terms of a potential contract modification, certain milestone billings permitted under the existing contract will be deferred and approximately $18,000 of the currently unbilled amount will be billed after June 29, 2008.

3. Inventories

Inventories consist of the following:

	June 29, 2007	December 31, 2006
Merchandise for resale	$ 133,909	$ 130,694
Contracts and other work in process	94,836	87,137
Finished goods (including certain general stock materials)	12,818	13,519
Total	$ 241,563	$ 231,350

4. Shareholders’ Equity

Changes in shareholders’ equity for the six months ended June 29, 2007 were as follows:

Balance, January 1, 2007	$ 296,561
Net earnings	20,134
Change in pension & post-retirement benefit plans, net	1,311
Foreign currency translation adjustment	1,225
Comprehensive income	22,670
Dividends declared	(6,091)
Employee stock plans and related tax benefit	4,004
Adoption of FIN 48 - adjustment to retained earnings	415
Debentures	975
Balance, June 29, 2007	$ 318,534

Shareholders’ equity consists of the following:

	June 29, 2007	December 31, 2006
Common stock	$ 24,565	$ 24,565
Additional paid in capital	62,084	60,631
Retained earnings	233,595	219,137
Other shareholders' equity	(1,710)	(7,772)
Total	$ 318,534	$ 296,561

5. Earnings Per Share

The following table presents a reconciliation of the numerators and denominators of basic and diluted earnings per share:

(In thousands except per share amounts)	For the Three Months Ended		For the Six Months Ended	
	June 29, 2007	June 30, 2006	June 29, 2007	June 30, 2006
Basic:				
Net earnings	$ 10,059	$ 7,486	$ 20,134	$ 13,406
Weighted average number of shares outstanding	24,285	24,031	24,213	23,984
Net earnings per share - basic	$ 0.41	$ 0.31	$ 0.83	$ 0.56
Diluted:				
Net earnings	$ 10,059	$ 7,486	$ 20,134	$ 13,406
Elimination of interest expense on 6% subordinated convertible debentures (net after taxes)	139	153	291	310
Net earnings (as adjusted)	$ 10,198	$ 7,639	$ 20,425	$ 13,716
Weighted average number of shares outstanding	24,285	24,031	24,213	23,984
Weighted averages shares issuable on conversion of 6% subordinated convertible debentures	627	706	657	736
Weighted average shares issuable on exercise of dilutive stock options	298	143	287	163
Total	25,210	24,880	25,157	24,883
Net earnings per share - diluted	$ 0.40	$ 0.31	$ 0.81	$ 0.55

There were no anti-dilutive shares options, based on average stock price, excluded from earnings per share diluted for any of the periods presented.

6. Exit Activity

The following table displays the activity and balances of various exit activities as of and for the six months ended June 29, 2007:

Balance at January 1, 2007	$	3,467
Additions to accrual		-
Cash payments		(712)
Release to income		-
Balance at June 29, 2007	$	2,755

In connection with the acquisition of Musicorp in August 2005, the company accrued $3,500 for certain exit costs. These costs relate primarily to lease consolidation and employee severance payments for reductions primarily in administrative and warehousing personnel. For the first half of 2007, the segment paid $578 in exit costs. The total Musicorp accrual as of June 29, 2007, was $191.

The accrual related to the Moosup, CT plant closure as of June 29, 2007 was $2,564, which consists primarily of the estimated cost of ongoing voluntary environmental investigating and remediation activities. During the six months ended June 29, 2007, the company paid $134 against this accrual for costs associated with environmental remediation activities for the facility. Ongoing maintenance costs of $205 for the six months ended June 29, 2007 related to this idle facility are included in selling, general and administrative expenses.

These exit activity accruals are included in other accruals and payables on the condensed consolidated balance sheets for the periods presented.

7. Product Warranty Costs

The following table presents the activity and balances of accrued product warranty costs included in other accruals and payables on the condensed consolidated balance sheets as of June 29, 2007:

Balance at January 1, 2007	$	2,028
Product warranty accrual		28
Warranty costs incurred		(255)
Release to income		(5)
Balance at June 29, 2007	$	1,796

The company continues to work to resolve two warranty-related matters that primarily impact our FMU-143 program at the Dayron facility, which is part of our Fuzing segment, that have been previously reported. The net reserve as of the end of the second quarter of 2007 related to these two matters was $873.

As previously disclosed, in March 2005 the U.S. Attorney's Office for the Middle District of Florida and the Defense Criminal Investigative Service (DCIS) initiated an investigation into the second warranty matter. Dayron has cooperated fully with the authorities, working to resolve the matter in a mutually satisfactory manner. As of the date of this report, the company has not received any notification from the authorities regarding final disposition of the investigation.

The company also has a warranty reserve for $677 for a matter related to our Aerostructures segment’s facility in Wichita, Kansas as previously reported. There has been no activity with respect to this matter during the six-month period ended June 29, 2007.

8. Accrued Contract Losses

The following is a summary of activity and balances of accrued contract losses as of and for the six months ended June 29, 2007:

Balance at January 1, 2007	$	11,542
Additions to loss accrual		6,155
Costs incurred		(6,092)
Release to income		(128)
Balance at June 29, 2007	$	11,477

During the second quarter of 2007, the company recorded an additional $2,383 pretax charge for the SH-2G(A) Helicopter Program for Australia based upon additional work that is necessary to complete the production portion of the program. This contract has been in a loss position since 2002. The remaining accrued contract loss for the Australia program as of June 29, 2007 was $10,563. This contract loss accrual continues to be monitored and adjusted as necessary to reflect the anticipated cost of the complex integration process and the results of the software testing.

9. Pension Cost

Components of net pension cost for the qualified pension plan and Supplemental Employees' Retirement Plan (SERP) are as follows:

	Qualified Pension Plan			
	For the Three Months Ended		For the Six Months Ended	
	June 29, 2007	June 30, 2006	June 29, 2007	June 30, 2006
Service cost for benefits earned	$ 3,330	$ 3,142	$ 6,659	$ 6,284
Interest cost on projected benefit obligation	6,930	6,603	13,861	13,206
Expected return on plan assets	(8,074)	(7,362)	(16,148)	(14,724)
Net amortization and deferral	226	752	451	1,504
Net pension cost	$ 2,412	$ 3,135	$ 4,823	$ 6,270

	SERP			
	For the Three Months Ended		For the Six Months Ended	
	June 29, 2007	June 30, 2006	June 29, 2007	June 30, 2006
Service cost for benefits earned	$ 116	$ 528	$ 232	$ 1,056
Interest cost on projected benefit obligation	505	432	1,010	864
Expected return on plan assets	-	-	-	-
Net amortization and deferral	882	389	1,765	778
Net pension cost	$ 1,503	$ 1,349	$ 3,007	$ 2,698

For the 2007 plan year, the company expects to contribute $10,000 to the qualified pension plan and $2,438 to the SERP. Through the first six months of 2007, the company has paid $2,500 and $446 with respect to the qualified pension plan and SERP, respectively, for the 2007 plan year.

10. <u>Business Segments</u>

Summarized financial information by business segment is as follows:

	For the Three Months Ended		For the Six Months Ended				
	June 29, 2007	June 30, 2006	June 29, 2007	June 30, 2006			
Net sales:							
Aerostructures	$ 23,322	$ 17,052	$ 48,501	$ 33,972			
Fuzing	23,962	14,634	42,462	33,676			
Helicopters	19,025	15,212	36,483	26,715			
Specialty Bearings	31,471	27,500	63,450	53,671			
Subtotal Aerospace Segments	97,780	74,398	190,896	148,034			
Industrial Distribution	174,602	170,476	348,016	341,053			
Music	47,571	48,093	98,359	100,517			
	$ 319,953	$ 292,967	$ 637,271	$ 589,604			
Operating income:							
Aerostructures	$ 3,680	$ 1,997	$ 8,231	$ 4,364			
Fuzing	4,015	1,484	6,545	4,427			
Helicopters	(244)	(1,164)	(1,269)	(3,226)			
Specialty Bearings	10,204	8,346	20,763	15,099			
Subtotal Aerospace Segments	17,655	10,663	34,270	20,664	863	$ 1,082	$ 16,317
Loans:							
Loans individually evaluated for impairment	$ 12,879	$ 21,165	$ 2,221	$ 714		$	$ 36,979
Loans collectively evaluated for impairment	772,562	628,786	197,128	83,232			1,681,708
Total ending loan balance	$ 785,441	$ 649,951	$ 199,349	$ 83,946		$	$ 1,718,687

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A summary of impaired loans at June 30, 2015 and December 31, 2014 is as follows (in thousands):

	June 30, 2015	December 31, 2014
Impaired loans with no allocated allowance for loan losses	$ 32,218	$ 26,487
Impaired loans with allocated allowance for loan losses	11,340	10,492
	$ 43,558	$ 36,979
Amount of the allowance for loan losses allocated	$ 2,106	$ 2,161

At June 30, 2015, impaired loans include troubled debt restructuring loans of $31,450,000 of which $27,618,000 were performing in accordance with their restructured terms for a minimum of six months and were accruing interest. At December 31, 2014, impaired loans include troubled debt restructuring loans of $23,493,000 of which $21,462,000 were performing in accordance with their restructured terms and were accruing interest.

The summary of loans individually evaluated for impairment by loan portfolio segment as of June 30, 2015 and December 31, 2014 and for the three months ended June 30, 2015 and 2014 follows (in thousands):

	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated
As of June 30, 2015			
With no related allowance recorded:			
Residential real estate	$ 13,094	$ 12,674	$
Commercial real estate	16,591	16,513	
Consumer	2,813	2,328	
Commercial and industrial	703	703	
	$ 33,201	$ 32,218	$
With an allowance recorded:			
Residential real estate	$ 295	$ 261	$ 65
Commercial real estate	10,592	10,532	1,721
Consumer			
Commercial and industrial	547	547	320
	$ 11,434	$ 11,340	$ 2,106
As of December 31, 2014			
With no related allowance recorded:			
Residential real estate	$ 12,351	$ 11,931	$

Commercial real estate	12,174	12,142	
Consumer	2,243	1,700	
Commercial and industrial	714	714	
	$ 27,482	$ 26,487	$
With an allowance recorded:			
Residential real estate	$ 948	$ 948	$ 88
Commercial real estate	9,023	9,023	1,741
Consumer	521	521	332
Commercial and industrial			
	$ 10,492	$ 10,492	$ 2,161

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	Three months ended June 30,			
	2015		2014	
	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:				
Residential real estate	$ 13,724	$ 144	$ 17,707	$ 169
Commercial real estate	15,182	97	8,046	20
Consumer	2,255	30	2,141	20
Commercial and industrial	707		276	3
	$ 31,868	$ 271	$ 28,170	$ 212
With an allowance recorded:				
Residential real estate	$ 263	$ 3	$ 1,259	$ 15
Commercial real estate	10,087	19	12,721	26
Consumer			685	11
Commercial and industrial	366	2		
	$ 10,716	$ 24	$ 14,665	$ 52

	Six months ended June 30,			
	2015		2014	
	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:				
Residential real estate	$ 12,775	$ 294	$ 17,608	$ 317
Commercial real estate	13,626	169	7,526	70
Consumer	2,201	59	2,161	41
Commercial and industrial	709		277	5
	$ 29,311	$ 522	$ 27,572	$ 433
With an allowance recorded:				
Residential real estate	$ 262	$ 6	$ 1,264	$ 31
Commercial real estate	10,008	42	12,888	63
Consumer			678	21
Commercial and industrial	183	2		
	$ 10,453	$ 50	$ 14,830	$ 115

The following table presents the recorded investment in non-accrual loans by loan portfolio segment as of June 30, 2015 and December 31, 2014 (in thousands):

	June 30, 2015	December 31, 2014
Residential real estate	$ 4,288	$ 3,115
Commercial real estate	14,601	12,758
Consumer	1,901	1,877
Commercial and industrial	115	557
	$ 20,905	$ 18,307

The following table presents the aging of the recorded investment in past due loans as of June 30, 2015 and December 31, 2014 by loan portfolio segment (in thousands):

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	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days Past Due	Total Past Due	Loans Not Past Due	Total
June 30, 2015						
Residential real estate	$ 4,797	$ 1,846	$ 3,204	$ 9,847	$ 790,543	$ 800,390
Commercial real estate	1,374		14,601	15,975	682,311	698,286
Consumer	263	323	1,608	2,194	190,157	192,351
Commercial and industrial			115	115	111,114	111,229
	$ 6,434	$ 2,169	$ 19,528	$ 28,131	$ 1,774,125	$ 1,802,256
December 31, 2014						
Residential real estate	$ 7,365	$ 1,695	$ 1,619	$ 10,679	$ 774,762	$ 785,441
Commercial real estate	119		12,758	12,877	637,074	649,951
Consumer	845	232	1,833	2,910	196,439	199,349
Commercial and industrial			557	557	83,389	83,946
	$ 8,329	$ 1,927	$ 16,767	$ 27,023	$ 1,691,664	$ 1,718,687

The Company categorizes all commercial and commercial real estate loans, except for small business loans, into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation and current economic trends, among other factors. This analysis is performed on a quarterly basis. The Company uses the following definitions for risk ratings:

Special Mention. Loans classified as Special Mention have a potential weakness that deserves management s close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the Bank s credit position at some future date.

Substandard. Loans classified as Substandard are inadequately protected by the current net worth and paying capacity of the borrower or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected.

Doubtful. Loans classified as Doubtful have all the weaknesses inherent in those classified as Substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable.

Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered to be Pass rated loans. As of June 30, 2015 and December 31, 2014, and based on the most recent analysis performed, the risk category of loans by loan portfolio segment is as follows (in thousands):

	Pass	Special Mention	Substandard	Doubtful	Total
June 30, 2015					

Commercial real estate	$ 650,776	$ 24,264	$ 23,246	$	$ 698,286
Commercial and industrial	106,551	1,867	2,811		111,229
	$ 757,327	$ 26,131	$ 26,057	$	$ 809,515
December 31, 2014					
Commercial real estate	$ 611,987	$ 12,684	$ 25,280	$	$ 649,951
Commercial and industrial	82,693	173	1,080		83,946
	$ 694,680	$ 12,857	$ 26,360	$	$ 733,897

For residential, consumer and small business loan classes, the Company evaluates credit quality based on the aging status of the loan, which was previously presented, and by payment activity. The following table presents the recorded investment in residential and consumer loans based on payment activity as of June 30, 2015 and December 31, 2014 (in thousands):

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	Residential Real Estate	
	Residential	Consumer
June 30, 2105		
Performing	$ 796,102	$ 190,450
Non-performing	4,288	1,901
	$ 800,390	$ 192,351
December 31, 2014		
Performing	$ 782,326	$ 197,472
Non-performing	3,115	1,877
	$ 785,441	$ 199,349

The Company classifies certain loans as troubled debt restructurings when credit terms to a borrower in financial difficulty are modified. The modifications may include a reduction in rate, an extension in term, the capitalization of past due amounts and/or the restructuring of scheduled principal payments. Included in the non-accrual loan total at June 30, 2015 and December 31, 2014 were $3,832,000 and $2,031,000, respectively, of troubled debt restructurings. At June 30, 2015 and December 31, 2014, the Company has allocated $482,000 and $419,000, respectively, of specific reserves to loans that are classified as troubled debt restructurings. Non-accrual loans which become troubled debt restructurings are generally returned to accrual status after six months of performance. In addition to the troubled debt restructurings included in non-accrual loans, the Company also has loans classified as troubled debt restructurings which are accruing at June 30, 2015 and December 31, 2014, which totaled $27,618,000 and $21,462,000, respectively. In the second quarter of 2015, the Bank restructured a commercial real estate loan with an outstanding balance of $3.9 million by extending the term and lowering the monthly repayment amount. The interest rate was unchanged. Troubled debt restructurings are considered in the allowance for loan losses similar to other impaired loans.

The following table presents information about troubled debt restructurings which occurred during the three and six months ended June 30, 2015 and 2014, and troubled debt restructurings modified within the previous year and which defaulted during the three and six months ended June 30, 2015 and 2014 (dollars in thousands):

	Number of Loans	Pre-modification Recorded Investment	Post-modification Recorded Investment
Three months ended June 30, 2015			
Troubled Debt Restructurings:			
Residential real estate	2	$ 268	$ 231
Commercial real estate	1	3,939	3,939
Consumer	4	259	243

	Number of Loans	Recorded Investment
Troubled Debt Restructurings		
Which Subsequently Defaulted:	None	None

	Number of Loans	Pre-modification Recorded Investment	Post-modification Recorded Investment
Six months ended June 30, 2015			
Troubled Debt Restructurings:			
Residential real estate	4	$ 517	$ 480
Commercial real estate	3	6,033	5,944
Consumer	8	395	379

	Number of Loans	Recorded Investment
Troubled Debt Restructurings Which Subsequently Defaulted:	None	None

	Number of Loans	Pre-modification Recorded Investment	Post-modification Recorded Investment
Three months ended June 30, 2014			
Troubled Debt Restructurings:			
Residential real estate	1	$ 358	$ 358
Consumer	3	93	97

	Number of Loans	Recorded Investment
Troubled Debt Restructurings Which Subsequently Defaulted:	None	None

	Number of Loans	Pre-modification Recorded Investment	Post-modification Recorded Investment
Six months ended June 30, 2014			
Troubled Debt Restructurings:			
Residential real estate	4	$ 882	$ 805
Consumer	5	168	171

	Number of Loans	Recorded Investment
Troubled Debt Restructurings		
Which Subsequently Defaulted:	None	None

Note 5. Reserve for Repurchased Loans and Loss Sharing Obligations

The reserve for repurchased loans and loss sharing obligations was $1.0 million at June 30, 2015, unchanged from December 31, 2014 and was $1.3 million at June 30, 2014 a decrease of $163,000 from December 31, 2013 due to realized losses. The reserve for repurchased loans and loss sharing obligations was established to provide for expected losses related to repurchase requests which may be received on residential mortgage loans previously sold to investors and other loss sharing obligations. The reserve is included in other liabilities in the accompanying statements of financial condition.

At June 30, 2015, and December 31, 2014, there were no outstanding loan repurchase requests.

Note 6. Deposits

The major types of deposits at June 30, 2015 and December 31, 2014 were as follows (in thousands):

Type of Account	June 30, 2015	December 31, 2014
Non-interest-bearing	$ 328,175	$ 279,944
Interest-bearing checking	794,310	836,120
Money market deposit	123,017	95,663
Savings	306,079	301,190
Time deposits	210,094	207,218
Total deposits	$ 1,761,675	$ 1,720,135

Included in time deposits at June 30, 2015 and December 31, 2014, is $73,900,000 and $64,416,000, respectively, in deposits of $100,000 and over.

Note 7. Recent Accounting Pronouncements

In January 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-04, Receivables Troubled Debt Restructurings by Creditors (Subtopic 310-40) Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure, which applies to all creditors who obtain physical possession of residential real estate property collateralizing a consumer mortgage loan in satisfaction of a receivable. The amendments in this update clarify when an in-substance repossession or foreclosure occurs and requires disclosure of both (1) the amount of foreclosed residential real estate property held by a creditor and (2) the recorded investment in consumer mortgage loans collateralized by residential real estate property that are in the process of foreclosure. The amendments in ASU 2014-04 are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2014. The adoption of this standard in the first quarter of 2015 did not to have a material impact on the Company s consolidated financial statements.

Note 8. Fair Value Measurements

Fair value is defined 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 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.

The Company uses 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 and 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 and developed based on the best information available in the circumstances. In that regard, a fair value hierarchy has been established for valuation inputs that give the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. Movements within the fair value hierarchy are recognized at the end of the applicable reporting period. There were no transfers between the levels of the fair value hierarchy for the three and six months ended June 30, 2015. 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.

Assets and Liabilities Measured at Fair Value

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. 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).

Securities Available-For-Sale

Securities classified as available-for-sale are reported at fair value utilizing Level 1 and Level 2 inputs. In general, fair value is based upon quoted market prices, where available. Most of the Company s investment and mortgage-backed securities, however, 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.

Fair value estimates are made at a point in time, based on relevant market data as well as the best information available about the security. Illiquid credit markets have resulted in inactive markets for certain of the Company s securities. As a result, there is limited observable market data for these assets. Fair value estimates for securities for which limited observable market data is available are based on judgments regarding current economic conditions, liquidity discounts, credit and interest rate risks, and other factors. These estimates involve significant uncertainties and judgments and cannot be determined with precision. As a result, such calculated fair value estimates may not be realizable in a current sale or immediate settlement of the security.

The Company utilizes third party pricing services to obtain fair values for its corporate bonds. Management s policy is to obtain and review all available documentation from the third party pricing service relating to their fair value determinations, including their methodology and summary of inputs. Management reviews this documentation, makes inquiries of the third party pricing service and makes a determination as to the level of the valuation inputs. Based on the Company s review of the available documentation from the third party pricing service, management concluded that Level 2 inputs were utilized. The significant observable inputs include benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, other market information and observations of equity and credit default swap curves related to the issuer.

Other Real Estate Owned and Impaired Loans

Other real estate owned and loans measured for impairment based on the fair value of the underlying collateral are recorded at estimated fair value, less estimated selling costs. Fair value is based on independent appraisals.

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The following table summarizes financial assets and financial liabilities measured at fair value as of June 30, 2015 and December 31, 2014, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value (in thousands):

June 30, 2015	Total Fair Value	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs
		Fair Value Measurements at Reporting Date Using:		
Items measured on a recurring basis:				
Investment securities available-for-sale:				
U.S. agency obligations	$ 30,030	$	$ 30,030	$
Items measured on a non-recurring basis:				
Other real estate owned	3,357			3,357
Loans measured for impairment based on the fair value of the underlying collateral	13,093			13,093

December 31, 2014	Total Fair Value	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs
		Fair Value Measurements at Reporting Date Using:		
Items measured on a recurring basis:				
Investment securities available-for-sale:				
U.S. agency obligations	$ 19,804	$	$ 19,804	$
Items measured on a non-recurring basis:				
Other real estate owned	4,664			4,664
Loans measured for impairment based on the fair value of the underlying collateral	11,675			11,675

Assets and Liabilities Disclosed at Fair Value

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

Cash and Due from Banks

For cash and due from banks, the carrying amount approximates fair value.

Securities Held-to-Maturity

Securities classified as held-to-maturity are carried at amortized cost, as the Company has the positive intent and ability to hold these securities to maturity. The Company determines the fair value of the securities utilizing Level 1, Level 2 and infrequently Level 3 inputs. In general, fair value is based upon quoted market prices, where available. Most of the Company s investment and mortgage-backed securities, however, 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.

Fair value estimates are made at a point in time, based on relevant market data as well as the best information available about the security. Illiquid credit markets have resulted in inactive markets for certain of the Company s securities. As a result, there is limited observable market data for these assets. Fair value estimates for securities for which limited observable market data is available are based on judgments regarding current economic conditions, liquidity discounts, credit and interest rate risks, and other factors. These estimates involve significant uncertainties and judgments and cannot be determined with precision. As a result, such calculated fair value estimates may not be realizable in a current sale or immediate settlement of the security.

The Company utilizes third party pricing services to obtain fair values for its corporate debt securities. Management s policy is to obtain and review all available documentation from the third party pricing service relating to their fair value determinations, including their methodology and summary of inputs. Management reviews this documentation, makes inquiries of the third party pricing service and makes a determination as to the level of the valuation inputs. Based on the Company s review of the available documentation from the third party pricing service, management concluded that Level 2 inputs were utilized for all securities except for certain state and municipal obligations known as bond anticipation notes (BANs) where management utilized Level 3 inputs. In the case of the Level 2 securities, the significant observable inputs include benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, other market information and observations of equity and credit default swap curves related to the issuer. Management based its fair value estimate of the BANs on the local nature of the issuing entities, the short-term life of the security and current market conditions.

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Federal Home Loan Bank of New York Stock

The fair value for Federal Home Loan Bank of New York stock is its carrying value since this is the amount for which it could be redeemed. There is no active market for this stock and the Company is required to maintain a minimum investment based upon the outstanding balance of mortgage related assets and outstanding borrowings.

Loans

Fair values are estimated for portfolios of loans with similar financial characteristics. Loans are segregated by type such as residential mortgage, construction, consumer and commercial. Each loan category is further segmented into fixed and adjustable rate interest terms.

Fair value of performing and non-performing loans was estimated by discounting the future cash flows, net of estimated prepayments, at a rate for which similar loans would be originated to new borrowers with similar terms. Fair values estimated in this manner do not fully incorporate an exit price approach to fair value, but instead are based on a comparison to current market rates for comparable loans.

Deposits Other than Time Deposits

The fair value of deposits with no stated maturity, such as non-interest-bearing demand deposits, savings, and interest-bearing checking accounts and money market accounts are, by definition, equal to the amount payable on demand. The related insensitivity of the majority of these deposits to interest rate changes creates a significant inherent value which is not reflected in the fair value reported.

Time Deposits

The fair value of time deposits is based on the discounted value of contractual cash flows. The discount rate is estimated using the rates currently offered for deposits of similar remaining maturities.

Securities Sold Under Agreements to Repurchase with Retail Customers

Fair value approximates the carrying amount as these borrowings are payable on demand and the interest rate adjusts monthly.

Borrowed Funds

Fair value estimates are based on discounting contractual cash flows using rates which approximate the rates offered for borrowings of similar remaining maturities.

The book value and estimated fair value of the Bank s significant financial instruments not recorded at fair value as of June 30, 2015 and December 31, 2014 are presented in the following tables (in thousands):

		Fair Value Measurements at Reporting Date Using:		
	Book	Level 1	Level 2	Level 3
June 30, 2105	Value	Inputs	Inputs	Inputs
Financial Assets:				

Cash and due from banks	$ 40,359	$ 40,359	$	$
Securities held-to-maturity	414,625		420,409	
Federal Home Loan Bank of New York stock	18,740			18,740
Loans receivable and mortgage loans held for sale	1,774,333			1,785,437
Financial Liabilities:				
Deposits other than time deposits	1,551,581		1,551,581	
Time deposits	210,094		211,369	
Securities sold under agreements to repurchase with retail customers	71,687	71,687		
Federal Home Loan Bank advances and other borrowings	323,116		323,536	

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		Fair Value Measurements at Reporting Date Using:		
December 31, 2014	Book Value	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs
Financial Assets:				
Cash and due from banks	$ 36,117	$ 36,117	$	$
Securities held-to-maturity	469,417		474,215	
Federal Home Loan Bank of New York stock	19,170			19,170
Loans receivable and mortgage loans held for sale	1,693,047			1,709,819
Financial Liabilities:				
Deposits other than time deposits	1,512,917		1,512,917	
Time deposits	207,218		208,651	
Securities sold under agreements to repurchase with retail customers	67,812	67,812		
Federal Home Loan Bank advances and other borrowings	332,738		332,432	

Limitations

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company s entire holdings of a particular financial instrument. Because a limited market exists for a significant portion of the Company s financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments and other significant unobservable inputs. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and, therefore, cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Fair value estimates are based on existing balance sheet financial instruments without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. Significant assets and liabilities that are not considered financial assets or liabilities include deferred tax assets, and premises and equipment. In addition, the tax ramifications related to the realization of the unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in the estimates.

Note 9. Subsequent Events

On July 31, 2015 the Company closed on the acquisition of Colonial American Bank (Colonial) headquartered in Middletown, New Jersey, in an all stock transaction valued at approximately $11.9 million. Each outstanding share of Colonial common stock and preferred stock was exchanged for 0.3658 shares of the Company s common stock for a total issuance of 660,098 shares.

Colonial operates two full service banking offices in Middletown and Shrewsbury, New Jersey with total assets of $143.2 million, including $125.8 million in total loans and $127.5 million in total deposits as of June 30, 2015. The combined institution will have 26 offices serving the central New Jersey market.

Additionally, on July 31, 2015, the Bank executed an agreement to purchase an existing retail branch with total deposits of $24.6 million and core deposits of $20.2 million located in the Toms River market.

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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

For a summary of risk factors relevant to the Company, see Part I, Item 1A, Risk Factors, in the 2014 Form 10-K. There were no material changes to risk factors relevant to the Company s operations since December 31, 2014.

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

On July 24, 2014, the Company announced the authorization of the Board of Directors to repurchase up to 5% of the Company s outstanding common stock, or 867,923 shares. Information regarding the Company s common stock repurchases for the three month period ended June 30, 2015 is as follows:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
April 1 through April 30, 2015	0	$ 0	0	0
May 1, 2015 through May 31, 2015	104,317	17.10	104,317	403,938
June 1, 2015 through June 30, 2015	45,480	17.30	45,480	358,458

Item 3. Defaults Upon Senior Securities

Not Applicable

Item 4. Mine Safety Disclosures

Not Applicable

Item 5. Other Information

Not Applicable

Item 6. Exhibits

Exhibits:

31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.0	Certification pursuant to 18 U.S.C. Section 1350 as added by Section 906 of the Sarbanes-Oxley Act of 2002
101.0	The following materials from the Company s Quarterly Report on Form 10-Q for the quarter ended June 30, 2015, formatted in XBRL (Extensible Business Reporting Language): (i) the Consolidated Statements of Financial Condition, (ii) the Consolidated Statements of Income, (iii) the Consolidated Statements of Comprehensive Income, (iv) the Consolidated Statements of Changes in Stockholders Equity, (v) the Consolidated Statements of Cash Flows and (vi) the Notes to Consolidated Financial Statements.

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SIGNATURES

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

	OceanFirst Financial Corp. Registrant
DATE: August 7, 2015	/s/ Christopher D. Maher Christopher D. Maher President and Chief Executive Officer
DATE: August 7, 2015	/s/ Michael J. Fitzpatrick Michael J. Fitzpatrick Executive Vice President and Chief Financial Officer

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