Oconee Federal Financial Corp.
Form 10-Q
November 14, 2013
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the Quarterly Period ended September 30, 2013

Or

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

For transition period from to

Commission File Number 001-35033

Oconee Federal Financial Corp.

(Exact Name of Registrant as Specified in Charter)

Federal	**32-0330122**
(State of Other Jurisdiction	(I.R.S Employer
of Incorporation)	Identification Number)
201 East North Second Street, Seneca, South Carolina	**29678**
(Address of Principal Executive Officers)	(Zip Code)

(864) 882-2765

Registrant s telephone number, including area code

Not Applicable

(Former name or former address, if changed since last report)

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 o.

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer, or a smaller reporting company. See definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o	Accelerated filer o
Non-accelerated filer o	Smaller reporting company x

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

Indicate the number of shares outstanding of each of the Issuer s classes of common stock as of the latest practicable date.

There were 5,833,395 shares of Common Stock, par value $.01 per share, outstanding as of November 1, 2013.

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OCONEE FEDERAL FINANCIAL CORP.

CONSOLIDATED BALANCE SHEETS

(Amounts in thousands, except share and per share data)

OCONEE FEDERAL FINANCIAL CORP.

Form 10-Q Quarterly Report

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OCONEE FEDERAL FINANCIAL CORP.

CONSOLIDATED BALANCE SHEETS

(Amounts in thousands, except share and per share data)

PART I

ITEM 1. FINANCIAL STATEMENTS

	September 30, 2013 (Unaudited)	June 30, 2013 (*)
ASSETS		
Cash and due from banks	$ 1,594	$ 1,362
Interest-bearing deposits	27,896	36,580
Total cash and cash equivalents	29,490	37,942
Securities held-to-maturity (fair value: September 30, 2013 - $8,890 and June 30, 2013 - $8,223)	8,726	8,039
Securities available-for-sale	90,891	87,985
Loans, net of allowance for loan losses of $832 and $751	221,858	221,163
Premises and equipment, net	3,015	3,047
Real estate owned, net	857	1,047
Accrued interest receivable		
Loans	808	863
Investments	401	269
Restricted equity securities	449	449
Bank owned life insurance	8,526	8,450
Other assets	867	841
Total assets	$ 365,888	$ 370,095
LIABILITIES		
Deposits		
Non-interest bearing	$ 4,791	$ 4,861
Interest bearing	283,986	287,561
Total deposits	288,777	292,422
Accrued interest payable and other liabilities	1,920	1,511
Total liabilities	290,697	293,933
SHAREHOLDERS EQUITY		
Common stock, $0.01 par value, 100,000,000 shares authorized; 5,833,395 and 5,923,295 shares outstanding at September 30, 2013 and June 30, 2013	64	64
Treasury stock, at par 601,699 and 511,799 shares at September 30, 2013 and June 30, 2013	(6)	(5)
Additional paid in capital	12,068	13,413
Retained earnings	65,650	65,315

Accumulated other comprehensive loss		(565)		(559)
Unearned ESOP shares		(2,020)		(2,066)
Total shareholders equity		75,191		76,162
Total liabilities and shareholders equity	$	365,888	$	370,095

*Derived from audited consolidated financial statements.

See accompanying notes to the consolidated financial statements

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OCONEE FEDERAL FINANCIAL CORP.

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

(Unaudited)

(Amounts in thousands, except share and per share data)

	Three Months Ended September 30, 2013	Three Months Ended September 30, 2012
Interest and dividend income:		
Loans, including fees	$ 2,852	$ 3,370
Securities, taxable	371	266
Federal funds sold and other	15	18
Total interest income	3,238	3,654
Interest expense:		
Deposits	429	625
Total interest expense	429	625
Net interest income	2,809	3,029
Provision for loan losses	81	141
Net interest income after provision for loan losses	2,728	2,888
Noninterest income:		
Service charges on deposit accounts	18	20
Gain (loss) on sales of real estate owned	(14)	57
Other	76	9
Total noninterest income	80	86
Noninterest expense:		
Salaries and employee benefits	861	790
Occupancy and equipment	155	177
Data processing	63	59
Professional and supervisory fees	112	79
Office expense	15	23
Advertising	21	19
FDIC deposit insurance	40	27
Provision for real estate owned and related expenses	32	37
Other	77	76
Total noninterest expense	1,376	1,287
Income before income taxes	1,432	1,687
Income tax expense	513	670
Net income	$ 919	$ 1,017
Other comprehensive income (loss)		
Unrealized (loss) gain on securities available-for-sale	$ (9)	$ 618
Tax effect	3	(235)

Total other comprehensive income (loss)		(6)		383
Comprehensive income	$	913	$	1,400
Basic net income per share: (Note 2)	$	0.16	$	0.16
Diluted net income per share: (Note 2)	$	0.16	$	0.16
Dividends declared per share:	$	0.10	$	0.10

See accompanying notes to the consolidated financial statements

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OCONEE FEDERAL FINANCIAL CORP.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY

(Unaudited)

(Amounts in thousands, except share and per share data)

	Common Stock	Treasury Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Unearned ESOP Shares	Total
Balance at July 1, 2012	$ 64	$	$ 20,880	$ 63,693	$ 599	$ (2,252)	$ 82,984
Net income				1,017			1,017
Other comprehensive income					383		383
Stock-based compensation expense			58				58
Dividends				(643)			(643)
ESOP shares earned			9			39	48
Balance at September 30, 2012	$ 64	$	$ 20,947	$ 64,067	$ 982	$ (2,213)	$ 83,847
Balance at July 1, 2013	$ 64	$ (5)	$ 13,413	$ 65,315	$ (559)	$ (2,066)	$ 76,162
Net income				919			919
Other comprehensive loss					(6)		(6)
Purchase of 89,900 shares of treasury stock (1)		(1)	(1,423)				(1,424)
Stock-based compensation expense			57				57
Dividends (2)				(584)			(584)
ESOP shares earned			21			46	67
Balance at September 30, 2013	$ 64	$ (6)	$ 12,068	$ 65,650	$ (565)	$ (2,020)	$ 75,191

(1) The weighted average cost of treasury shares purchased during the three months ended was $15.85 per share. Treasury stock repurchases were accounted for using the par value method.

(2) Cash dividends declared on July 25, 2013 were paid on August 15, 2013.

See accompanying notes to the consolidated financial statements

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OCONEE FEDERAL FINANCIAL CORP.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(Amounts in thousands, except share and per share data)

	Three Months Ended September 30, 2013	Three Months Ended September 30, 2012
Cash Flows From Operating Activities		
Net income	$ 919	$ 1,017
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	81	141
Depreciation and amortization, net	252	276
Deferred loan fees, net	6	70
(Gain) loss on sale of real estate owned	14	(57)
Increase in cash surrender value of bank owned life insurance	(76)	
ESOP compensation expense	67	48
Stock based compensation expense	57	58
Net change in operating assets and liabilities:		
Accrued interest receivable	(77)	(83)
Accrued interest payable	(1)	5
Other	387	689
Net cash provided by operating activities	1,629	2,164
Cash Flows From Investing Activities		
Purchases of premises and equipment	(19)	(31)
Purchases of securities held-to-maturity	(1,494)	(498)
Purchases of securities available-for-sale	(5,324)	(8,347)
Proceeds from maturities, paydowns and calls of securities available-for-sale	2,218	2,746
Proceeds from maturities, paydowns and calls of securities held-to-maturity	797	830
Proceeds from sale of real estate owned	176	674
Loan originations and repayments, net	(782)	5,287
Net cash provided by (used in) investing activities	(4,428)	661
Cash Flows from Financing Activities		
Net change in deposits	(3,638)	144
Dividends paid	(584)	(643)
Purchase of treasury stock	(1,431)	
Net cash used in financing activities	(5,653)	(499)
Change in cash and cash equivalents	(8,452)	2,326
Cash and cash equivalents, beginning of year	37,942	47,612
Cash and cash equivalents, end of period	$ 29,490	$ 49,938

See accompanying notes to the consolidated financial statements

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OCONEE FEDERAL FINANCIAL CORP.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(Amounts in thousands, except share and per share data)

(1) BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements of Oconee Federal Financial Corp., which include the accounts of its wholly owned subsidiary Oconee Federal Savings and Loan Association (the Association) (referred to herein as the Company, we, us, or our) have b prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. Intercompany accounts and transactions are eliminated during consolidation. The Company is majority owned (70.76%) by Oconee Federal, MHC. These financial statements do not include the transactions and balances of Oconee Federal, MHC.

In the opinion of management, the accompanying unaudited consolidated financial statements contain all adjustments (consisting only of normal recurring accruals) necessary to present fairly the Company s financial position as of September 30, 2013 and June 30, 2013 and the results of operations and cash flows for the interim periods ended September 30, 2013 and 2012. All interim amounts have not been audited, and the results of operations for the interim periods herein are not necessarily indicative of the results of operations to be expected for the year. These consolidated financial statements should be read in conjunction with the Company s audited consolidated financial statements and notes thereto included in the Form 10-K Annual Report of Oconee Federal Financial Corp. for the year ended June 30, 2013.

(2) EARNINGS PER SHARE (EPS)

Basic EPS is determined by dividing net earnings available to common shareholders by the weighted average number of common shares outstanding for the period. ESOP shares are considered outstanding for this calculation unless unearned. The factors used in the earnings per common share computation follow:

	Three Months Ended	
	September 30, 2013	**September 30, 2012**
Earnings per share		
Net income	$ 919	$ 1,017
Less: distributed earnings allocated to participating securities	(7)	(8)
Less: (undistributed income) dividends in excess of earnings allocated to participating securities	(4)	(5)
Net earnings available to common shareholders	$ 908	$ 1,004

Weighted average common shares outstanding including participating securities		5,850,522		6,423,645
Less: participating securities		(71,095)		(87,092)
Less: average unearned ESOP shares		(204,302)		(222,912)
Weighted average common shares outstanding		5,575,125		6,113,641
Basic earnings per share	$	0.16	$	0.16
Weighted average common shares outstanding		5,575,125		6,113,641
Add: dilutive effects of assumed exercises of stock options		47,856		7,522
Average shares and dilutive potential common shares		5,622,981		6,121,163
Diluted earnings per share	$	0.16	$	0.16

During the three months ended September 30, 2013 and 2012, there were no potential anti-dilutive common shares.

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OCONEE FEDERAL FINANCIAL CORP.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(Amounts in thousands, except share and per share data)

(3) SECURITIES AVAILABLE-FOR-SALE AND HELD-TO-MATURITY

Debt, mortgage-backed and equity securities have been classified in the consolidated balance sheets according to management s intent. Investment securities at September 30, 2013 and June 30, 2013 are as follows:

		Amortized Cost		Gross Unrealized Gains		Gross Unrealized Losses		Fair Value
September 30, 2013								
Held-to-maturity:								
Certificates of deposit	$	5,229	$	16	$	(22)	$	5,223
GNMA mortgage-backed securities		3,497		170				3,667
Total held-to-maturity	$	8,726	$	186	$	(22)	$	8,890
Available-for-sale:								
FHLMC common stock	$	20	$	82	$		$	102
Preferred stock (1)		271		26				297
FNMA CMO/REMIC		3,303				(101)		3,202
FHLMC CMO/REMIC		1,892				(62)		1,830
GNMA CMO/REMIC		6,602				(316)		6,286
FNMA mortgage-backed securities		18,625		197		(163)		18,659
FHLMC mortgage-backed securities		18,189		120		(241)		18,068
GNMA mortgage-backed securities		3,559				(98)		3,461
U.S. Government agencies		39,341		338		(693)		38,986
Total available-for-sale	$	91,802	$	763	$	(1,674)	$	90,891
June 30, 2013								
Held-to-maturity:								
Certificates of deposit	$	3,985	$	18	$	(13)	$	3,990
GNMA mortgage-backed securities		4,054		179				4,233
Total held-to-maturity	$	8,039	$	197	$	(13)	$	8,223
Available-for-sale:								
FHLMC common stock	$	20	$	90	$		$	110
Preferred stock (1)		271		26				297
FNMA CMO/REMIC		3,389				(108)		3,281
FHLMC CMO/REMIC		1,941				(74)		1,867
GNMA CMO/REMIC		6,879		5		(173)		6,711
FNMA mortgage-backed securities		17,562		112		(160)		17,514
FHLMC mortgage-backed securities		17,819		67		(246)		17,640

GNMA mortgage-backed securities		2,619				(105)		2,514
U.S. Government agencies		38,387		294		(630)		38,051
Total available-for-sale	$	88,887	$	594	$	(1,496)	$	87,985

(1) Consists of 300 shares of Southern First Bancshares, Inc. cumulative perpetual preferred stock, series T.

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OCONEE FEDERAL FINANCIAL CORP.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(Amounts in thousands, except share and per share data)

The following table shows securities with unrealized losses at September 30, 2013, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position:

	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
September 30, 2013						
Available for Sale:						
FNMA CMO/REMIC	$ 3,202	$ (101)	$	$	$ 3,202	$ (101)
FHLMC CMO/REMIC			1,830	(62)	1,830	(62)
GNMA CMO/REMIC	6,286	(316)			6,286	(316)
FNMA mortgage-backed securities	18,659	(163)			18,659	(163)
FHLMC mortgage-backed securities	18,068	(241)			18,068	(241)
GNMA mortgage-backed securities	3,461	(98)			3,461	(98)
U.S. Government agencies	38,986	(693)			38,986	(693)
	$ 88,662	$ (1,612)	$ 1,830	$ (62)	$ 90,492	$ (1,674)

At September 30, 2013, there were twelve U.S. Government agency securities, five GNMA CMO/REMIC securities, two FNMA CMO/REMIC securities, two FHLMC CMO/REMIC securities, five FHLMC mortgage-backed securities, five FNMA mortgage-backed securities, three GNMA mortgage-backed securities, and ten certificates of deposit securities with unrealized losses at September 30, 2013. None of the unrealized losses for these securities have been recognized into net income for the three months ended September 30, 2013 because the issuer s bonds are of high credit quality, management does not intend to sell and it is likely that management will not be required to sell the securities prior to their anticipated recovery, and the decline in fair value is largely due to changes in interest rates. The fair value of these securities is expected to recover as they approach their maturity date or reset date. None of the unrealized losses at June 30, 2013 was recognized as OTTI during the three months ended September 30, 2013.

At September 30, 2013, none of the securities classified as held-to-maturity with unrealized losses were in an unrealized loss position for 12 continuous months or more. There were no securities at June 30, 2013 with unrealized losses that had been in an unrealized loss position for 12 continuous months or more.

The Company evaluates securities for OTTI at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. The Company considers the length of time and the extent to which the fair value has been less than cost and the financial condition and near-term prospects of the issuer. Additionally, the Company considers its intent to sell or whether it will be more likely than not it will be required to sell the security prior to the security s anticipated recovery in fair value. In analyzing an issuer s financial condition, the Company may consider whether the securities are issued by the federal Government agencies, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuer s financial condition.

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OCONEE FEDERAL FINANCIAL CORP.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(Amounts in thousands, except share and per share data)

The amortized cost and fair value of debt securities classified available-for-sale and held-to-maturity at September 30, 2013 by contractual maturity are summarized as follows:

	September 30, 2013		June 30, 2013	
	Amortized Cost	**Estimated Fair Value**	**Amortized Cost**	**Estimated Fair Value**
Less than one year	$ 1,245	$ 1,247	$ 996	$ 997
Due from one to five years	28,880	29,159	26,178	26,437
Due from five to ten years	10,445	10,045	11,198	10,800
Due after ten years	4,000	3,758	4,000	3,807
Mortgage backed securities	55,667	55,173	54,263	53,760
Total	$ 100,237	$ 99,382	$ 96,635	$ 95,801

There were no sales of securities during the three months ended September 30, 2013 and 2012.

(4) LOANS

The components of loans at September 30, 2013 and June 30, 2013 were as follows:

	September 30, 2013	June 30, 2013
Real estate loans:		
One- to four-family	$ 205,271	$ 204,397
Multi-family	256	258
Home equity	268	292
Nonresidential	8,365	8,521
Construction and land	8,818	8,735
Total real estate loans	222,978	222,203
Consumer and other loans	932	925
Total loans	223,910	223,128
Net deferred loan fees	(1,220)	(1,214)
Allowance for loan losses	(832)	(751)
Loans, net	$ 221,858	$ 221,163

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OCONEE FEDERAL FINANCIAL CORP.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(Amounts in thousands, except share and per share data)

The following tables present the activity in the allowance for loan losses for the three months ended September 30, 2013 and 2012 and the balances in the allowance for loan losses and the recorded investment in loans by portfolio segment based on impairment method at September 30, 2013 and 2012:

Three Months Ended September 30, 2013	**One-to-four family**	**Multi-family**	**Real estate Home Equity**	**Nonresidential**	**Construction and land**	**Consumer**	**Total**
Beginning balance	$ 665	$ 4	$ 1	$ 52	$ 27	$ 2	$ 751
Provision	82			(2)	1		81
Charge-offs							
Recoveries							
Ending balance	$ 747	$ 4	$ 1	$ 50	$ 28	$ 2	$ 832
Allowance for loan losses:							
Ending allowance attributed to loans:							
Individually evaluated for impairment	$ 110	$	$	$	$	$	$ 110
Collectively evaluated for impairment	637	4	1	50	28	2	722
Total ending allowance balance	$ 747	$ 4	$ 1	$ 50	$ 28	$ 2	$ 832
Loans:							
Loans individually evaluated for impairment	$ 3,203	$	$	$	$	$	$ 3,203
Loans collectively evaluated for impairment	202,068	256	268	8,365	8,818	932	220,707
Total ending loans balance	$ 205,271	$ 256	$ 268	$ 8,365	$ 8,818	$ 932	$ 223,910

Three Months Ended September 30, 2012	**One-to-four family**	**Multi-family**	**Real estate Home Equity**	**Nonresidential**	**Construction and land**	**Consumer**	**Total**
Beginning balance	$ 773	$ 4	$ 1	$ 56	$ 21	$ 2	$ 857
Provision	139				1	1	141
Charge-offs	(68)						(68)
Recoveries							
Ending balance	$ 844	$ 4	$ 1	$ 56	$ 22	$ 3	$ 930
Allowance for loan losses:							
Ending allowance attributed to loans:							
Individually evaluated for impairment	$ 192	$	$	$	$	$	$ 192
Collectively evaluated for impairment	652	4	1	56	22	3	738
Total ending allowance balance	$ 844	$ 4	$ 1	$ 56	$ 22	$ 3	$ 930
Loans:							

Loans individually evaluated for impairment	$ 2,756	$	$	$	$	$	$ 2,756
Loans collectively evaluated for impairment	225,437	262	383	9,110	7,345	851	243,388
Total ending loans balance	$ 228,193	$ 262	$ 383	$ 9,110	$ 7,345	$ 851	$ 246,144

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OCONEE FEDERAL FINANCIAL CORP.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(Amounts in thousands, except share and per share data)

The following table presents the balances in the allowance for loan losses and the recorded investment in loans by portfolio segment based on impairment method at June 30, 2013:

June 30, 2013	One-to-four family	Multi-family	Real estate Home Equity	Nonresidential	Construction and land	Consumer	Total
Allowance for loan losses:							
Ending allowance attributed to loans:							
Individually evaluated for impairment	$ 27	$	$	$	$	$	$ 27
Collectively evaluated for impairment	638	4	1	52	27	2	724
Total ending allowance balance	$ 665	$ 4	$ 1	$ 52	$ 27	$ 2	$ 751
Loans:							
Loans individually evaluated for impairment	$ 1,986	$	$	$	$	$	$ 1,986
Loans collectively evaluated for impairment	202,411	258	292	8,521	8,735	925	221,142
Total ending loans balance	$ 204,397	$ 258	$ 292	$ 8,521	$ 8,735	$ 925	$ 223,128

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OCONEE FEDERAL FINANCIAL CORP.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(Amounts in thousands, except share and per share data)

The following table presents loans individually evaluated for impairment by portfolio segment at September 30, 2013 and June 30, 2013, including the average recorded investment balance and interest earned for the three months ended September 30, 2013 and year ended June 30, 2013:

	September 30, 2013					June 30, 2013				
	Unpaid Principal Balance	Recorded Investment	Related Allowance	Average Recorded Investment	Interest Income Recognized	Unpaid Principal Balance	Recorded Investment	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no recorded allowance:										
Real estate loans:										
One- to four-family	$ 929	$ 929	$	$ 1,332	$ 9	$ 1,734	$ 1,734	$	$ 1,202	$ 27
Multi-family										
Home equity										
Nonresidential										
Construction and land										
Total real estate loans	929	929		1,332	9	1,734	1,734		1,202	27
Consumer and other loans										
Total	$ 929	$ 929	$	$ 1,332	$ 9	$ 1,734	$ 1,734	$	$ 1,202	$ 27
With recorded allowance:										
Real estate loans:										
One- to four-family	$ 2,274	$ 2,274	$ 110	$ 1,263	$ 7	$ 252	$ 252	$ 27	$ 1,033	$ 6
Multi-family										
Home equity										
Nonresidential										
Construction and land										
Total real estate loans	2,274	2,274	110	1,263	7	252	252	27	1,033	6
Consumer and other loans										
Total	$ 2,274	$ 2,274	$ 110	$ 1,263	$ 7	$ 252	$ 252	$ 27	$ 1,033	$ 6
Totals:										
Real estate loans	$ 3,203	$ 3,203	$ 110	$ 2,595	$ 16	$ 1,986	$ 1,986	$ 27	$ 2,235	$ 33
Consumer and other loans										
Total	$ 3,203	$ 3,203	$ 110	$ 2,595	$ 16	$ 1,986	$ 1,986	$ 27	$ 2,235	$ 33

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OCONEE FEDERAL FINANCIAL CORP.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(Amounts in thousands, except share and per share data)

The following table presents the aging of the recorded investment in past due loans at September 30, 2013 and June 30, 2013 by portfolio segment of loans:

September 30, 2013	**30-59 Days Past Due**	**60-89 Days Past Due**	**90 Days or More Past Due**	**Total Past Due**	**Current**	**Total Loans**	**Accruing Loans Past Due 90 Days or More**
Real estate loans:							
One- to four-family	$ 3,753	$ 1,163	$ 2,806	$ 7,722	$ 197,549	$ 205,271	$
Multi-family					256	256	
Home equity					268	268	
Nonresidential	21			21	8,344	8,365	
Construction and land					8,818	8,818	
Total real estate loans	3,774	1,163	2,806	7,743	215,235	222,978	
Consumer and other loans					932	932	
Total	$ 3,774	$ 1,163	$ 2,806	$ 7,743	$ 216,167	$ 223,910	$

June 30, 2013	**30-59 Days Past Due**	**60-89 Days Past Due**	**90 Days or More Past Due**	**Total Past Due**	**Current**	**Total Loans**	**Accruing Loans Past Due 90 Days or More**
Real estate loans:							
One- to four-family	$ 5,932	$ 2,397	$ 1,726	$ 10,055	$ 194,342	$ 204,397	$ 493
Multi-family					258	258	
Home equity	30			30	262	292	
Nonresidential					8,521	8,521	
Construction and land					8,735	8,735	
Total real estate loans	5,962	2,397	1,726	10,085	212,118	222,203	493
Consumer and other loans	1			1	924	925	
Total	$ 5,963	$ 2,397	$ 1,726	$ 10,086	$ 213,042	$ 223,128	$ 493

At September 30, 2013, nonaccrual loans were $3,203, of which $2,806 were past due 90 days or more. There were $223 of nonaccrual loans that were classified in the 60-89 days past due category and $174 of nonaccrual loans that were classified in the 30-59 days past due category. Nonaccrual loans at June 30, 2013 were $1,493. All of these loans were past due 90 days or more except one loan of $73 classified in the 30-59 days past due category. There were no troubled debt restructures at September 30, 2013 or June 30, 2013.

All loans graded pass, special mention, substandard and doubtful not specifically evaluated for impairment are collectively evaluated for impairment by portfolio segment. To develop and document a systematic methodology for determining the portion of the allowance for loan losses for loans evaluated collectively, the Company has divided the loan portfolio into six portfolio segments, each with different risk characteristics and methodologies for assessing risk and utilizes a loan grading system whereby all loans within each portfolio segment are assigned a grade based on the risk profile of each loan. Loan grades are determined based on an evaluation of relevant information about the ability of borrowers to service their debt such as current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. All loans, regardless of size, are analyzed and assigned a grade based upon management s assessment of the ability of borrowers to service their debts. The following describes each of the Company s loan grades and general information as to the risk profile of each of the Company s loan portfolio segments:

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Loan Grades:

Pass: Loans not meeting any of the criteria listed below for special mention, substandard, or doubtful are graded Pass.

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 repayment prospects for the loan or of the institution 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 obligor 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 institution 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.

Portfolio Segments:

One-to-four family: One-to-four family residential loans consist primarily of loans secured by first or second deeds of trust on primary residences, and are originated as adjustable-rate or fixed-rate loans for the construction, purchase or refinancing of a one-to-four family residence. These loans are collateralized by owner-occupied properties located in the Company s market area. We currently originate residential mortgage loans for our portfolio with loan-to-value ratios of up to 80% for traditional owner-occupied homes.

Multi-family: Multi-family real estate loans generally have a maximum term of 5 years with a 30 year amortization period and a final balloon payment and are secured by properties containing five or more units in the Company s market area. These loans are generally made in amounts of up to 75% of the lesser of the appraised value or the purchase price of the property with an appropriate projected debt service coverage ratio. The Company s underwriting analysis includes considering the borrower s expertise and requires verification of the borrower s credit history, income and financial statements, banking relationships, independent appraisals, references and income projections for the property. The

Company generally obtains personal guarantees on these loans.

Multi-family real estate loans generally present a higher level of risk than loans secured by one-to-four family residences. This greater risk is due to several factors, including the concentration of principal in a limited number of loans and borrowers, the effects of general economic conditions on income-producing properties and the increased difficulty of evaluating and monitoring these types of loans. Furthermore, the repayment of loans secured by multi-family residential real estate is typically dependent upon the successful operation of the related real estate project.

Home Equity: We originate fixed-rate home equity loans secured by a lien on the borrower s primary residence but only where we hold the first mortgage on the property. Our home equity loans are limited to an 80% loan-to-value ratio (including all prior liens), and have terms of up to 10 years with 10-year amortization periods. We use the same underwriting standards for home equity loans as we use for one- to four-family residential mortgage loans.

Nonresidential Real Estate: Our non-residential real estate loans are secured primarily by churches and, to a much lesser extent, office buildings, and retail and mixed-use properties located in our primary market area. The non-residential real estate loans that we originate generally have maximum terms of 5 years with amortization periods of 30 years. For loans secured by church property, our loans generally have maximum terms of 20 years with amortization periods of up to 20 years. The maximum loan-to-value ratio of our non-residential real estate loans is generally 75%.

Loans secured by non-residential real estate generally are larger than one- to four-family residential loans and involve greater credit risk. Non-residential real estate loans often involve large loan balances to single borrowers or groups of related borrowers. Repayment of these loans depends to a large degree on the results of operations and management of the properties securing the loans or the businesses conducted on such property, and may be affected to a greater extent by adverse conditions in the real estate market or the economy in general, including the current adverse conditions. In addition, because a church s financial stability often depends on donations from congregation members, some of whom may not reside in our market area,

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rather than income from business operations, repayment may be affected by economic conditions that affect individuals located both in our market area and in other market areas with which we are not as familiar. In addition, due to the unique nature of church buildings and properties, the real estate securing church loans may be less marketable than other non-residential real estate.

Construction and Land: We make construction loans to individuals for the construction of their primary residences and interim construction loans for non-residential properties. These loans generally have maximum terms of eight months, and upon completion of construction convert to conventional amortizing mortgage loans. These construction loans have rates and terms comparable to one- to four-family residential mortgage loans that we originate. During the construction phase, the borrower generally pays interest only. The maximum loan-to-value ratio of our owner-occupied construction loans is 80%. Residential construction loans are generally underwritten pursuant to the same guidelines used for originating permanent residential mortgage loans. Finally, we make loans secured by land to complement our construction and non-residential lending activities. These loans have terms of up to 10 years, and maximum loan-to-value ratios of 75% for improved lots and 65% for unimproved land.

To the extent our construction loans are not made to owner-occupants of single-family homes, they are more vulnerable to changes in economic conditions and the concentration of credit with a limited number of borrowers. Further, the nature of these loans is such that they are more difficult to evaluate and monitor. Our risk of loss on a construction or land loan is dependent largely upon the accuracy of the initial estimate of the property s value upon completion of the project and the estimated cost (including interest) of the project. If the estimate of value proves to be inaccurate, we may be confronted, at or prior to the maturity of the loan, with a project with a value which is insufficient to assure full repayment and/or the possibility of having to make substantial investments to complete and sell the project. Because defaults in repayment may not occur during the construction period, it may be difficult to identify problem loans at an early stage.

Consumer and Other Loans: We offer installment loans for various consumer purposes, including the purchase of automobiles, boats, appliances and recreational vehicles, and for other legitimate personal purposes. The maximum terms of consumer loans is 18 months for unsecured loans, 12 months for loans secured by marketable securities and 18-60 months for loans secured by a vehicle, depending on the age of the vehicle. We generally only extend consumer loans to existing customers or their immediate family members, and these loans generally have relatively low limits.

Consumer loans may entail greater credit risk than residential mortgage loans, particularly in the case of consumer loans that are unsecured or are secured by rapidly depreciable assets, such as automobiles. In addition, consumer loan collections are dependent on the borrower s continuing financial stability, and thus are more likely to be affected by adverse personal circumstances. Furthermore, the application of various federal and state laws, including bankruptcy and insolvency laws, may limit the amount which can be recovered on such loans.

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At September 30, 2013 and June 30, 2013, and based on the most recent analyses performed, the loan grade for each loan by portfolio segment is as follows:

	Real estate One-to four family September 30, 2013	Real estate One-to four family June 30, 2013	Real estate Multi-family September 30, 2013	Real estate Multi-family June 30, 2013	Real estate Home Equity September 30, 2013	Real estate Home Equity June 30, 2013	Real estate Nonresidential September 30, 2013	Real estate Nonresidential June 30, 2013
Pass	$ 202,068	$ 202,411	$ 256	$ 258	$ 268	$ 292	$ 8,365	$ 8,521
Special mention								
Substandard	3,203	1,986						
Total	$ 205,271	$ 204,397	$ 256	$ 258	$ 268	$ 292	$ 8,365	$ 8,521

	Real estate Construction and Land September 30, 2013	Real estate Construction and Land June 30, 2013	Consumer September 30, 2013	Consumer June 30, 2013	Total September 30, 2013	Total June 30, 2013
Pass	$ 8,818	$ 8,735	$ 932	$ 925	$ 220,707	$ 221,142
Special mention						
Substandard					3,203	1,986
Total	$ 8,818	$ 8,735	$ 932	$ 925	$ 223,910	$ 223,128

Loan risk ratings in the table above were updated for the three months ended September 30, 2013 and the year ended June 30, 2013.

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(5) FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. There are three levels of inputs that may be used to measure fair values:

Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2: Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3: Significant unobservable inputs that reflect a reporting entity s own assumptions about the assumptions that market participants would use in pricing an asset or liability.

Investment Securities:

The fair values for investment securities are determined by quoted market prices, if available (Level 1). For securities where quoted prices are not available, fair values are calculated based on market prices of similar securities (Level 2). For securities where quoted prices or market prices of similar securities are not available, fair values are calculated using discounted cash flows or other market indicators (Level 3). The Company s preferred stock investments are not actively traded; therefore, management estimates the fair value of its preferred stock using estimations provided by external dealer quotes.

Impaired Loans:

The fair value of impaired loans with specific allocations of the allowance for loan losses is generally based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are typically significant and result in a Level 3 classification of the inputs for determining fair value.

Real estate owned:

Nonrecurring adjustments to certain commercial and residential real estate properties classified as real estate owned are measured at the lower of carrying amount or fair value, less costs to sell. Fair values are generally based on third party appraisals of the property, resulting in a Level 3 classification. In cases where the carrying amount exceeds the fair value, less costs to sell, an impairment loss is recognized.

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Assets and liabilities measured at fair value on a recurring basis at September 30, 2013 and June 30, 2013 are summarized below:

	Fair Value Measurements (Level 2) September 30, 2013	(Level 2) June 30, 2013
Financial assets:		
Securities available-for-sale	$ 90,891	$ 87,985
Total financial assets	$ 90,891	$ 87,985

Presented in the table below are assets measured at fair value on a non-recurring basis using level 3 inputs at September 30, 2013 and June 30, 2013:

	Fair Value Measurements (Level 3) September 30, 2013	(Level 3) June 30, 2013
Financial assets:		
Impaired real estate loans, with specific allocations:		
One-to-four-family	$ 2,164	225
Non-financial assets:		
Real estate owned, net:		
One- to four-family	857	1,047
Total non-financial assets	857	1,047
Total assets measured at fair value on a non-recurring basis	$ 3,021	$ 1,272

Impaired loans, which are measured for impairment using the fair value of the collateral for collateral dependent loans, had a carrying amount of $2,164 and $225 at September 30, 2013 and June 30, 2013, respectively. The carrying values included a valuation allowance of $110 and $27, respectively, resulting in an increase in the provision for loan loss of $82 for the three months ended September 30, 2013.

Real estate owned is carried at the lower of carrying value or fair value less costs to sell. The outstanding balances of real estate owned and their respective valuation allowances at September 30, 2013 and June 30, 2013 were $857 and $0 and $1,047 and $0, respectively. There were no write-downs for measuring real estate owned at the lower of carrying or fair value less costs to sell for the three months ended September 30, 2013.

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The table below presents the valuation methodology and unobservable inputs for Level 3 assets measured at fair value on a non-recurring basis at September 30, 2013:

	Level 3 Quantitative Information at September 30, 2013			
	Fair Value	**Valuation Technique**	**Unobservable Inputs**	**Range (Weighted Average)**
Impaired real estate loans net, with specific allocations:				
One-to four-family	$ 2,164	Sales comparison approach	Adjustment for differences between the comparable sales	0% to 30% (15%)
Real estate owned:				
One-to four-family	$ 857	Sales comparison approach	Adjustment for differences between the comparable sales	0% to 20% (10%)

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Many of the Company s assets and liabilities are short-term financial instruments whose carrying amounts reported in the consolidated balance sheet approximate fair value. These items include cash and cash equivalents, accrued interest receivable and payable balances, variable rate loan and deposits that re-price frequently and fully. The estimated fair values of the Company s remaining on-balance sheet financial instruments at September 30, 2013 and June 30, 2013 are summarized below:

		September 30, 2013			
	Carrying Amount	**(Level 1)**	**(Level 2)**	**(Level 3)**	**Total**
Financial assets					
Securities available-for-sale	$ 90,891	$	$ 90,891	$	$ 90,891
Securities held-to-maturity	8,726		8,890		8,890
Loans, net	221,858			228,707	229,664
Restricted equity securities (1)	449	N/A	N/A	N/A	N/A
Financial liabilities					
Deposits	$ 288,784	$ 75,616	$ 213,593	$	$ 292,324

		June 30, 2013			
	Carrying Amount	**(Level 1)**	**(Level 2)**	**(Level 3)**	**Total**
Financial assets					
Securities available-for-sale	$ 87,985	$	$ 87,985	$	$ 87,985
Securities held-to-maturity	8,039		8,223		8,223
Loans, net	221,163			229,745	229,745
Restricted equity securities (1)	449	N/A	N/A	N/A	N/A
Financial liabilities					
Deposits	$ 292,422	$ 74,471	$ 218,395	$	$ 292,866

(1) It was not practicable to determine fair value of restricted equity securities due to restrictions placed on transferability.

(6) EMPLOYEE STOCK OWNERSHIP PLAN

Employees participate in an Employee Stock Ownership Plan (ESOP). The ESOP borrowed from the Company to purchase 248,842 shares of the Company s common stock at $10 per share during 2011. The Company makes discretionary contributions to the ESOP, and pays dividends on unallocated shares to the ESOP, and the ESOP uses funds it receives to repay the loan. When loan payments are made, ESOP shares are allocated to participants based on relative compensation and expense is recorded. Dividends on allocated shares increase participant accounts.

Participants receive the shares at the end of employment. No contributions to the ESOP were made during the three months ended September 30, 2013. The expense recognized for the three months ended September 30, 2013 and 2012 was $67 and $48, respectively.

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Shares held by the ESOP at September 30, 2013 and June 30, 2013 were as follows:

	September 30, 2013	June 30, 2013
Committed to be released to participants	13,595	9,064
Allocated to participants	33,211	33,211
Unearned	202,036	206,567
Total ESOP shares	248,842	248,842
Fair value of unearned shares	$ 3,333,594	$ 3,059,257

(7) STOCK BASED COMPENSATION

On April 5, 2012, the shareholders of Oconee Federal Financial Corp. approved the Oconee Federal Financial Corp. 2012 Equity Incentive Plan (the Plan) for employees and directors of the Company. The Plan authorizes the issuance of up to 435,472 shares of the Company s common stock, with no more than 124,420 of shares as restricted stock awards and 311,052 as stock options, either incentive stock options or non-qualified stock options. The exercise price of options granted under the Plan may not be less than the fair market value on the date the stock option is granted. The compensation committee of the board of directors has sole discretion to determine the amount and to whom equity incentive awards are granted.

On April 27, 2012, the compensation committee of the board of directors approved the issuance of 62,208 stock options to purchase Company stock and 24,884 shares of restricted stock to its directors. In addition, a total of 171,078 stock options and 62,210 shares of restricted stock were granted to officers. Stock options and restricted stock have vesting periods of 5 years or 7 years, a percentage of which vests annually on each anniversary date of grant. The weighted average vesting period of stock options and restricted stock granted was 5.7 and 5.6 years, respectively. Stock options expire ten years after issuance. Apart from the vesting schedule for both stock options and restricted stock, there are no performance-based conditions or any other material conditions applicable to the awards issued.

The following table summarizes stock option activity for the three months ended September 30, 2013:

	Options	Weighted-Average	Weighted-Average	Aggregate Intrinsic Value(1)

		Exercise Price/Share	Remaining Contractual Life (in years)	
Outstanding - July 1, 2013	233,286	$ 11.58		
Granted				
Exercised				
Forfeited				
Outstanding - September 30, 2013	233,286	$ 11.58	8.58	$ 1,147,767
Fully vested and exercisable at September 30, 2013	42,214	$ 11.58	8.58	$ 207,693
Expected to vest in future periods	191,072			
Fully vested and expected to vest - September 30, 2013	233,286	$ 11.58	8.58	$ 1,147,767

(1) Based on closing price of $16.50 per share on September 30, 2013.

Intrinsic value for stock options is defined as the difference between the current market value and the exercise price.

The fair value for each option grant is estimated on the date of grant using the Black-Scholes-Merton option pricing model that uses the following assumptions. The Company uses the U.S. Treasury yield curve in effect at the time of the grant to determine the risk-free interest rate. The expected dividend yield is estimated using the projected annual dividend level and recent stock price of the Company s common stock at the date of grant. Expected stock volatility is based on historical

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volatilities of the SNL Financial Index of Thrifts. The expected life of the options is calculated based on the simplified method as provided for under Staff Accounting Bulletin No.110.

The weighted-average fair value of options granted and assumptions used in the Black-Scholes-Merton option pricing model to determine the fair value of options are listed below:

Risk-free interest rate		1.54%
Expected dividend yield		3.45%
Expected stock volatility		15.3
Expected life (years)		8
Weighted-average fair value of options granted	$	1.00

Stock options are assumed to be earned ratably over their respective vesting periods and charged to compensation expense based upon their grant date fair value and the number of options assumed to be earned. There were 10,640 options that were earned during the three months ended September 30, 2013 and 2012. Stock-based compensation expense for stock options for the three months ended September 30, 2013 and 2012 was $10 and $11, respectively. Total unrecognized compensation cost related to nonvested stock options was $170 at September 30, 2013 and is expected to be recognized over a weighted-average period of 4.2 years.

The following table summarizes non-vested restricted stock activity for the three months ended September 30, 2013:

	September 30, 2013
Balance - beginning of year	71,095
Granted	
Forfeited	
Vested	
Balance - end of period	71,095

The fair value of the restricted stock awards is amortized to compensation expense over their respective vesting periods and is based on the market price of the Company s common stock at the date of grant multiplied by the number of shares granted that are expected to vest. The weighted-average grant date fair value of restricted stock granted during the year ended June 30, 2012 was $11.58 per share or $1,009. Stock-based compensation expense for restricted stock included in noninterest expense was $47 for the three months ended September 30, 2013 and 2012. Unrecognized compensation expense for nonvested restricted stock awards was $730 at September 30, 2013 and is expected to be recognized over a weighted-average period of 4.2 years.

(8) SUPPLEMENTAL CASH FLOW INFORMATION

Supplemental cash flow information for the three months ended September 30, 2013 and 2012:

	September 30, 2013	September 30, 2012
Cash paid during the period for:		
Interest paid	$ 430	$ 620
Income taxes paid	$ 200	$ 35
Supplemental noncash disclosures:		
Transfers from loans to real estate owned	$	$ 583
Unrealized gains (losses) on securities available-for-sale, net	$ (6)	$ 383

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(9) SUBSEQUENT EVENTS

On October 24, 2013, the Board of Directors of Oconee Federal Financial Corp. (the Company) declared a quarterly cash dividend of $0.10 per share of the Company s common stock. The dividend will be payable to stockholders of record as of November 7, 2013, and will be paid on or about November 21, 2013.

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ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

This Quarterly Report contains forward-looking statements, which can be identified by the use of such words as estimate, project, believe, intend, anticipate, plan, seek, expect and similar expressions. These forward-looking statements include:

- statements of our goals, intentions and expectations;
- statements regarding our business plans and prospects and growth and operating strategies;
- statements regarding the asset quality of our loan and investment portfolios; and
- estimates or our risks and future costs and benefits.

These forward-looking statements are based on our current beliefs and expectations and are inherently subject to significant business, economic, and competitive uncertainties and contingencies, many of which are beyond our control. In addition, these forward-looking statements are subject to assumptions with respect to future business strategies and decisions that are subject to change. We are under no duty to and do not take any obligation to update any forward-looking statements after the date of this Quarterly Report.

The following factors, among others, could cause actual results to differ materially from the anticipated results or other expectations expressed in the forward-looking statements:

- our ability to manage our operations under the current adverse economic conditions (including real estate values, loan demand, inflation, commodity prices and employment levels) nationally and in our market areas;
- adverse changes in the financial industry, securities, credit and national and local real estate markets (including real estate values);
- significant increases in our delinquencies and loan losses, including as a result of our inability to resolve classified assets, changes in the underlying cash flows of our borrowers, and management s assumptions in determining the adequacy of the allowance for loan losses;

- credit risks of lending activities, including changes in the level and trend of loan delinquencies and write-offs and in our allowance and provision for loan losses;

- use of estimates for determining the fair value of certain of our assets, which may prove to be incorrect and result in significant declines in valuations;

- increased competition among depository and other financial institutions;

- our ability to attract and maintain deposits, including attracting and maintaining deposits and introducing new deposit products;

- changes in interest rates generally, including changes in the relative differences between short term and long term interest rates and in deposit interest rates, that may affect our net interest margin and funding sources;

- fluctuations in the demand for loans, which may be affected by the number of unsold homes, land and other properties in our market areas and by declines in the value of real estate in our market area;

- declines in the yield on our assets resulting from the current low interest rate environment;

- our ability to successfully implement our business strategies, including attracting and maintaining deposits and introducing new financial products;

- risks related to high concentration of loans secured by real estate located in our market areas;

- changes in laws or government regulations or policies affecting financial institutions, including the Dodd-Frank Act and the JOBS Act, which could result in, among other things, increased deposit insurance premiums and assessments, capital requirements, regulatory fees and compliance costs, particularly the new capital regulations;

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- changes in the level of government support of housing finance;
- our ability to manage our operations following increased leverage and risk-based capital requirements due to the implementation of Basel III by our regulators;
- the results of examinations by our regulators, including the possibility that our regulators may, among other things, require us to increase our reserve for loan losses, write down assets, change our regulatory capital position, limit our ability to borrow funds or maintain or increase deposits, or prohibit us from paying dividends, which could adversely affect our dividends and earnings;
- our ability to enter new markets successfully and capitalize on growth opportunities;
- risks relating to acquisitions, including losses that we may incur on loans originated by such institutions, and an ability to integrate and operate profitably any financial institution that we may acquire;
- our reliance on a small executive staff;
- changes in our compensation and benefit plans, and our ability to retain key members of our senior management team and to address staffing needs to implement our strategic plan;
- changes in consumer spending, borrowing and savings habits;
- changes in accounting policies and practices, as may be adopted by the bank regulatory agencies, the Financial Accounting Standards Board, the Securities and Exchange Commission and the Public Company Accounting Oversight Board;
- our ability to control costs and expenses, particularly those related to operating as a publicly traded company;
- changes in our financial condition or results of operations that reduce capital available to pay dividends;

- changes in the financial condition or future prospects of issuers of securities that we own, including our stock in the FHLB of Atlanta; and

- other economic, competitive, governmental, regulatory and operational factors affecting our operations, pricing, products and services.

Because of these and a wide variety of other uncertainties, our actual future results may be materially different from the results indicated by these forward-looking statements.

Critical Accounting Policies

There are no material changes to the critical accounting policies disclosed in the Annual Report on Form 10-K for Oconee Federal Financial Corp. for the year ended June 30, 2013, as filed with the Securities and Exchange Commission.

Comparison of Financial Condition at September 30, 2013 and June 30, 2013

Our total assets decreased by $4.2 million, or 1.1%, to $365.9 million at September 30, 2013 from $370.1 million at June 30, 2013. A substantial portion of this decrease is reflected in the decrease in cash and cash equivalents of $8.5 million, or 22.3%, offset partially by an increase in investment securities of $3.6 million, or 3.7% and an increase in net loans of $695 thousand, or 0.3%. We are continuing to deploy excess funds to purchase high-quality investment securities. The decrease in cash is reflective of a slight increase in loan demand and a decline in loan pay-offs for the three months ended September 30, 2013. The remaining portion of the decrease in cash and cash equivalents is attributed to the repurchase of $1.4 million of shares of treasury stock, the payment of $584 thousand in dividends, and approximately $3.6 million decrease in total deposits, exclusive of the treasury stock repurchases and dividend payments. Total equity decreased to $75.2 million at September 30, 2013 compared with $76.2 million at June 30, 2013. The decrease in total equity is the result of the repurchase of 89,900 shares of treasury stock for $1.4 million and the payment of dividends of $584 thousand, offset partially by net income of $919 thousand.

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Total gross loans increased by $782 thousand, or 0.35%, to $223.9 million at September 30, 2013 from $223.1 million at June 30, 2013. Our one-to four-family real estate loans increased by $874 thousand, or 0.43%, to $205.3 million at September 30, 2013 from $204.4 million at June 30, 2013. The increase is a reflection of increasing mortgage rates in the market. As mortgage rates have trended upward, our rates offered on one-to four-family mortgage loans have become more competitive in the market leading to a slight increase in demand and a reduction in loan pay-offs stemming from borrower refinances with other institutions. The increase in one-to four-family loans was offset by slight declines in every other loan category with the exception of construction and land and consumer and other loans, which both increased modestly by $83 thousand and $7 thousand, respectively.

Deposits decreased by $3.6 million, or 1.2%, to $288.8 million at September 30, 2013 from $292.4 million at June 30, 2013. The decrease was primarily attributed to a decrease in interest bearing deposit accounts of $3.6 million, or 1.2%, primarily within our certificates of deposit accounts. As older certificates of deposits with slightly higher rates have matured, some depositors have moved funds out of the Company and into other higher yielding investments. Oconee Federal MHC s cash is held on deposit with the Company. We generally do not accept brokered deposits and no brokered deposits were accepted during the three months ended September 30, 2013.

We had no advances from the Federal Home Loan Bank of Atlanta as of September 30, 2013 or June 30, 2013. We have credit available under a loan agreement with the Federal Home Loan Bank of Atlanta in the amount of 11% of total assets (as of September 30, 2013), or approximately $40.7 million.

Total equity decreased by $978 thousand, or 1.3%, to $75.2 million at September 30, 2013 compared with $76.2 million at June 30, 2013. The decrease in total equity is the result of the repurchase of 89,900 shares of treasury stock for $1.4 million and the payment of dividends of $584 thousand, offset partially by net income of $919 thousand.

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Nonperforming Assets

The table below sets forth the amounts and categories of our nonperforming assets at the dates indicated.

	September 30, 2013	June 30, 2013
	(Dollars in thousands)	
Non-accrual loans:		
Real estate loans:		
One- to four-family	$ 3,203	$ 1,493
Multi-family		
Home equity		
Non-residential		
Construction and land		
Total real estate loans	3,203	1,493
Consumer and other loans		
Total nonaccrual loans	$ 3,203	$ 1,493
Accruing loans past due 90 days or more:		
Real estate loans:		
One- to four-family	$	$ 493
Multi-family		
Home equity		
Non-residential		
Construction and land		
Total real estate loans		493
Consumer and other loans		
Total accruing loans past due 90 days or more		493
Total of nonaccrual and 90 days or more past due loans	$ 3,203	$ 1,986
Real estate owned, net:		
One- to four-family	$ 857	$ 1,047
Multi-family		
Home equity		
Non-residential		
Other		
Other nonperforming assets		
Total nonperforming assets	$ 4,060	$ 3,033
Troubled debt restructurings		
Troubled debt restructurings and total nonperforming assets	$ 4,060	$ 3,033
Total nonperforming loans to total loans	1.43%	0.89%
Total nonperforming assets to total assets	1.11%	0.82%
Total nonperforming assets to loans and real estate owned	1.81%	1.35%

There were no other loans that are not disclosed above where there is information about possible credit problems of borrowers that caused us serious doubts about the ability of the borrowers to comply with present loan repayment terms and that may result in disclosure of such loans in the future.

Interest income that would have been recorded had our non-accruing loans been current in accordance with their original terms was $63 thousand and $59 thousand for the three months ended September 30, 2013 and 2012, respectively. Interest of

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$16 thousand and $8 thousand was recognized on these loans and is included in net income for the three months ended September 30, 2013 and 2012, respectively.

The increase in the ratio of nonperforming loans to total loans was primarily the result of the declining balance of our loan portfolio along with an increase in nonperforming loans. The increase in nonperforming loans was primarily related to two large balance loans, totaling approximately $1.2 million that became past due 90 days during the three months ended September 30, 2013. All nonperforming loans, regardless of size, are evaluated by management for impairment.

Analysis of Net Interest Margin

The following tables set forth average balance sheets, average yields and rates, and certain other information at and for the periods indicated. No tax-equivalent yield adjustments were made, as the effect thereof was not material. All average balances are daily average balances. Nonaccrual loans were included in the computation of average balances, but have been reflected in the tables as loans carrying a zero yield. The yields set forth below include the effect of net deferred costs, discounts and premiums that are amortized or accreted to income.

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	For the Three Months Ended					
	September 30, 2013			September 30, 2012		
	Average Balance	Interest and Dividends	Yield/ Cost	Average Balance	Interest and Dividends	Yield/ Cost
	(Dollars in Thousands)					
Assets:						
Interest-earning assets:						
Loans	$ 221,611	$ 2,852	5.15%	$ 248,053	$ 3,370	5.43%
Investment securities	99,060	371	1.50	73,021	266	1.46
Interest-bearing deposits	31,178	15	0.19	47,857	18	0.15
Total interest-earning assets	351,849	3,238	3.68	368,931	3,654	3.96
Noninterest-earning assets	15,022			9,760		
Total assets	$ 366,871			$ 378,691		
Liabilities and equity:						
Interest-bearing liabilities:						
NOW and demand deposits	$ 18,872	$ 3	0.06%	$ 17,858	$ 3	0.07%
Money market deposits	12,271	6	0.20	12,060	7	0.24
Regular savings and other deposits	39,391	38	0.38	34,478	62	0.71
Certificates of deposit	215,474	382	0.70	225,130	553	0.97
Total interest-bearing deposits	286,008	429	0.60	289,526	625	0.86
Total interest-bearing liabilities	286,008			289,526		
Noninterest bearing deposits	3,781			3,764		
Other noninterest-bearing liabilities	1,416			1,986		
Total liabilities	291,205			295,275		
Equity	75,666			83,416		
Total liabilities and equity	$ 366,871			$ 378,691		
Net interest income		$ 2,809			$ 3,029	
Interest rate spread			3.09%			3.10%
Net interest margin			3.19%			3.28%
Average interest-earning assets to average interest-bearing liabilities	1.23X			1.27X		

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Comparison of Operating Results for the Three Months Ended September 30, 2013 and September 30, 2012

General. We recognized net income of $919 thousand for the three months ended September 30, 2013 as compared to net income of $1.0 million for the three months ended September 30, 2012. The decrease of $98 thousand was primarily attributable to a decrease in net interest income after provision for loan losses of $160 thousand, or 5.5%, and an increase in noninterest expense of $89 thousand, or 6.9%.

Interest Income. Interest income decreased by $416 thousand, or 11.4%, to $3.2 million for the three months ended September 30, 2013 from $3.7 million for the three months ended September 30, 2012. The decrease was primarily the result of a decrease in the average yield on interest earning assets of 28 basis points to 3.68% for the three months ended September 30, 2013 from 3.96% for the three months ended September 30, 2012 and a decrease in the average balance of interest earning assets of $17.1 million, or 4.6%, to $351.8 million for the three months ended September 30, 2013 from $368.9 million for the three months ended September 30, 2012.

Interest income on loans decreased by $518 thousand, or 15.4%, to $2.9 million for the three months ended September 30, 2013 from $3.4 million for the three months ended September 30, 2012. The decrease resulted from a decrease in the average balances of loans of $26.4 million, or 10.6%, to $221.6 million for the three months ended September 30, 2013 from $248.1 million for the three months ended September 30, 2012 and a decrease in the yield on loans of 28 basis points to 5.15% for the three months ended September 30, 2013 from 5.43% for the three months ended September 30, 2012. Interest income on investment securities increased by $105 thousand, or 39.5%, to $371 thousand for the three months ended September 30, 2013 from $266 thousand for the three months ended September 30, 2012. The increase reflected an increase in the average balance of securities of $26.1 million, or 35.6%, to $99.1 million for the three months ended September 30, 2013 from $73.0 million for the three months ended September 30, 2012 and a slight increase of four basis points in the yield on securities to 1.50% from 1.46%. The increase in average balances of our investment securities is reflective of our efforts to continue to invest in high-quality investment securities during this period of low loan demand.

Interest Expense. Interest expense decreased $196 thousand, or 31.4%, to $429 thousand for the three months ended September 30, 2013 from $625 thousand for the three months ended September 30, 2012. The decrease reflected a decrease of 26 basis points in the average rate paid on deposits for the three months ended September 30, 2013 to 0.60% from 0.86% for the three months ended September 30, 2012 and a decrease in the average balances of deposits of $3.5 million, or 1.2%, to $286.0 million for the three months ended September 30, 2013 from $289.5 million for the three months ended September 30, 2012. The largest decrease in interest expense came from certificates of deposit, which decreased $171 thousand, or 30.9%, to $382 thousand for the three months ended September 30, 2013 from $533 thousand for the same period. The decrease is reflective of a decrease of $9.6 million, or 4.3%, in the average balance of certificates of deposit to $215.5 million for the three months ended September 30, 2013 from $225.1 million for the three months ended September 30, 2012 and a decrease of 27 basis points in the average rate paid on such deposits to 0.70% from 0.97% for the same periods ended.

Net Interest Income. Net interest income before the provision for loan losses decreased by $220 thousand, or 7.3%, to $2.8 million for the three months ended September 30, 2013 from $3.0 million for the three months ended September 30, 2012. The decrease resulted from a decrease in our interest rate spread to 3.09% from 3.10% and a decrease in our net interest margin to 3.19% from 3.28% for the same periods. The decrease in our interest rate spread and margin was largely due to declining yields on interest earning assets, which reflected the continuing decline across the U.S. Treasury yield curve.

Provision for Loan Losses. We recorded a provision for loan losses of $81 thousand for the three months ended September 30, 2013, compared with a provision of $141 thousand for the three months ended September 30, 2012. Net charge-offs for the three months ended September 30, 2013 were $0 compared to $68 thousand for the three months ended September 30, 2012. The decrease in our provision is primarily a factor of lower net charge-offs as compared with the three months ended September 30, 2012 and an overall decline in our loan balances as compared with September 30, 2012. Our gross loans at September 30, 2013 were $223.9 million compared with $246.1 million at September 30, 2012. Our allowance for loan losses was $832 thousand at September 30, 2013 and $751 thousand at June 30, 2013.

We used the same methodology in assessing the allowances for both periods. To the best of our knowledge, we have recorded all losses that are both probable and reasonably estimable for the three months ended September 30, 2013 and 2012.

Noninterest Income. Noninterest income for the three months ended September 30, 2013 was $80 thousand compared with $86 thousand for the same period in 2012. The Company s $14 thousand loss on sales of real estate owned for the three months ended September 30, 2013 compared with three months ended September 30, 2012 was offset by an increase in other noninterest income of $67 thousand to $76 thousand for a $57 thousand gain the three months ended September 30, 2013 from $9 thousand for the same period in 2012. The $76 thousand of other noninterest income is largely attributable to income on bank owned life insurance. In April 2013, the Company purchased an additional $8.0 million in bank owned life insurance.

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Noninterest Expense. Noninterest expense for the three months ended September 30, 2013 increased by $89 thousand, or 6.9%, over the same period in 2012. The increase to the Company s noninterest expense primarily resulted from increases in salaries and employee benefits of $71 thousand, or 9.0%, and professional and supervisory fees of $33 thousand, or 41.8%. These increases were offset, partially, by a decrease in occupancy and equipment expenses of $22 thousand, or 12.4%

Income Tax Expense. Income tax expense for the three months ended September 30, 2013 was $513 thousand compared with $670 thousand for the three months ended September 30, 2012. Our effective income tax rate decreased to 35.8% for the three months ended September 30, 2013 from 39.7% for the three months ended September 30, 2012. The decrease in effective tax rates is largely due to income on bank owned life insurance, which is non-taxable for income tax purposes and represents a permanent difference between book and taxable income.

Liquidity and Capital Resources

Our primary sources of funds are deposits and the proceeds from principal and interest payments on loans and investment securities. While maturities and scheduled amortization of loans and securities are predictable sources of funds, deposit flows and mortgage prepayments are greatly influenced by general interest rates, economic conditions and competition. We generally manage the pricing of our deposits to be competitive within our market and to increase core deposit relationships.

Liquidity management is both a daily and long-term responsibility of management. We adjust our investments in liquid assets based upon management s assessment of (i) expected loan demand, (ii) expected deposit flows, (iii) yields available on interest-earning deposits and investment securities, and (iv) the objectives of our asset/liability management program. Excess liquid assets are invested generally in interest-earning overnight deposits, federal funds sold, and short and intermediate-term U.S. Government sponsored agencies and mortgage-backed securities of short duration. If we require funds beyond our ability to generate them internally, we have credit available under a loan agreement with the Federal Home Loan Bank of Atlanta in the amount of 11% assets (as of September 30, 2013), or approximately $40.7 million.

Common Stock Dividend Policy. The Company s Board of Directors declared $0.10 per share cash dividends on its common stock on July 25, 2013. Dividends were paid to stockholders of record as of August 15, 2013. Total dividends paid for the three months ended September 30, 2012 were $584 thousand.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Disclosures of quantitative and qualitative market risk are not required by smaller reporting companies, such as the Company.

ITEM 4. CONTROLS AND PROCEDURES

An evaluation was performed under the supervision and with the participation of the Company s management, including the Chief Executive Officer and the Chief Financial Officer, of the effectiveness of the design and operation of the Company s disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) promulgated under the Securities and Exchange Act of 1934, as amended) as of September 30, 2013. Based on that evaluation, the Company s management, including the Chief Executive Officer and the Chief Financial Officer, concluded that the Company s disclosure controls and procedures were effective.

During the quarter ended September 30, 2013, there have been no changes in the Company s internal control over financial reporting (as defined in Rule 13a-15(f) and 15d-15(f) under the Securities and Exchange Act of 1934, amended) that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

PART II

ITEM 1. LEGAL PROCEEDINGS

There are various claims and lawsuits in which the Company is periodically involved incidental to the Company s business. In the opinion of management, no material loss is expected from any of such pending claims or lawsuits.

ITEM 1A. RISK FACTORS

Disclosures of risk factors are not required by smaller reporting companies, such as the Company.

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ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

(a) None.

(b) Not applicable.

(c) ***Issuer Repurchases.*** The following table sets forth information in connection with repurchases of the Company s common stock for the period July 1, 2013 through September 30, 2013. On June 19, 2013, the Board of Directors authorized the repurchase of up to 150,000 shares of the Company s common stock. The repurchase authorization has no expiration date. In connection with this repurchase authorization, the Company had purchased a total of 89,900 shares of its common stock.

	Total Number of Shares Purchased		**Average Price Paid Per Share**	**Total Number of Shares Purchased as Part of Publicly Announced Plan**	**Approximate Maximum Dollar Value or Number of Shares That May Yet be Purchased Under Publicly Announced Plan**
July 1 - July 31, 2013	84,684		15.82	84,684(1)	65.316(2)
August 1 - August 31, 2013	5,216		16.29	5,216(1)	60,100(2)
September 1 - September 30, 2013					60,100(2)
Total	89,900	$	15.85	89,900	

(1) All shares were purchased pursuant to a publicly announced repurchase program that was approved by the Board of Directors on June 19, 2013.

(2) Represents the maximum number of shares available for repurchase under the June 19, 2013 plan at June 30, 2013.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

The exhibits required by Item 601 of Regulation S-K are included with this Form 10-Q and are listed on the Index to Exhibits immediately following the Signatures.

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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.

Oconee Federal Financial Corp.

Date: November 14, 2013

/s/ T. Rhett Evatt
T. Rhett Evatt
President and Chief Executive Officer

/s/ Curtis. T. Evatt
Curtis T. Evatt
Executive Vice President and Chief Financial Officer

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INDEX TO EXHIBITS

Exhibit number	Description
31.1	Certification of T. Rhett Evatt, President and Chief Executive Officer, Pursuant to Rule 13a-14(a) and Rule 15d-14(a).
31.2	Certification of Curtis T. Evatt, Executive Vice President and Chief Financial Officer, Pursuant to Rule 13a-14(a) and Rule 15d-14(a).
32.1	Certification of T. Rhett Evatt, President and Chief Executive Officer, and Curtis T. Evatt, Executive Vice President and Chief Financial Officer, Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101	The following materials from the Company s Quarterly Report on Form 10-Q for the quarter ended September 30, 2013, formatted in XBRL (Extensible Business Reporting Language):

(i) Consolidated Balance Sheets

(ii) Consolidated Statements of Income and Other Comprehensive Income

(iii) Consolidated Statements of Shareholders Equity

(iv) Consolidated Statements of Cash Flows, and

(v) Notes to The Consolidated Financial Statements