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CLAYTON HOMES, INC.

ANNUAL REPORT 1991

Company Profile

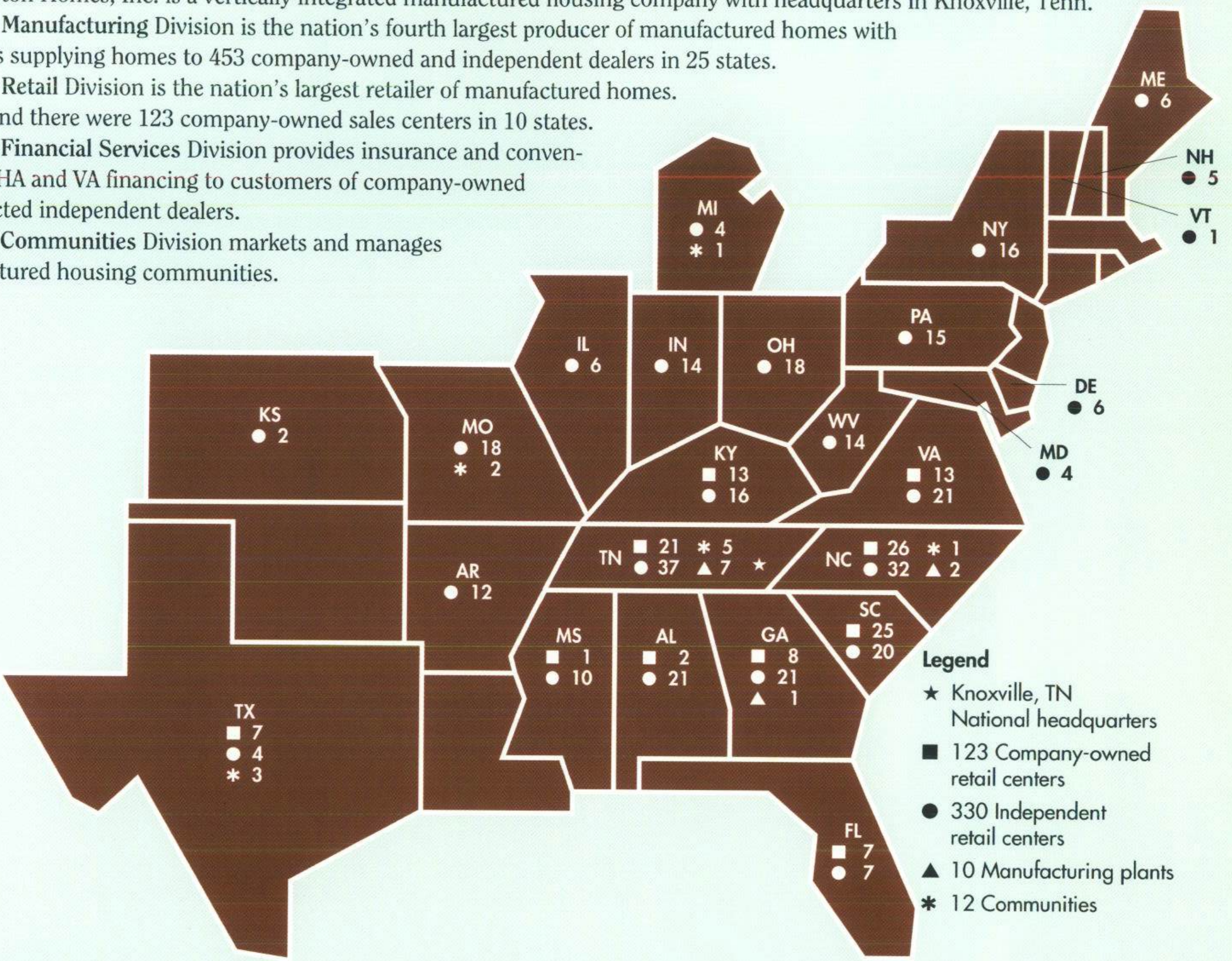
Clayton Homes, Inc. is a vertically integrated manufactured housing company with headquarters in Knoxville, Tenn.

The **Manufacturing** Division is the nation's fourth largest producer of manufactured homes with 10 plants supplying homes to 453 company-owned and independent dealers in 25 states.

The **Retail** Division is the nation's largest retailer of manufactured homes. At year end there were 123 company-owned sales centers in 10 states.

The **Financial Services** Division provides insurance and conventional, FHA and VA financing to customers of company-owned and selected independent dealers.

The **Communities** Division markets and manages manufactured housing communities.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MI ● 4 ✱ 1
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KY ■ 13 ● 16
VA ■ 13 ● 21
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TN ■ 21 ● 37 ✱ 5 ▲ 7 ★
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AR ● 12
SC ■ 25 ● 20
MS ■ 1 ● 10
AL ■ 2 ● 21
GA ■ 8 ● 21 ▲ 1
TX ■ 7 ● 4 ✱ 3
FL ■ 7 ● 7
Legend
★ Knoxville, TN National headquarters
■ 123 Company-owned retail centers
● 330 Independent retail centers
▲ 10 Manufacturing plants
✱ 12 Communities

About the Cover

Clayton's vertically integrated structure promotes teamwork, and results in high-quality products and services. Each person's unique contribution adds value along the way, enabling the Company to produce attractive, affordable homes and to be the leading retailer in the manufactured housing industry.

(Left to right) Eddie Venable, Cindy Tomlin, Aneitta White, Steve Williams and Jim Gillikin represent each segment of the Company working together to produce record results every year.

Eddie Venable manages a sales center in Middlesboro, Ky., where he has earned Manager of the Year honors three times and has been among the top 10 managers every year since 1976.

Cindy Tomlin is a sales professional at the Company's Waynesboro, Va., location and has earned Top Sales Professional of the Year honors for two consecutive years.

Aneitta White manages a Knoxville-area community location, having worked as a sales professional and sales manager with the Company for eight years.

Steve Williams is a senior finance manager and oversees all acquired portfolios for the Financial Services Division.

Jim Gillikin is general manager of the Maynardville, Tenn., plant, a post he has held since 1985. This year, the plant produced its 25,000th home.

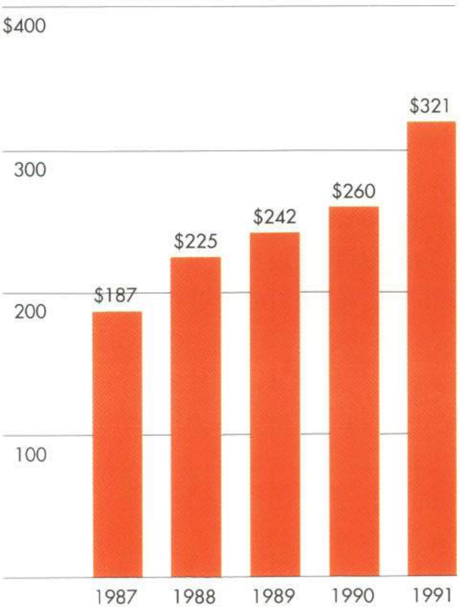
Together, these individuals – and 2,600 others – have created a financially sound Company based on teamwork, diligent effort and quality results.

Financial Highlights

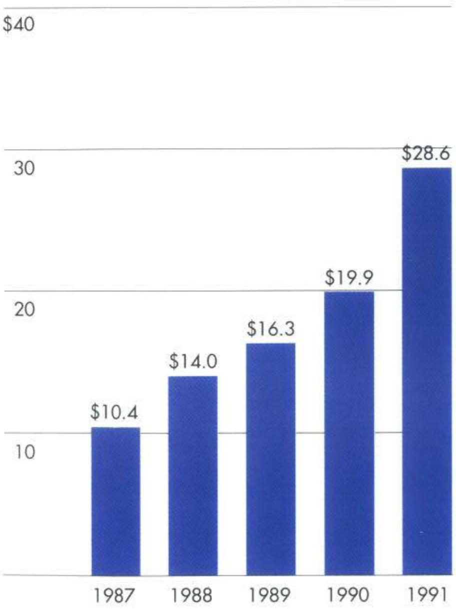
UNIVERSITY OF TEXAS AT ARLINGTON LIBRARY

	Year Ended June 30,		
(in thousands, except per share and Other Data)	1991	1990	% Change
Revenues	**$320,566**	$260,325	23%
Income before income taxes	**44,593**	31,370	42%
Net income	**28,593**	19,870	44%
Earnings per common share:			
Primary	**1.26**	.98	29%
Fully diluted	**1.15**	.87	32%
Balance Sheet Data:			
Total assets	**$488,817**	$339,099	44%
Shareholders' equity	**200,992**	108,334	86%
Return on average shareholders' equity	**19.5%**	20.3%	
Portfolio Data:			
Loans serviced	**$607,000**	$420,000	45%
Delinquency (over 30 days) %:			
Originated contracts	**2.5%**	2.1%	
All contracts serviced (including purchased portfolios)	**3.4%**	2.6%	
Net write-offs as % of average loans outstanding:			
Originated contracts	**.3%**	.4%	
All contracts (including purchased portfolios)	**.9%**	.6%	
Other Data:			
Total homes sold	**14,009**	12,153	15%
Market share (nation)	**7.3%**	5.7%	
Manufacturing plants	**10**	10	0%
Independent dealers	**330**	322	2%
Company-owned retail centers	**123**	96	28%
Community sites owned	**1,960**	1,182	66%
Employees	**2,595**	2,212	17%

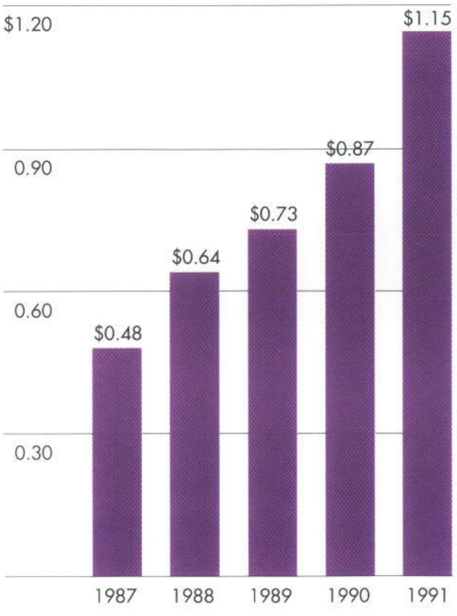
Revenues
(in millions)



Net Income
(in millions)



Earnings Per Share
(fully diluted)



Letter to Shareholders

Executive committee (left to right):
Richard B. Ray, James L. Clayton, Timothy W. Williams, E. Tyler Kelly.

Fiscal 1991 was our 11th consecutive record year of earnings:

- Net income surged 44% to $28.6 million.
- Fully diluted earnings per share advanced 32% to $1.15 a share.
- Revenues rose 23% to $321 million.
- Shareholders' equity grew to $201 million from $108 million.
- Fourth quarter net income was the 32nd increase in 33 quarters since going public in June 1983.
- National market share for total Company sales rose to 7.3% from 5.7%.

During 1991 we accomplished the following:

- Manufacturing moved from the sixth to fourth largest producer.
- Retail successfully integrated the July 2, 1990, purchase of 20 Country Squire sales centers, which contributed better-than-expected results.
- Financial Services' loan portfolio grew 45% to $607 million through originating $156 million in receivables and purchasing $119 million of manufactured housing loans.
- Communities purchased its joint venture partner's 50% ownership interest in nine communities on May 24, 1991.

In the third quarter the balance sheet was significantly strengthened by converting to equity $48 million of 7¾% and 6% debentures. Additionally, the Company raised $53 million of new capital by issuing 900,000 shares of common stock and selling $40 million of 7¾% convertible subordinated debentures due 2003. Standard & Poor's gave the new debentures a BBB- rating, which carries an implied investment grade rating of BBB on senior indebtedness. This upgrade in rating will facilitate funding the finance subsidiary.

SPECIAL RECOGNITION

Horatio Alger Award

Jim Clayton was one of 10 Americans selected to receive the 1991 Horatio Alger Award.

At the April Awards Banquet in Washington, D.C., Mr. Clayton said he was honored to be among such a distinguished gathering of great Americans. "I was able to meet people of a stature that I never dreamed possible," he said.

Other 1991 winners include General Colin L. Powell, chairman of the Joint Chiefs of Staff; Harold A. Poling, chairman and CEO, Ford Motor Co.; and sports legend and Baseball Hall of Famer Stan Musial.

Since 1947, the Horatio Alger Awards have been given to men and women who, like the characters in Horatio Alger's stories, started small and went on to achieve greatness. The Association was founded by Norman Vincent Peale, who told Mr. Clayton in a congratulatory letter, "Individuals like you are living proof the free enterprise system offers opportunity to all."

Mr. Clayton said the honor means a great deal to him because it recognizes not only his achievements but those of the people in the Company as well.

Clayton Homes, founded by Mr. Clayton in 1966, is one of a select group of companies that has two Horatio Alger awardees: Clayton and Director Wallace Rasmussen.

The Wall Street Transcript

For the fourth time in five years, *The Wall Street Transcript* named Jim Clayton the top chief executive officer in the manufactured housing industry.

The award is presented annually to CEOs whose actions have successfully increased shareholder value. Mr. Clayton said the award attests to the professionalism, dedication and consistent performance of the Company's management team.

In June, Standard & Poor's announced the introduction of its new Mid-Cap index to track the stock market performance of 400 medium capitalization stocks. Clayton Homes is included in this index, providing the Company with increased visibility, possible wider coverage by investment analysts and increased institutional interest in the stock.

Securities analysts and investors often ask how we consistently post increases in earnings when the number of homes sold by our industry decreases. The answer is multi-faceted. It ranges from the hard work and dedication of our people to the Company's overall structure and strategy.

For example, through financial and recognition incentives, virtually all personnel are rewarded for performing the daily basics in a manner that improves profitability. Our strategy of open, vertical integration allows each division to operate and grow with a degree of autonomy while simultaneously supporting each other's activities. Additionally, the Retail Division originates 90% of Financial Services' new loans, handles most of the re-marketing of the Company's repossessions and provides an efficient distribution system for half of the Manufacturing Division's production.

At the beginning of the year we updated our five-year strategic plan in which we decided to stick to what we do best: manufacturing and marketing affordable homes and offering related financing and insurance services. The plan calls for continued income growth at an annual rate of 15%. By the end of fiscal year 1995 we should have 13 manufacturing plants, 600 independent dealers, 200 company-owned sales centers and a $1.1 billion loan portfolio.

Plans for next year include:

- Expand the number of company-owned retail sales centers by 15.
- Add a manufacturing facility in the Southwest.
- Originate $180 million of manufactured housing installment contract receivables.

We look forward to reporting our progress.

Sincerely,

Jim Clayton

James L. Clayton
Chairman of the Board, Chief Executive Officer, President

E. Tyler Kelly
*Executive Vice President –
Manufacturing Division*

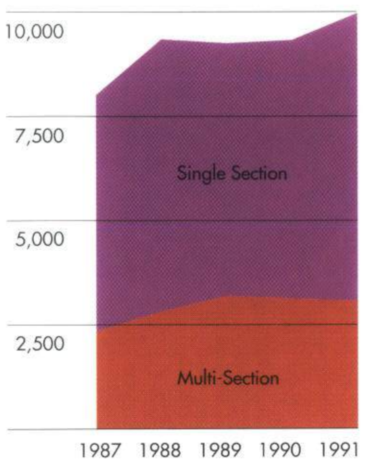
Tim Williams

Timothy W. Williams
*Executive Vice President –
Vanderbilt Mortgage and Finance, Inc.*

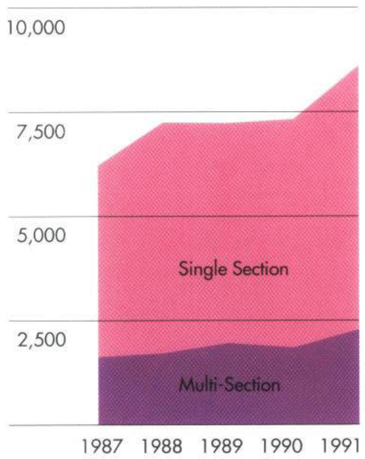
Richard Ray

Richard B. Ray
*Executive Vice President –
Finance, Chief Financial Officer*

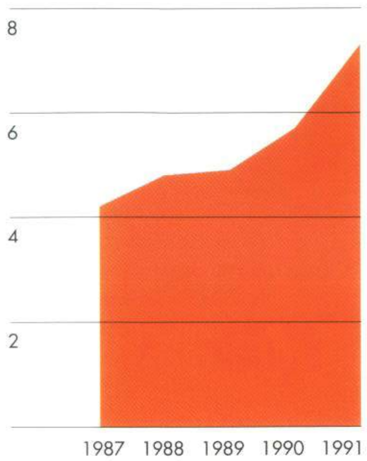
Homes Built



Homes Retailed



National Market Share
(total sales – fiscal year)

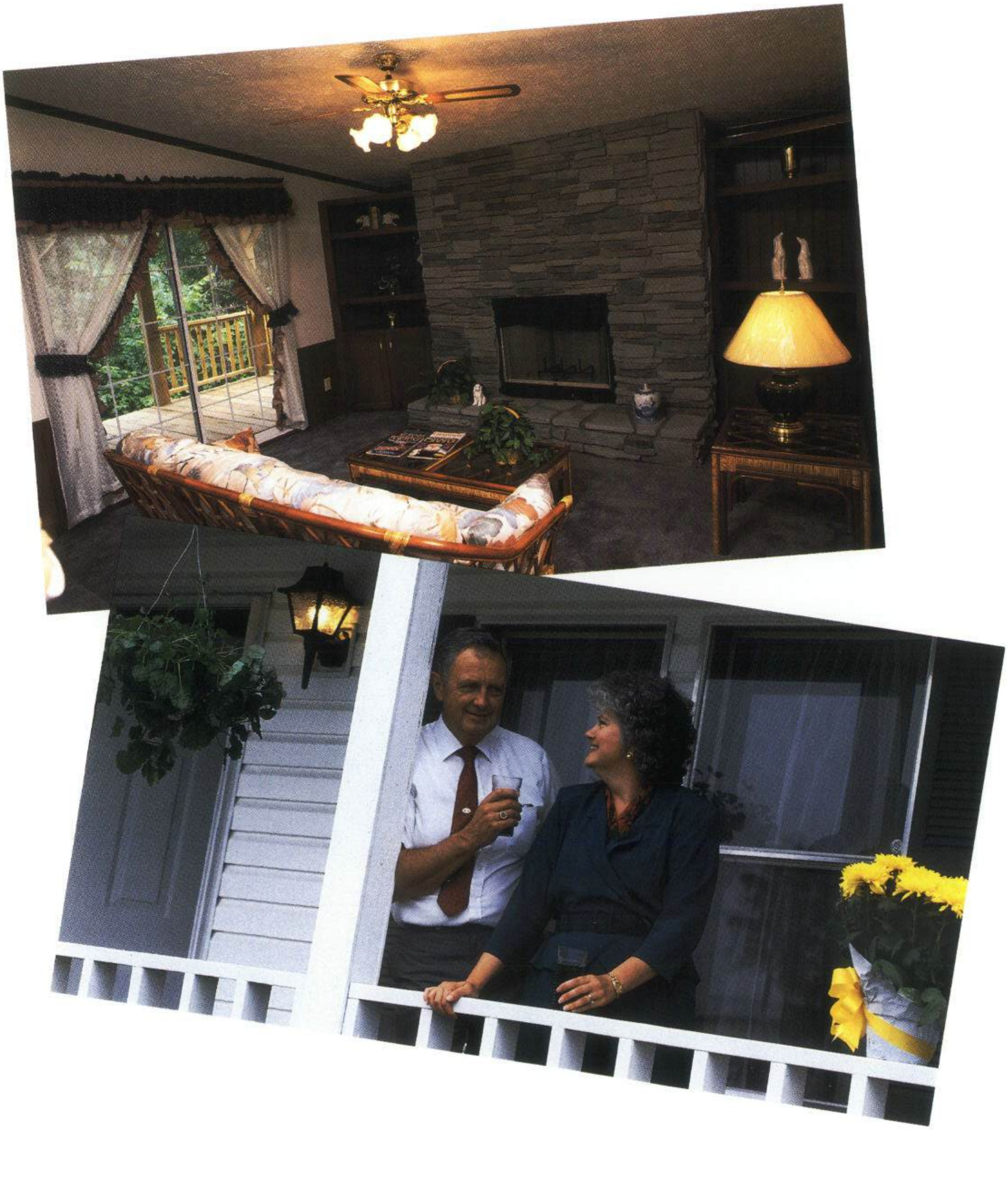


Clayton's 10 plants strive to produce the best homes on the market today. The production process requires coordination and teamwork from the plant general manager to line workers. The Halls, Tenn., plant employs 157, including (left to right) Jerry Jones, quality control supervisor; Ronnie Robertson, general manager; Ken Lowery, production manager; and Marie Mullins, quality control inspector.

Manufacturing In 1991 the Manufacturing Division posted record results in sales and profitability. Total dollar and unit sales to independent and company-owned dealers increased 6% and 7%, respectively. The dealer network grew 8% to 453 by adding 27 company-owned and eight independent dealers. These results were achieved despite an 8% drop in industry shipments in the 25-state market in which the division operates.

In calendar 1990 the Manufacturing Division jumped in ranking to the fourth largest manufacturer in the nation from sixth. The division's market share increased to 7.6% from 6.4% in the 25-state region in which the Company's 453 independent and company-owned dealers are located. This region represents 78% of the nation's manufactured housing sales.

($ in millions)	1991	1990	Percent Change
Manufacturing revenues:			
Independent dealers	$ 81.2	$ 76.8	6%
Intracompany	82.3	77.3	6
Total	$163.5	$154.1	6
Homes sold:			
Single-section	6,898	6,205	11
Multi-section	3,074	3,123	(2)
Total	9,972	9,328	7
Intracompany	(4,575)	(4,499)	2
Independent dealers	5,397	4,829	12



Key elements of the Manufacturing Division's consistent performance include:

- Gathering market feedback from its independent dealers, who also buy products from other manufacturers, and from the Retail Division, which purchases 25% of its inventory from non-affiliated manufacturers. This information allows the Company to quickly respond to changing consumer tastes and attitudes.
- Concentrating on producing a high-quality, "no defect" house with a strong relationship of value-to-price.
- Allowing employees to participate in decision-making and to benefit in terms of financial rewards and job satisfaction when plants operate efficiently and improve profitability.

The Manufacturing Division produces over 125 models in a wide price range. Retail prices range from $11,500 to $51,000 with sizes from 672 square feet to 1,904 square feet. This year the Company began making a triple-section home. Additionally, it altered three facilities to allow production of the 16-foot wide home now allowed in 21 states.

In the fourth quarter the Oxford, N.C., plant, which had been idled in December 1989, was reopened. The single-section plant produces a product line designed to fill a niche for lower-priced homes and should have a positive impact on income in fiscal 1992.

During the year the Company completed its first international sale in which 420 single-section homes were shipped in a $3 million transaction.

Next year a manufacturing facility will be added in the Southwest. This operation will supplement the Retail, Financial Services and Communities divisions already in Texas, a state in which shipments have increased 14% over the prior year and have risen in 17 of the last 18 months.

Retail The Retail Division achieved record results in sales and profitability in fiscal year 1991. Sales of 8,612 homes totalling $176 million makes the Company the largest retailer of manufactured homes in the nation.

($ in millions)	1991	1990	Percent Change
Revenues:			
New homes	$162.2	$129.7	25%
Used homes	14.1	13.0	8
Total	$176.3	$142.7	24
Homes sold:			
New single-section	4,653	3,877	20
New multi-section	2,277	1,848	23
Total – new	6,930	5,725	21
Used	1,682	1,599	5
Total	8,612	7,324	18

The division's market share increased to 8.4% from 6.3% in its 10-state marketing area in the Southeast, where 49% of the nation's manufactured housing sales occur.

The division's record performance was due primarily to a 23% increase in the average number of stores in operation during the year, including 20 locations acquired in the first quarter in South Carolina and Georgia. These sales centers were successfully integrated into the Retail Division and contributed better-than-expected results. In the second half, the Company opened five sales centers in Texas due to improving conditions and to support the acquisition of a portfolio of 7,500 manufactured housing loans located primarily in Texas and other southwestern states. Additionally, 10 other sales centers were opened and eight unprofitable locations were closed for a net gain of 27 new locations at year end. The Company constantly evaluates specific local markets and will open, acquire or close sales centers as conditions warrant.

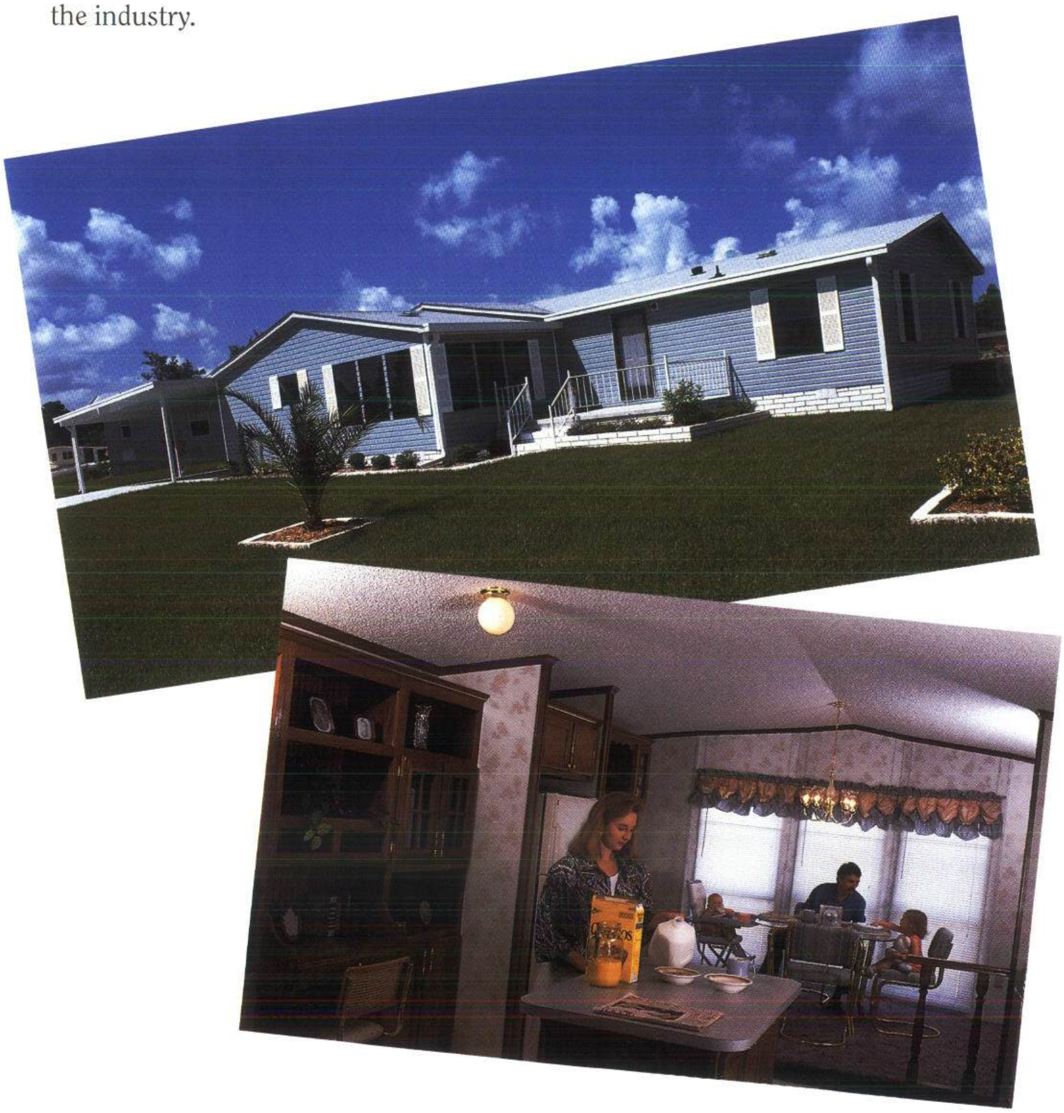
In conjunction with the finance subsidiary, the Retail Division has gained a competitive advantage by offering several unique financing alternatives not currently available to other retailers. These programs provide customers with significant interest savings and convenience. For example, the bi-weekly payment ("BUBBA") program facilitates the homeowner in making the equivalent of 13 monthly payments in a year. Because the payments are made through an electronic drafting system, the Company benefits since delinquencies, collection and administrative costs are reduced. Another program added during the year offers buyers of high-priced, multi-section homes a lower interest rate if the purchaser has an excellent credit rating.

In the pursuit of excellence and continued growth, Retail Division goals for the next year include:

- Improving or closing sales centers which do not meet profit objectives.
- Expanding the number of company-owned sales centers by 15.
- Improving gross profit margins and sales productivity while controlling costs.
- Generating optimum performance from managers and sales associates while reducing turnover.
- Recruiting the best management and sales talent inside and outside the industry.

Communities In fiscal 1991 the Communities Division developed over 550 sites in three communities bringing total sites owned to 1,960 at June 30, 1991, a 66% increase over the prior year. Sales rights to an additional 1,411 sites are reserved, bringing total sites under direct or indirect control to 3,371 at year end. On May 24, 1991, the Company purchased its joint venture partner's 50% ownership interest in nine communities.

During fiscal 1992 the Company will concentrate on increasing sales and occupancy levels at the start-up communities and improving systems and controls at all communities.



From closing the sale to assuring customer satisfaction after delivery, retail teams at 123 sales centers in 10 states use their talents to make Clayton Homes the top retailer in the manufactured housing industry. In Chester, Va., the team includes (from left) Service Coordinator Ed Lawson, Sales Center Manager Nell Smith and Sales Professional C.D. Sweetwyne.

The dream of home ownership becomes a reality for our customers every day with financing programs that make it smart to choose Clayton. Credit teams in the Company's mortgage subsidiary work together to assure a one-day turnaround on credit applications, good credit decisions and rapid, persistent follow up on past due accounts. The team serving the Company's Virginia sales centers includes (from left) Collector Amy Neff, Finance Unit Manager Joe Brawley and Credit Investigator Vada Haley.

Financial Services Record results in the Financial Services Division boosted pre-tax income 80% to $23 million from $13 million last year. The earnings increase was fueled by growth in the loan portfolio of Vanderbilt Mortgage and Finance, Inc. (VMF), the Company's wholly-owned finance subsidiary. This year's service portfolio increase consists of two components: originations and acquisitions.

($ in millions)	June 30, 1991	1990	Percent Change
Loans serviced	$607	$420	45%
Originations	156	119	31
Acquisitions	119	60	98
Number of loans (thousands)	41	29	41

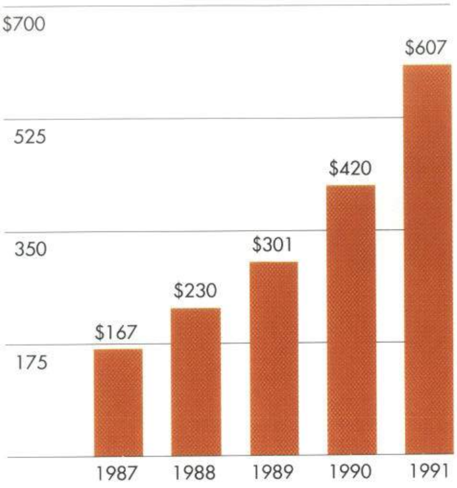
The growth in originations is due primarily to a 23% increase in the average number of company-owned sales centers. Additionally, VMF financed a higher proportion of Retail Division sales: 71% this year versus 69% last year.

The size of the portfolio grew substantially in September 1990 when VMF became servicer for a $100 million portfolio of over 7,000 manufactured housing installment contract receivables located primarily in Texas. The loans are owned by a REMIC Trust which issued $70 million of 9.4% senior certificates rated AAA by Standard & Poor's and Moody's. In accordance with generally accepted accounting principles, the notes receivable and related debt were recorded on the Company's balance sheet though the receivables are owned by the REMIC Trust.

After setting aside $14 million for repossession losses, a $16 million unearned discount will flow into income over the life of the portfolio. Unearned discount of $2.9 million from this portfolio was amortized into income in fiscal 1991. In addition the Company will receive a 5% gross servicing spread.

Loans Serviced

(in millions)



The $60 million portfolio acquired in 1989 again experienced better-than-expected collection results. As a consequence, $1 million was transferred from the reserve for future losses to the unamortized discount. In addition to normal service income, $1.8 million of unearned discount from this portfolio was amortized into income this year.

VMF delinquency and charge-off experience continues to meet objectives:

	June 30, 1991	1990
Delinquency (% over 30 days - VMF only)		
Contracts originated by VMF	2.5%	2.1%
Contract portfolios purchased	6.1	5.7
Total contracts serviced by VMF	3.4	2.6
Net losses as % of average loans outstanding		
Contracts except portfolios purchased	.3%	.4%
Contract portfolios purchased	2.6	1.3
Total contracts	.9	.6
Number of repossessions on hand	617	312

Delinquency and repossession rates are kept low by:

- Applying strict credit standards.
- Requiring liens on underlying real estate on multi-section homes.
- Using a real-time, computer-assisted collection system.
- Electronically drafting customer accounts under the bi-weekly payment plan.
- Linking each sales center manager's compensation to the performance of the loan portfolio at his or her sales center.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Results of Operations

The following table reflects the percentage changes in retail sales by the Company's sales centers and in wholesale sales to independent dealers. It also shows the percentage changes in the average number of company-owned sales centers and independent dealers. Comparative percentages are given between the fiscal years ended June 30, 1991, 1990 and 1989:

	1991 vs 1990	1990 vs 1989
Retail		
Dollar sales	+23.6%	+4.6%
Average number of sales centers	+23.3%	-3.0%
Average dollar sales per sales center	+.5%	+6.3%
Average home price	+5.1%	+3.3%

	1991 vs 1990	1990 vs 1989
Wholesale		
Dollar sales	+5.9%	+6.3%
Average number of independent dealers	+10.0%	+18.4%
Average dollar sales to independent dealers	-3.8%	-10.2%
Average home price	-5.3%	+4.2%

The following table reflects the fluctuations in interest and loan servicing revenues and financial services interest expense related to changes in interest and servicing rates and changes in the average balances of receivables owned, receivables sold and debt. Note that receivables owned or sold are the installment contract receivables related to the retail sale of homes by the Company or are purchased from independent dealers and unrelated financial institutions. Receivables owned generate interest income and are used to collateralize debt or, in certain cases, represent the Company's subordinated interest in a pool of receivables accounted for on the consolidated basis. Receivables sold generate loan service revenues and are pooled and sold. Servicing is retained by the Company in all cases. The change due to both rate and volume has been allocated to rate and volume fluctuations in proportion to the relationship of the absolute dollar amounts of the change in each. Comparative fluctuations are given between the years ended June 30, 1991, 1990 and 1989:

Rate/Volume Analysis (in thousands)

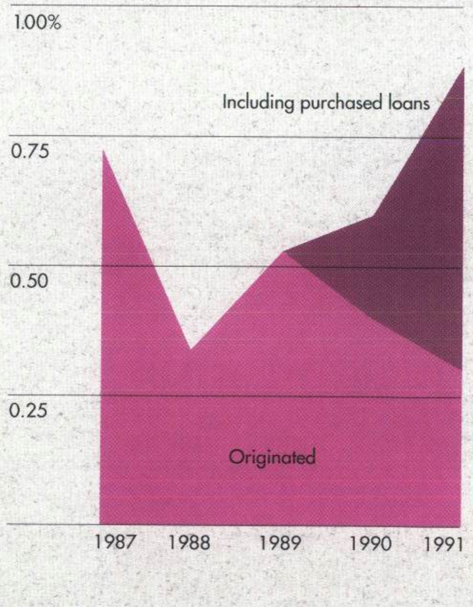
	1991 vs 1990 Increase (Decrease) Due to			1990 vs 1989 Increase (Decrease) Due to		
	Rate	Volume	Total	Rate	Volume	Total
Interest and loan servicing revenues:						
Receivables owned	$2,193	$15,255	$17,448	$(892)	$2,879	$1,987
Receivables sold	(1,132)	3,032	1,900	514	4,351	4,865
	$1,061	$18,287	$19,348	$(378)	$7,230	$6,852
Financial services interest expense	$ 238	$ 6,365	$ 6,603	$ 243	$1,441	$1,684

Fiscal 1991 Compared to Fiscal 1990

Total operating revenues for the year ended June 30, 1991, increased 23% because of the 17% increase in manufactured housing sales to $258 million from $219 million last year and the 54% jump in financial services and other income to $63 million from $41 million.

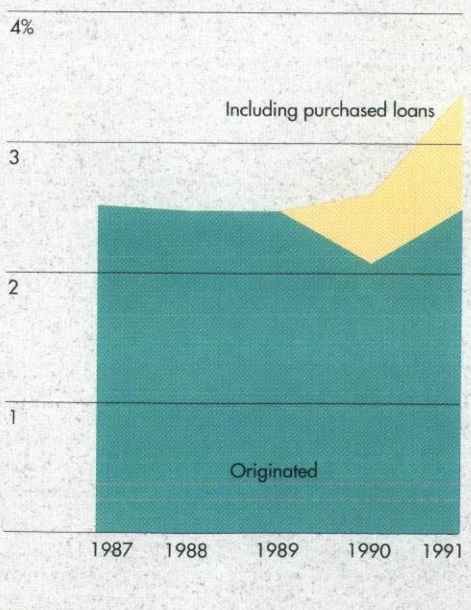
Net sales of the Retail Division rose 24% due to an 18% increase in the number of homes sold and a 5% increase in the average home price. During the year, the Company acquired or opened 35 retail locations while eight unprofitable sales centers were closed. The Company constantly evaluates specific local markets and opens, acquires, or closes sales centers as conditions warrant. The average store sales for company-owned dealerships increased .5% over the prior year while average unit sales per location declined 5%. The rise in the average home price is primarily attributable to a slight shift in the product mix toward the multi-section home and a modest increase in raw material costs.

Net Losses as a Percent of Average Loans Outstanding



Delinquency Rates (VMF)

(Percent over 30 days)



Quarterly Results (Unaudited)

(in thousands except per share data)	First Sept. 30	Second Dec. 31	Third Mar. 31	Fourth June 30	Year
1991					
Revenues	$76,631	$74,744	$70,695	$98,496	$320,566
Operating income	9,055	8,682	11,321	16,744	45,802
Net income	5,505	5,031	6,707	11,350	28,593
Earnings per share:					
Primary	.27	.24	.30	.45	1.26
Fully diluted	.24	.21	.27	.43	1.15
Shares outstanding:					
Primary	20,339	20,630	23,269	26,894	22,783
Fully diluted	25,414	25,646	25,881	28,935	26,469
Price range of common stock:					
High	$ 9.30	$ 13.88	$ 19.00	$ 22.00	$ 22.00
Low	7.50	8.10	12.25	15.50	7.50
1990					
Revenues	$62,980	$55,340	$60,758	$81,247	$260,325
Operating income	7,105	5,023	7,487	12,896	32,511
Net income	4,215	3,243	4,461	7,951	19,870
Earnings per share:					
Primary	.21	.16	.22	.39	.98
Fully diluted	.18	.15	.20	.34	.87
Shares outstanding:					
Primary	20,110	20,085	20,080	20,268	20,136
Fully diluted	25,185	25,160	25,155	25,343	25,211
Price range of common stock:					
High	$ 8.20	$ 8.00	$ 7.50	$ 9.50	$ 9.50
Low	6.80	6.90	6.30	6.80	6.30

Net sales of the Manufacturing Division to independent dealers increased 6% due to the 12% increase in the number of homes sold, partially offset by a 5% drop in the average home price to independent dealers. The decrease in the average home price is primarily attributable to a shift in the product mix toward the single-section home, partially offset by a modest increase in raw material costs. The average dollar sales to independent retail centers fell 4%.

The financial services and other income increase resulted principally from a rise in interest and servicing revenues and other financial income from the wholly-owned finance subsidiary, Vanderbilt Mortgage and Finance, Inc. (VMF).

For the year ended June 30, 1991, interest and loan servicing revenues rose $19 million, or 59%, to $52 million. The average balance of receivables owned increased 62% to $260 million with an increase in the weighted average interest rate to 15.5% from 14.2%. The average balance of receivables sold increased 33% to $287 million with a decrease in the weighted average loan service spread to 4.2% from 4.7%.

Gross profit margins improved to 31.1% compared to 29.5% last year. The increase is primarily attributable to an increase in the proportion of retail sales as a percent of total company sales. Retail sales have higher gross margins than wholesale sales. Retail sales represented 68.5% of consolidated sales this year versus 65% last year.

Selling, general and administrative expenses were 29.2% and 27.0% of sales for the years ended June 30, 1991 and 1990, respectively. The increase is primarily attributable to higher compensation costs related to the Company's growth and financial incentives, higher home delivery and set-up expenses for retail sales, increased health and liability insurance costs, and the inclusion of certain expenses related to the nine communities purchased on May 24, 1991, which were previously offset with other income under the equity method of accounting.

Financial Services interest expense rose $7 million, or 57% to $18 million. Average debt collateralized by installment contract receivables increased 54% to $172 million with an increase in the weighted average interest rate to 10.6% from 10.4%.

Provisions for credit losses and contingencies increased primarily as a result of an increase in the volume of originations of installment contract receivables through company-owned and independent dealers and an increase in the percentage of sales of the Retail Division for which the Company is at risk.

Inventories were up $21 million at June 30, 1991 from June 30, 1990 due to:

	(in millions)
Retail Division	
Net increase of 27 company-owned sales centers	$ 9.4
Increase in average inventory levels at 123 company-owned sales centers	4.9
Acquisition of nine manufactured housing communities and related inventory	3.4
Manufacturing Division	
Reopening plant	1.2
Increase in raw materials	1.6
Increase in finished goods	.5
	$21.0

Seven Year Review

(in thousands except per share and Other Data)	1991	1990	1989	1988	1987	1986	1985
Income Statement Data:							
Revenues:							
Net sales	$257,557	$219,443	$208,624	$196,110	$166,272	$152,742	$111,539
Financial services and other income	63,009	40,882	33,270	28,671	20,659	15,709	10,309
	320,566	260,325	241,894	224,781	186,931	168,451	121,848
Cost and expenses:							
Cost of sales	177,551	154,790	147,982	138,468	117,538	108,886	82,056
Selling, general and administrative	75,243	59,216	55,456	50,781	40,222	36,914	22,573
Financial services interest	18,198	11,595	9,911	10,127	6,628	5,658	3,889
Provision for credit losses and contingencies	3,772	2,213	1,539	2,010	1,863	1,600	1,600
	274,764	227,814	214,888	201,386	166,251	153,058	110,118
Operating income	45,802	32,511	27,006	23,395	20,680	15,393	11,730
Other income (expense):							
Investment income	2,341	2,918	2,868	2,627	1,829	986	1,519
Interest expense	(3,550)	(4,059)	(3,910)	(3,700)	(2,667)	(1,262)	(339)
	(1,209)	(1,141)	(1,042)	(1,073)	(838)	(276)	1,180
Income before income taxes	44,593	31,370	25,964	22,322	19,842	15,117	12,910
Provision for income taxes	(16,000)	(11,500)	(9,714)	(8,370)	(9,486)	(6,741)	(5,775)
Net income	$ 28,593	$ 19,870	$ 16,250	$ 13,952	$ 10,356	$ 8,376	$ 7,135
Net income per common share:							
Primary	$ 1.26	$ .98	$ .81	$ .70	$ .50	$ .42	$ .36
Fully diluted	1.15	.87	.73	.64	.48	.41	.36
Average shares outstanding:							
Primary	22,783	20,136	20,014	19,978	20,413	20,320	20,023
Fully diluted	26,469	25,211	25,151	25,220	23,915	21,493	20,023
Balance Sheet Data:							
Total assets	$488,817	$339,099	$294,754	$275,835	$232,159	$164,835	$114,853
Long-term obligations	227,444	177,374	163,471	157,153	132,220	85,225	49,719
Shareholders' equity	200,992	108,334	87,462	70,651	58,530	49,257	40,661
Other Data:							
Company-owned sales centers	123	96	99	100	88	86	85
Independent dealers	330	322	269	245	240	218	200
Manufacturing plants	10	10	10	10	8	7	6

Fiscal 1990 Compared to Fiscal 1989

Total operating revenues for the year ended June 30, 1990, increased 8% because of the 23% increase in financial services and other income to $41 million from $33 million last year and the 5% improvement in manufactured housing sales to $219 million from $209 million. Net sales of the Retail Division rose 5% due to a 1% increase in the number of homes sold and a 3% increase in the average home price. Net sales of the Manufacturing Division to independent dealers increased 6% due to the 4% increase in the number of homes sold and the 2% rise in the average home price. The increase in the average home price in both divisions is primarily attributable to an increase in raw material costs, partially offset by a shift in product mix away from the multi-section home. The average dollar sales per company-owned dealership increased 6% over the prior year. The average dollar sales to independent retail centers fell 10%. During the year, the Company opened three retail locations while six unprofitable sales centers were closed in markets with weak long-term outlooks.

The financial services and other income increase results principally from a rise in interest and servicing revenues and other financial income from VMF.

For the year ended June 30, 1990, interest and loan servicing revenues rose $7 million, or 26%, to $33 million. The average balance of receivables owned increased 14% to $161 million with a decrease in the weighted average interest rate to 14.2% from 14.8%. The average balance of receivables sold increased 77% to $216 million with an increase in the weighted average loan service spread to 4.7% from 4.3%. Other financial income grew primarily due to a $1 million increase in gains from the sale of loans with excess service spreads.

Gross profit margins improved to 29.5% compared to 29.1% last year. Selling, general and administrative expenses were 27.0% and 26.6% of sales for the years ended June 30, 1990 and 1989, respectively.

Financial Services interest expense rose $2 million, or 17%, to $12 million. Average debt collateralized by installment contract receivables increased 14% to $112 million with an increase in the weighted average interest rate to 10.4% from 10.1%.

Provisions for credit losses and contingencies increased primarily as a result of increased write-offs, net of recoveries, over the prior year's experience, an increase in the number of originations of installment contract receivables through independent dealers and an increase in the percentage of sales of the Retail Division for which the Company is at risk.

The $7 million decrease in inventories at June 30, 1990, from June 30, 1989, consists of:

	(in millions)
Retail Division	
Net decrease of three company-owned sales centers	$ .8
Other	.2
Manufacturing Division	
Decrease in finished goods	4.0
Decrease in raw materials	1.2
Plant closing	.8
	$7.0

Strong sales activity in the second half of the year aided management in its plans to reduce inventory levels below the prior year balances.

Fourth Quarter Results

The substantial increase in revenues and net income during the fourth quarters of fiscal 1991 and 1990 are not indicative of future operating trends but rather reflect the seasonality of the manufactured housing industry. In recent years, approximately 30% of the Company's sales have occurred in the fourth quarter.

Liquidity and Capital Resources

During fiscal 1991, the Company originated and acquired approximately $275 million of installment contract receivables for $242 million. The Company financed these originations and acquisitions primarily through the pooling and sale of approximately $106 million of installment contract receivables and the issuance by either the Company or the REMIC trust, described in Note 1 to the consolidated financial statements, of approximately $87 million of indebtedness secured by $123 million in installment contract receivables. The remainder of the funding came from short-term borrowings, cash flows and cash balances. The Company invested approximately $10 million in the acquisition or construction of properties for manufactured housing communities and approximately $5 million for the opening of company-owned sales centers and the replacement or improvement of manufacturing facilities. The Company used cash flow from operations to finance these acquisitions and improvements.

During fiscal 1991, $48 million of convertible subordinated debentures were converted to approximately 5 million shares of common stock. Additionally the Company raised $53 million of capital by issuing 900,000 shares of common stock at $16⅛ and selling $40 million of 7¾% convertible subordinated debentures due 2003. The Company anticipates that the proceeds will be utilized primarily by VMF to support increased levels of installment financing for purchasers of manufactured homes.

The Company expects to invest approximately $2 million in 1992 in the acquisition or construction of properties for manufactured housing communities, expend $3 million for the opening of company-owned sales centers, use $3 million for the purchase and improvement of manufacturing facilities and originate $180 million of installment contract receivables. The Company anticipates meeting cash needs for 1992 and thereafter with cash flows from operations, current cash balances, sale of installment contract receivables and issuing asset-backed securities and GNMA certificates.

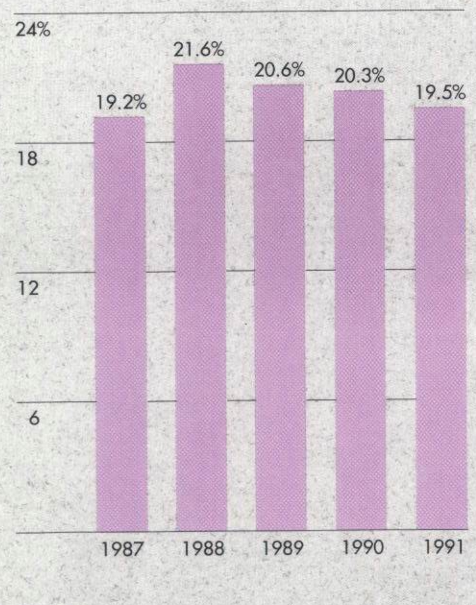
New Accounting Standard

The Financial Accounting Standards Board issued a new accounting standard that revises the accounting for income taxes. The Company has not yet adopted this standard. The accounting standard is discussed in Note 8 to the consolidated financial statements.

Effects of Inflation

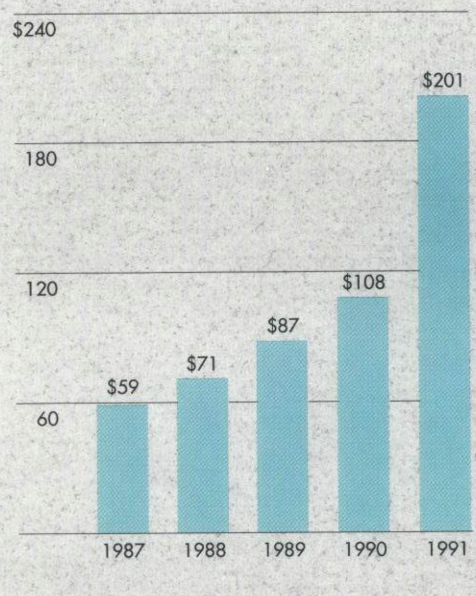
Inflation has had an insignificant impact on the Company over the past several years.

Return on Average Equity



Shareholders' Equity

(in millions)



Clayton Homes, Inc. and Consolidated Subsidiaries

Consolidated Balance Sheets

(in thousands)	June 30, 1991	1990
Assets		
Cash and cash equivalents	$ 57,531	$ 50,200
Receivables, principally installment contracts, net of reserve for credit losses of $20,511 and $8,377 (Note 6) and unamortized discount of $25,882 and $13,648	272,035	172,429
Inventories (Note 2)	60,228	39,295
Property, plant and equipment, at cost, net of depreciation and amortization (Note 3)	52,779	27,879
Equity in net assets of and advances to 50%-owned joint venture (Note 4)	–	14,879
Other assets (Note 12)	46,244	34,417
Total assets	$488,817	$339,099
Liabilities and Shareholders' Equity		
Accounts payable and accrued liabilities	$ 30,139	$ 21,867
Long-term obligations (Note 5)	227,444	177,374
Deferred income taxes	6,444	10,388
Other liabilities (Notes 6 and 12)	23,798	21,136
Total liabilities	287,825	230,765
Shareholders' equity		
Preferred stock, $.10 par value, authorized 1,000,000 shares, none issued	–	–
Common stock, $.10 par value, authorized 30,000,000 shares, issued 26,380,228 at June 30, 1991, and 16,151,280 at June 30, 1990	2,638	1,615
Additional paid-in capital	79,602	18,039
Retained earnings	118,752	90,159
Less – common stock in treasury, at cost (1990 – 199,223 shares)	–	(1,479)
Shareholders' equity	200,992	108,334
Total liabilities and shareholders' equity	$488,817	$339,099

The accompanying notes are an integral part of these consolidated financial statements.

Clayton Homes, Inc. and Consolidated Subsidiaries

Report of Independent Accountants

We have audited the accompanying consolidated balance sheets of Clayton Homes, Inc. and consolidated subsidiaries as of June 30, 1991 and 1990, and the related consolidated statements of income, changes in shareholders' equity, and cash flows for each of the three years in the period ended June 30, 1991. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Clayton Homes, Inc. and consolidated subsidiaries as of June 30, 1991 and 1990, and the consolidated results of their operations and their cash flows for each of the three years in the period ended June 30, 1991 in conformity with generally accepted accounting principles.

Coopers & Lybrand
Knoxville, Tennessee
August 6, 1991

Clayton Homes, Inc. and Consolidated Subsidiaries

Consolidated Statements of Income

	Year ended June 30,		
(in thousands except per share data)	1991	1990	1989
Revenues:			
Net sales	$257,557	$219,443	$208,624
Financial services and other income	63,009	40,882	33,270
	320,566	260,325	241,894
Costs and expenses:			
Cost of sales	177,551	154,790	147,982
Selling, general and administrative	75,243	59,216	55,456
Financial services interest	18,198	11,595	9,911
Provision for credit losses and contingencies (Note 6)	3,772	2,213	1,539
	274,764	227,814	214,888
Operating income	45,802	32,511	27,006
Other income (expense):			
Investment income	2,341	2,918	2,868
Interest expense	(3,550)	(4,059)	(3,910)
	(1,209)	(1,141)	(1,042)
Income before income taxes	44,593	31,370	25,964
Provision for income taxes (Note 8)	(16,000)	(11,500)	(9,714)
Net income	$ 28,593	$ 19,870	$ 16,250
Net income per common share:			
Primary	$ 1.26	$ .98	$ .81
Fully diluted	1.15	.87	.73
Average shares outstanding:			
Primary	22,783	20,136	20,014
Fully diluted	26,469	25,211	25,151

Consolidated Statements of Changes in Shareholders' Equity

(in thousands)	Total Shareholders' Equity	Common Stock	Additional Paid-in Capital	Retained Earnings	Treasury Stock
Balance at June 30, 1988	$ 70,651	$1,615	$18,655	$ 54,039	$(3,658)
Net income	16,250	–	–	16,250	–
Exercise of stock options	722	–	(106)	–	828
Purchase of 25,000 shares for treasury	(161)	–	–	–	(161)
Balance at June 30, 1989	87,462	1,615	18,549	70,289	(2,991)
Net income	19,870	–	–	19,870	–
Exercise of stock options	1,103	–	(510)	–	1,613
Purchase of 12,266 shares for treasury	(101)	–	–	–	(101)
Balance at June 30, 1990	108,334	1,615	18,039	90,159	(1,479)
Net income	28,593	–	–	28,593	–
Five-for-four stock split	–	400	(400)	–	–
Issuance of 900,000 shares of stock	13,829	90	13,739	–	–
Conversion of debentures, net of expenses	48,371	526	47,845	–	–
Exercise of stock options	1,415	15	591	–	809
Sale of treasury stock	450	–	286	–	164
Cancellation of treasury stock	–	(8)	(498)	–	506
Balance at June 30, 1991	$200,992	$2,638	$79,602	$118,752	$ –

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated Statements of Cash Flows

	Year ended June 30,		
(in thousands)	1991	1990	1989
Cash Flows from Operating Activities:			
Net income	$ 28,593	$ 19,870	$ 16,250
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	2,899	2,563	2,383
Deferred income taxes	(3,391)	(3,001)	(2,546)
Provision for credit losses and contingencies	3,772	2,213	1,539
(Increase) in manufactured housing receivables	(174)	(546)	(1,239)
(Increase) decrease in inventories	(20,933)	6,979	(8,461)
Increase (decrease) in accounts payable and accrued liabilities	8,272	2,215	(3,183)
Gain on sale of installment contract receivables, net of amortization	(1,063)	(1,168)	(196)
Other	(635)	8	(146)
Net cash provided by operating activities	17,340	29,133	4,401
Cash Flows from Investing Activities:			
Origination and acquisition of installment contract receivables	(242,184)	(162,521)	(109,871)
Proceeds from sales of installment contract receivables	105,619	126,345	72,431
Principal collected on installment contract receivables	43,683	28,280	28,520
Advances to 50%-owned joint venture	(10,021)	(8,605)	(6,274)
Acquisition of interest in joint venture	(1,500)	–	–
Acquisition of property, plant and equipment	(4,900)	(4,284)	(2,963)
Increase in restricted cash and investments	(12,243)	(4,497)	(6,440)
Other	3,502	1,650	1,494
Net cash used in investing activities	(118,044)	(23,632)	(23,103)
Cash Flows from Financing Activities:			
Proceeds from issuance of debt collateralized by installment contract receivables	87,018	32,000	22,856
Repayment of debt collateralized by installment contract receivables	(34,346)	(17,986)	(15,400)
Proceeds from issuance of debt by manufactured housing	40,163	–	–
Reduction in manufactured housing obligations	(494)	(111)	(1,138)
Sale (purchase) of treasury stock	450	(101)	(161)
Proceeds from capital stock issued	13,829	–	–
Proceeds from stock options exercised	1,415	1,103	722
Net cash provided by financing activities	108,035	14,905	6,879
Net increase (decrease) in cash and cash equivalents	7,331	20,406	(11,823)
Cash and cash equivalents at beginning of year	50,200	29,794	41,617
Cash and cash equivalents at end of year	$ 57,531	$ 50,200	$ 29,794

Supplemental disclosures of cash flow information:			
Cash paid during the year for:			
Interest	$ 33,094	$ 23,325	$ 21,803
Income taxes	18,066	13,939	8,335

The accompanying notes are an integral part of these consolidated financial statements.

Note 1 – Summary of Significant Accounting Policies

Consolidated Financial Statements

The consolidated financial statements include the accounts of Clayton Homes, Inc. (CHI) and its wholly-owned subsidiaries. Financial Services subsidiaries consist of Vanderbilt Mortgage and Finance, Inc. (VMF), a finance subsidiary, and Vanderbilt Life Insurance Company (VLIC), an insurance subsidiary. CHI and its subsidiaries are collectively referred to as the Company. Significant intercompany accounts and transactions have been eliminated in the financial statements. The Company operates in two principal business segments: Manufactured Housing and Financial Services.

Parent Company

Condensed financial information of CHI with VMF and VLIC accounted for on the equity basis is as follows:

Condensed Balance Sheets

	June 30,	
(in thousands)	1991	1990
Cash and cash equivalents	$ 55,448	$ 51,743
Receivables	12,707	5,447
Inventories	60,228	39,295
Advances to unconsolidated subsidiaries	65,000	15,000
Current assets	193,383	111,485
Investments in and advances to unconsolidated subsidiaries and 50%-owned joint venture	45,250	50,492
Endorsement fees receivable, less current portion	1,268	1,900
Property, plant and equipment, at cost, net of accumulated depreciation and amortization	52,779	27,879
Other assets	1,559	5,289
Total assets	$294,239	$197,045
Current maturities of long-term obligations	$ 815	$ 1,459
Accounts payable	8,279	8,110
Accrued expenses and other liabilities	17,723	11,379
Federal and state income taxes	2,845	567
Current liabilities	29,662	21,515
Long-term obligations less current maturities	49,259	51,216
Reserve for credit losses and contingencies	8,959	6,439
Deferred income taxes	5,367	9,541
Shareholders' equity	200,992	108,334
Total liabilities and shareholders' equity	$294,239	$197,045

Condensed Statements of Income

		Year ended June 30,	
(in thousands)	1991	1990	1989
Revenues:			
Net sales	$257,557	$219,443	$208,624
Equity in net income of unconsolidated subsidiaries and 50%-owned joint venture	14,264	8,557	7,113
Insurance commissions and other	13,291	9,059	8,224
Interest and dividend income	6,219	6,320	5,104
	291,331	243,379	229,065
Costs and expenses:			
Cost of sales	177,551	154,790	147,982
Selling, general and administrative	70,484	56,252	53,732
Provision for credit losses and contingencies	3,453	1,908	1,291
Interest	3,550	4,059	3,910
	255,038	217,009	206,915
Income before provision for income taxes	36,293	26,370	22,150
Provision for income taxes	7,700	6,500	5,900
Net income	$ 28,593	$ 19,870	$ 16,250

Subsidiaries

The following information is provided for the consolidated financial services subsidiaries. Such subsidiaries consist of VMF and VLIC. Through VMF, CHI arranges to finance a portion of its retail sales. VLIC reinsures risk on credit life insurance policies issued by a non-related insurance company (ceding company) in connection with credit sales. Also included below are the financial statements of the Manufactured Home Contracts 1990-1 Trust. The assets of this REMIC trust consist of a portfolio of manufactured housing installment contract receivables purchased in September 1990, when the face amount of the receivables was approximately $100,000,000. The purchase price of $70,000,000 was financed by the issuance by the trust of 9.4% senior certificates to unrelated investors. The trust also issued to the Company junior certificates in the amount of $30,000,000, which represent the residual interest in the portfolio. In exchange for the junior certificates, the Company established a $12,500,000 cash reserve fund for the senior certificates and has agreed to pay the premium for a financial guaranty policy. Condensed combined financial information for these subsidiaries is as follows:

Condensed Combined Balance Sheets

	June 30,	
(in thousands)	**1991**	1990
Installment contract receivables (pledged $189,620 and $133,981 at June 30, 1991, and 1990, respectively)	**$262,918**	$169,100
Other assets	**46,090**	24,627
Total assets	**$309,008**	$193,727
Notes payable collateralized by installment contract receivables	**$177,370**	$124,699
Unearned premiums	**3,779**	3,290
Other liabilities	**17,060**	15,126
Due to CHI	**65,079**	20,897
Shareholder's equity	**45,720**	29,715
Total liabilities and shareholder's equity	**$309,008**	$193,727

Condensed Combined Statements of Income

	Year ended June 30,		
(in thousands)	**1991**	1990	1989
Revenue	**$57,925**	$37,288	$28,869
Expenses:			
Interest expense	**22,201**	14,997	12,147
Other	**11,081**	7,991	5,662
Provision for credit losses and contingencies	**319**	305	248
Income taxes	**8,319**	4,974	3,834
	41,920	28,267	21,891
Net income	**$16,005**	$ 9,021	$ 6,978

VMF paid CHI endorsement fees of $5,941,000 in 1991; $4,898,000 in 1990; and $3,843,000 in 1989. VMF also paid interest to CHI of $3,845,000 in 1991; $3,402,000 in 1990; and $2,236,000 in 1989. Such intercompany payments have been eliminated in the consolidated financial statements but are expensed on VMF's separate financial statements to arrive at operating income for the Financial Services Division (Note 11). The finance subsidiary has loan commitments of approximately $98,000,000 from unrelated financial institutions.

VMF provides servicing for investors in installment contract receivables. Total contracts serviced at June 30, 1991 and 1990, including contracts held for investment, were approximately $607,000,000 and $420,000,000, respectively.

Income Recognition – Manufactured Housing

Sales to independent dealers of homes produced by CHI are recognized as revenue upon shipment. Retail sales are recognized when cash payment is received, or in the case of credit sales, which represent the majority of retail sales, when a down payment is received and the customer enters into an installment sales contract. Most of these installment sales contracts, which are normally payable over 36 to 180 months, are sold to VMF.

As is customary in the manufactured housing industry, CHI receives from VMF, and other financial institutions, endorsement fees over the lives of installment contract receivables in consideration for CHI's guaranty of such installment contract receivables. Additionally, CHI receives agent's commissions on physical damage and credit life insurance sold to manufactured home purchasers. Insurance commission income less an estimate of refundable commissions is recognized when insurance is written.

Income Recognition – Financial Services

Installment contract receivables originated or purchased by VMF are sold to investors or pledged as collateral to long-term lenders. VMF retains servicing in both cases. Profit (loss) on installment contract receivables sold to investors is recorded at the time of sale and represents the discounted present value of the excess (deficiency) of principal and interest to be collected during the expected normal life of the contracts over 1) the amount required to be remitted to the investors and 2) the estimated cost of servicing such contracts.

Certain of the installment contract receivables are purchased in bulk at a discount. The purchase discounts are allocated between unamortized discount and the reserve for credit losses based on management's assessment of risks existing in the portfolio. Unamortized discount is amortized into revenue over the life of the related portfolio after giving consideration to prepayments. Adjustments between the reserve for credit losses and unamortized discount are made to reflect changes in the estimated collectibility of each portfolio purchased.

Most of the installment contract receivables are with borrowers in the southern portion of the United States and are collateralized by manufactured homes.

Interest income on installment contract receivables is recognized by a method which approximates the interest method. Service fee income is recognized as the service is performed.

Inventories – Manufactured Housing

New homes and raw materials are valued at the lower of cost, using the last-in, first-out (LIFO) method of inventory valuation, or market. Previously-owned manufactured homes are valued at estimated wholesale prices, which are not in excess of net realizable value.

Property, Plant and Equipment – Manufactured Housing

Land and improvements, buildings, and furniture and equipment are valued at cost. Major renewals and improvements are capitalized while replacements, maintenance and repairs, which do not improve or extend the life of the respective assets, are expensed currently. When depreciable assets are sold or retired, the cost and related accumulated depreciation are removed from the accounts, and any gain or loss is included in earnings for the period. Depreciation is computed primarily by the straight-line method with estimated useful lives as follows:

Land improvements	3-20 years
Buildings	7-25 years
Furniture and equipment	3-10 years

Warranty Obligation – Manufactured Housing

Manufactured Housing warrants its homes against manufacturing defects for a period of one year commencing at the time of the retail sale. Warranty costs are accrued for sales to independent dealers. Warranty costs related to the sales at company-owned retail centers are not material and are recognized as incurred.

Federal Income Taxes

Deferred income taxes are provided for timing differences between financial and income tax accounting.

Reserves for Credit Losses and Contingent Liabilities

Future credit losses are provided currently for installment contract receivables. Actual credit losses are charged to the reserve when incurred. The amounts provided for such losses are determined based on the Company's historical loss experience after giving effect to current economic conditions. Management, in assessing the loss experience and economic conditions, may adjust the reserve. Adjustments are recognized currently. The Company also maintains a reserve for contingent liabilities related to guarantees of installment contract receivables sold with recourse. Reserves and the applicable provisions related to guarantees are considered as part of the Manufactured Housing business segment.

Net Income Per Share

Primary earnings per share are computed based on the weighted average number of shares of common stock outstanding during the periods presented, including common share equivalents arising from stock options. Fully diluted earnings per share have been computed assuming conversion of the Company's convertible subordinated debentures. The fully diluted computation adds to net income the interest expense (net of income tax) on the debentures.

Cash Equivalents

For purposes of the statement of cash flows, all highly liquid debt instruments purchased with a maturity of three months or less are considered to be cash equivalents.

Other

Certain reclassifications have been made to the 1990 and 1989 financial statements to conform to the 1991 presentation.

Per share and share data have been retroactively adjusted to reflect a 5-for-4 stock split effected by a 25% stock dividend in December 1990.

Note 2 – Inventories

Inventories at June 30, 1991, and 1990 are as follows:

(in thousands)	1991	1990
Manufactured homes:		
New	$43,909	$28,923
Previously-owned	10,124	5,786
Raw materials	6,195	4,586
	$60,228	$39,295

If the first-in, first-out (FIFO) method of inventory valuation had been used, inventories would have been higher by $3,377,000 and $3,063,000 at June 30, 1991, and 1990, respectively.

Note 3 – Property, Plant and Equipment

Property, plant and equipment at June 30, 1991, and 1990 are as follows:

(in thousands)	1991	1990
Land and improvements	$38,600	$15,415
Buildings	18,694	15,005
Furniture and equipment	9,066	8,161
	66,360	38,581
Less: accumulated depreciation and amortization	(13,581)	(10,702)
	$52,779	$27,879

Depreciation charged to operations was $2,782,000, $2,438,000 and $2,258,000 for each of the years ended June 30, 1991, 1990 and 1989, respectively.

Note 4 – Joint Venture

Until May 24, 1991, the Company had a 50% interest in a joint venture (Venture) engaged in developing, owning, marketing and managing manufactured housing communities. Advances to the Venture of $14,936,000 at June 30, 1990, accrued interest at the prevailing bank prime rate – 10%.

On May 24, 1991, the Company purchased its partner's 50% interest in the Venture resulting in the Company owning all the assets and assuming all the liabilities of the Venture. Prior to May 24, 1991, the operations of the Venture were accounted for on the equity basis. Subsequent to May 24, 1991, and at June 30, 1991, this investment is being accounted for as a purchase and included in the consolidated financial statements. At the time of acquisition the fair value of the assets of the Venture amounted to $34,824,000 and liabilities amounted to $33,324,000, including $24,957,000 in advances from the Company.

Note 5 – Long-term Obligations

Long-term obligations at June 30, 1991, and 1990 are summarized as follows:

(in thousands)	1991	1990
CHI		
Industrial revenue bonds:		
8.5%, monthly installments through 1999	$ 916	$ 999
8.4%, monthly installments through 1999	2,200	2,392
67% of lender's prime rate (5.7% and 6.7% on June 30, 1991, and 1990, respectively) and monthly installments through 2005	563	609
Convertible subordinated debentures:		
7.75%, due 2003	40,000	–
7.75%, due 2001	–	20,957
6%, due 2007	–	27,500
Note payable prime rate (8.5% on June 30, 1991), annual installments 1992 through 1995	5,866	–
Other notes payable	529	218
	50,074	52,675
VMF		
Debt collateralized by installment contract receivables:		
Demand note payable to Clayton Employees Savings Plan at ½% above prime	2,000	2,000
Maturing in fiscal years through:		
1991 interest average rate of 9.97%	–	1,969
1992 interest average rate of 7.56% at June 30, 1991, and 8.01% at June 30, 1990	20,000	3,324
1992 to 2005, 9.4% REMIC trust senior certificates	56,135	–
1993 to 2004 adjustable rates, 9.56% at June 30, 1991, and 10.02% at June 30, 1990; average maximum rate 10.4% at June 30, 1991, and 11.0% at June 30, 1990	94,993	112,070
2000 to 2001 adjustable rates, 8.55% at June 30, 1991, and 10.04% at June 30, 1990	4,242	5,336
	177,370	124,699
Total	$227,444	$177,374

The aggregate maturities of long-term debt of CHI for the five fiscal years subsequent to 1991 are as follows:

1992	$ 815,000
1993	868,000
1994	873,000
1995	5,129,000
1996	465,000

The debt of VMF is generally repaid based on the scheduled and prepaid principal collections of the installment contract receivables collateralizing such debt. Certain debt agreements require fixed payments which approximate the scheduled payments of the underlying installment contract receivables.

The Company has a $50,000,000 revolving credit agreement of which $17,000,000 was outstanding at June 30, 1991, and is included above in VMF debt. This line of credit bears interest at the Company's option of either 1.375% above the London Interbank Offering Rate (LIBOR) or the Banks' national lending rate. At June 30, 1991, the rate was 7.5%. The agreement also requires the Company pay an unused facility fee of .375%.

The industrial revenue bonds are collateralized by manufacturing facilities and corporate headquarters with net book values of $4,777,000.

On December 31, 1990, the Company called for redemption on January 31, 1991, of all of its 7.75% convertible subordinated debentures due 2001. Of the $20,457,000 of such debentures, $20,318,000 were converted into approximately 2,376,000 shares of common stock and $139,000 were redeemed for cash. An additional 18,000 shares of common stock were issued pursuant to an agreement with two investment banking firms underwriting the redemption.

On January 29, 1991, the Company called for redemption on February 28, 1991, of all of its 6% convertible subordinated debentures due 2007. All of the $27,500,000 of such debentures converted into approximately 2,600,000 shares of common stock. An additional 113,000 shares of common stock were issued pursuant to an agreement with two investment banking firms underwriting the redemption.

The 7.75% convertible subordinated debentures due 2003 are convertible into common stock at $19.60 per share, or 51.02 shares per $1,000 principal amount on June 30, 1991. The debentures have various covenants which restrict payments which may be made for dividends and other stock transactions.

VMF has $98,000,000 of unused loan commitments available from financial institutions. No compensating balances are required.

Certain of the long-term obligations have various covenants relating to working capital, total indebtedness and dividend payments. At June 30, 1991, the aggregate amount of earnings available for cash dividends or for repurchase of the Company stock was approximately $67,000,000.

Note 6 – Reserves for Credit Losses and Contingent Liabilities

An analysis of the reserve for losses on installment contract receivables and reserve for contingent liabilities for the years ended June 30, 1991, 1990 and 1989 is as follows:

(in thousands)	1991	1990	1989
Balance, beginning of year	$13,574	$ 8,265	$5,780
Provision	3,772	2,213	1,539
Losses, net of recoveries applicable to installment contract receivables:			
Purchased	(3,714)	(926)	(542)
Other	(1,361)	(1,478)	(1,057)
Reserves transferred to unamortized discount	(1,000)	–	–
Reserves applicable to installment contract receivables purchased	15,320	5,500	2,545
Balance, end of year	$26,591	$13,574	$8,265
Reserve for credit losses	$20,511	$ 8,377	$6,561
Reserve for contingencies	6,080	5,197	1,704
	$26,591	$13,574	$8,265

The Company is contingently liable as guarantor on installment contract receivables sold with recourse. The installment contract receivables and related contingent liabilities are shown in the table below.

Total Installment Contract Receivables (in thousands)	Contingent Liability %	Contingent Liabilities (in thousands)
June 30, 1991		
$ 48,000	100%	$48,000
159,000	11%-25%	32,000
115,000	10% and below	12,000
$322,000		$92,000
June 30, 1990		
$ 64,000	100%	$64,000
113,000	11%-25%	24,000
88,000	10% and below	8,000
$265,000		$96,000

Proceeds from receivables sold with recourse amounted to $105,619,000, $126,345,000 and $72,431,000 during 1991, 1990 and 1989, respectively.

The reserve related to contingent liabilities is included in other liabilities in the consolidated balance sheet.

Approximately 83% of the installment contract receivables owned or guaranteed by the Company have fixed rates of interest and approximately 17% are at variable rates of interest based on either the prime rate or the U.S. Treasury rates.

Approximately 98% of the Company's servicing arrangements are based on interest spreads with fixed rates or variable rates with ceilings while the remaining 2% have variable rates which provide for no minimum or maximum rate of interest.

Note 7 – Shareholders' Equity

Stock Option Plan

In 1983 and 1985, the Company established Stock Option Plans for a total of 1,258,850 shares of common stock which provide for granting "incentive stock options" or "non-qualified options" at not less than the fair market value as of the date of grant and stock appreciation rights to officers and key employees of the Company. Options are exercisable after one or more years and expire no later than 10 years from the date of grant.

Non-eligible members of the Board of Directors have granted options to purchase shares of common stock to the Company's non-management directors. The option prices were established at not less than the fair market value either as of the date of grant, or as of February 1988. The option prices and provisions for exercise were approved by shareholders. Options are exercisable after one or more years and expire no later than 10 years from the date of grant.

Activity and price information regarding the plans follow:

	Shares	Stock Option Price Range
Balance June 30, 1988	879,665	$3.22 – $ 7.68
Granted	53,125	$6.48 – $ 7.40
Exercised	(35,225)	$3.22 – $ 4.79
Canceled	(28,446)	$3.22 – $ 7.68
Balance June 30, 1989	869,119	$3.22 – $ 7.68
Granted	200,000	$6.70 – $ 6.80
Exercised	(171,816)	$3.22 – $ 5.28
Canceled	(70,805)	$4.19 – $ 7.68
Balance June 30, 1990	826,498	$3.22 – $ 7.68
Granted	273,750	$8.40 – $17.63
Exercised	(218,162)	$3.22 – $ 7.40
Canceled	(20,419)	$4.19 – $ 8.40
Balance June 30, 1991	**861,667**	**$3.22 – $17.63**

Options available for future grant at June 30, 1991 and 1990 were 47,772 and 289,288, respectively.

At June 30, 1991 and 1990, options for 270,156 and 359,854 shares, respectively, were exercisable. Options were held by 160 persons at June 30, 1991.

Stock Purchase Plan

In 1986 the Company established an employee stock purchase plan for a total of 976,563 shares of common stock which provides for granting options at 85% of the lower of the closing market price on the first trading day of the plan period or the closing market price on the last trading day of the plan period. A plan period is six months beginning each January 1 and July 1 of each plan year. Any full time employee is eligible after one year's employment. At June 30, 1991, there were 564,479 shares reserved for the plan. Information as to shares issued under this plan is as follows:

	Shares issued	Average price
1991	**84,131**	**$6.73**
1990	56,974	5.35
1989	104,295	5.19

Note 8 – Income Taxes

Components of income tax provisions for each of the three years ended June 30, 1991, 1990 and 1989 were as follows:

(in thousands)	**1991**	1990	1989
Current tax provisions:			
Federal	**$17,927**	$12,942	$10,735
State	**1,464**	1,559	1,525
	19,391	14,501	12,260
Deferred tax credit	**(3,391)**	(3,001)	(2,546)
	$16,000	$11,500	$ 9,714

Deferred income tax credits result from timing differences in the recognition of revenues and expenses for tax and financial statement purposes. The sources of these differences and the tax effect of each were as follows:

(in thousands)	**1991**	1990	1989
Reserves for credit losses and contingencies	**$ (860)**	$ (819)	$ (764)
Future servicing fees	**361**	397	67
Installment method	**(1,874)**	(1,937)	(2,025)
Insurance reserves	**(544)**	(116)	186
Other items	**(474)**	(526)	(10)
	$(3,391)	$(3,001)	$(2,546)

The provision for income taxes reflected in the financial statements differs from income taxes calculated at federal income tax rates as follows:

(in thousands)	**1991**	1990	1989
Income taxes at statutory rate	**$15,162**	$10,664	$8,828
State income taxes, net of federal benefit	**966**	1,029	1,006
Other, net	**(128)**	(193)	(120)
	$16,000	$11,500	$9,714

In December 1987, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 96, "Accounting for Income Taxes" (SFAS No. 96). The Company has not yet adopted SFAS No. 96. Adoption in the year ending June 30, 1993, is mandatory. When adopted, the standard, among other things, will result in the restatement of the Company's deferred tax balances to the statutory tax rates in effect at the time these balances are expected to be payable. Because most of these deferred taxes were recorded in prior years at tax rates higher than rates currently in effect, the Company anticipates that net income will increase in the year SFAS No. 96 is adopted, assuming no increase in statutory tax rates.

Note 9 – Employee Benefit Plans

The Company has a profit-sharing plan covering all employees who meet participation requirements. Effective July 1, 1990, the Internal Revenue Code Section 401(k) feature was added to the plan allowing employees to defer a portion of their compensation. The amount of the Company's contribution is discretionary as determined by the Board of Directors, up to the maximum deduction allowed for federal income tax purposes. Contributions amounted to $1,564,000, $700,000 and $575,000 for the years ended June 30, 1991, 1990 and 1989, respectively.

Note 10 – Commitments and Contingencies

Leases

Certain operating properties are rented under non-cancelable operating leases which expire at various dates through 2001. Total rental expense under operating leases was $1,729,000 in 1991, $1,410,430 in 1990 and $1,603,000 in 1989. The following is a schedule of minimum rental commitments under non-cancelable operating leases, primarily for retail sales centers, in effect at June 30, 1991:

1992	$992,000
1993	658,000
1994	458,000
1995	332,000
1996	235,000
1997 and thereafter	129,000

Repurchase Agreements

Institutions financing independent dealer purchases require the Company to execute repurchase agreements. As a result of these agreements, the Company is contingently liable for repurchasing units in the event of a default by the dealer to the lending institution. These agreements are customary in the manufactured housing industry, and the Company's losses in the past have not been significant.

Guarantor of Installment Contract Receivables

Please see discussion of contingencies at Note 6.

Note 11 – Industry Segment Information

The Company operates in two major business segments: Manufactured Housing and Financial Services. The Manufactured Housing segment is engaged in the production, wholesale and retail sale of manufactured homes and the development and management of manufactured housing communities. Financial Services is composed of VMF, which is engaged in retail financing of manufactured homes, and VLIC, which reinsures risk on credit life insurance policies. Operating profit is total revenue less cost of sales, operating expenses and financial interest expense. The following items have not been included in the computation of operating income: non-operating income and expenses and income taxes. Identifiable assets are those assets used in the operation of each industry segment. Corporate assets primarily consist of short-term investments.

Information concerning operations by industry segment follows:

	Manufactured Housing	Financial Services	Corporate	Total
1991				
Revenues	**$262,641**	**$ 57,925**	**$ –**	**$320,566**
Intersegment income	**9,786**	**–**	**(9,786)**	**–**
Operating income	**21,478**	**24,324**	**–**	**45,802**
Identifiable assets	**120,087**	**309,008**	**59,722**	**488,817**
Intersegment advances	**65,079**	**–**	**(65,079)**	**–**
Depreciation and amortization	**2,899**	**–**	**–**	**2,899**
Capital expenditures	**4,900**	**–**	**–**	**4,900**
1990				
Revenues	$223,037	$ 37,288	$ –	$260,325
Intersegment income	8,300	–	(8,300)	–
Operating income	18,516	13,995	–	32,511
Identifiable assets	92,349	193,727	53,023	339,099
Intersegment advances	20,897	–	(20,897)	–
Depreciation and amortization	2,563	–	–	2,563
Capital expenditures	4,284	–	–	4,284
1989				
Revenues	$213,025	$ 28,869	$ –	$241,894
Intersegment income	6,079	–	(6,079)	–
Operating income	16,194	10,812	–	27,006
Identifiable assets	91,732	176,622	26,400	294,754
Intersegment advances	26,596	–	(26,596)	–
Depreciation and amortization	2,383	–	–	2,383
Capital expenditures	2,963	–	–	2,963

Note 12 – Other Assets and Liabilities

At June 30, 1991 and 1990 other assets and liabilities consisted of:

(in thousands)	**1991**	1990
Other assets		
Restricted cash and investments	**$30,624**	$18,381
Interest receivable	**10,228**	6,597
Deferred debt costs	**3,793**	2,520
Other	**1,599**	6,919
	$46,244	$34,417
Other liabilities		
Interest payable	**$ 7,938**	$ 8,928
Reserve for contingencies	**6,080**	5,197
Escrow deposits	**5,260**	3,539
Unearned insurance premiums	**3,779**	3,290
Other	**741**	182
	$23,798	$21,136

Corporate Officers

James L. Clayton
Chairman of the Board,
Chief Executive Officer, President

E. Tyler Kelly
Executive Vice President –
Manufacturing Division

Richard B. Ray
Executive Vice President – Finance
Chief Financial Officer

Timothy W. Williams
Executive Vice President –
Vanderbilt Mortgage and Finance, Inc.

James R. Conner
Vice President – Computer Services

William O. Henry
Secretary – Treasurer

Shareholder Information

Counsel
Bernstein, Stair & McAdams
Knoxville, Tennessee

Special Counsel
Bass, Berry & Sims
Nashville, Tennessee

Registrar and Transfer Agent
Trust Company Bank
P.O. Box 4625
Atlanta, Georgia 30302
(404) 581-1579

Trustee for Debentures
Third National Bank in Nashville
P. O. Box 2544, Uptown Station
Nashville, Tennessee 37244
(615) 748-4742

Independent Accountants
Coopers & Lybrand
Knoxville, Tennessee

Form 10-K
Clayton's Form 10-K Annual Report to the Securities and Exchange Commission is available without charge to shareholders and debenture holders upon written request to:

Chief Financial Officer
Clayton Homes, Inc.
P.O. Box 15169
Knoxville, Tennessee 37901

Common Share and Debenture Information
The Company's common shares (symbol CMH) and 7.75% convertible subordinated debentures are listed on the New York Stock Exchange.

Shareholders
There were approximately 5,600 beneficial holders of common stock on June 30, 1991.

Annual Meeting
The annual meeting of shareholders will be held on November 12, 1991 at 10:30 a.m. (EST) at the Clayton Building of The Knoxville Museum of Art in Knoxville, Tennessee. Shareholders of record at close of business on September 24, 1991 will be entitled to vote.

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Board of Directors

Standing, left to right: E. Tyler Kelly, Joseph Stegmayer, Richard Ray, William Lomicka.
Seated: B. Joe Clayton, James Clayton, Wallace Rasmussen.

James L. Clayton
Chairman of the Board,
Chief Executive Officer, President
Director, Dollar General Corporation

B. Joe Clayton
Chief Executive Officer,
Clayton Motors, Inc. and
affiliated companies
Director, Valley Fidelity Bank and
Trust Company

E. Tyler Kelly
Executive Vice President –
Manufacturing Division

William H. Lomicka[1] [2]
President, Mayfair Capital
Director, Citizens Financial Corporation
and Vencor, Inc.

Wallace N. Rasmussen[1]
Director, Sovran Bank Nashville,
Shoney's Inc. and
Dollar General Corporation

Richard B. Ray
Executive Vice President – Finance

Joseph H. Stegmayer[1] [2]
Vice President, Chief Financial Officer,
Treasurer and Director of
Worthington Industries, Inc.
Director, The Cardinal Group of
Funds, Inc. and The Buckeye Savings
and Loan Company

[1] Audit Committee
[2] Compensation Committee

Clayton Homes, Inc.
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