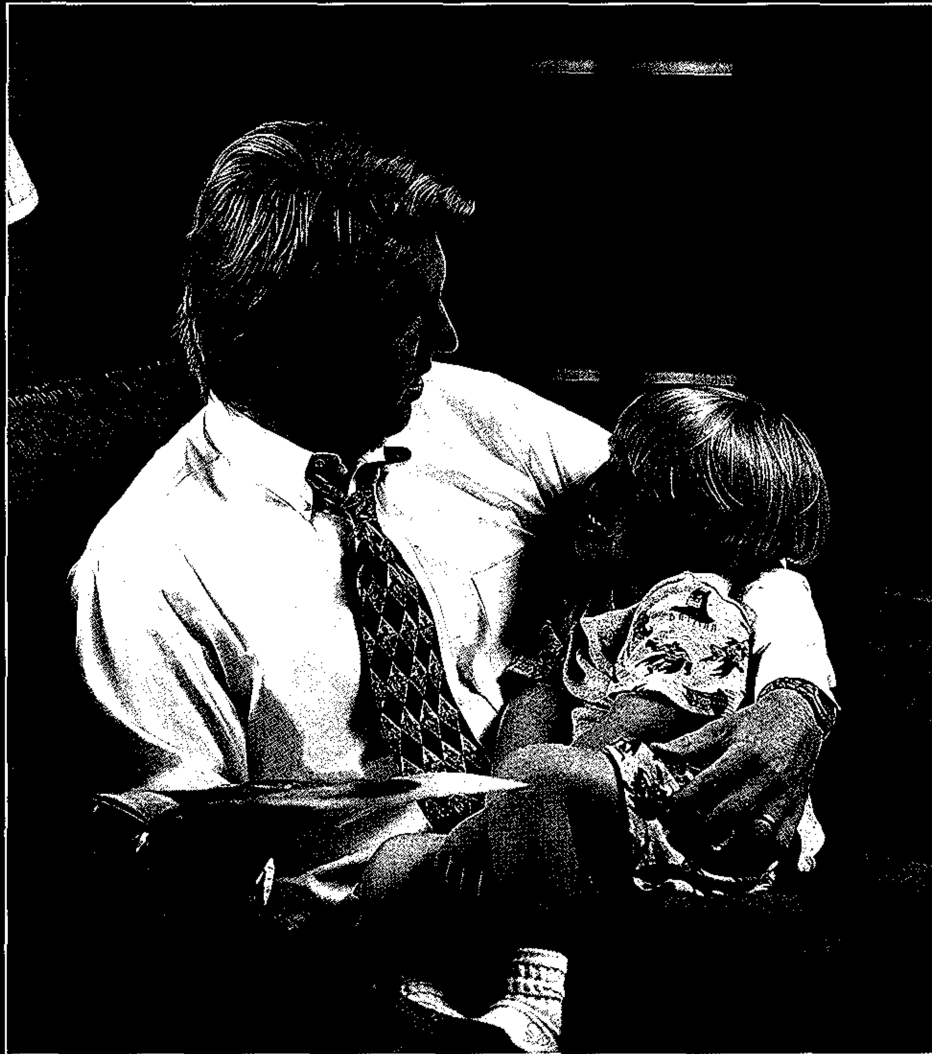
Clayton Homes, Inc.



We Build Dreams

15 Years as a Public Company

1998 Annual Report

COMPANY PROFILE

Clayton Homes, Inc. is a vertically integrated manufactured housing company headquartered in Knoxville, Tennessee. Employing more than 6,700 people and operating in 28 states, the Company builds, sells, finances and insures manufactured homes, and owns and operates residential manufactured housing communities.

The ***Manufacturing*** group is a leading producer of manufactured homes with 18 plants supplying homes to 1,046 independent and Company-owned retail centers.

The ***Retail*** group sells, installs, and services factory-built homes. At year end, there were 273 Company-owned retail centers in 21 states.

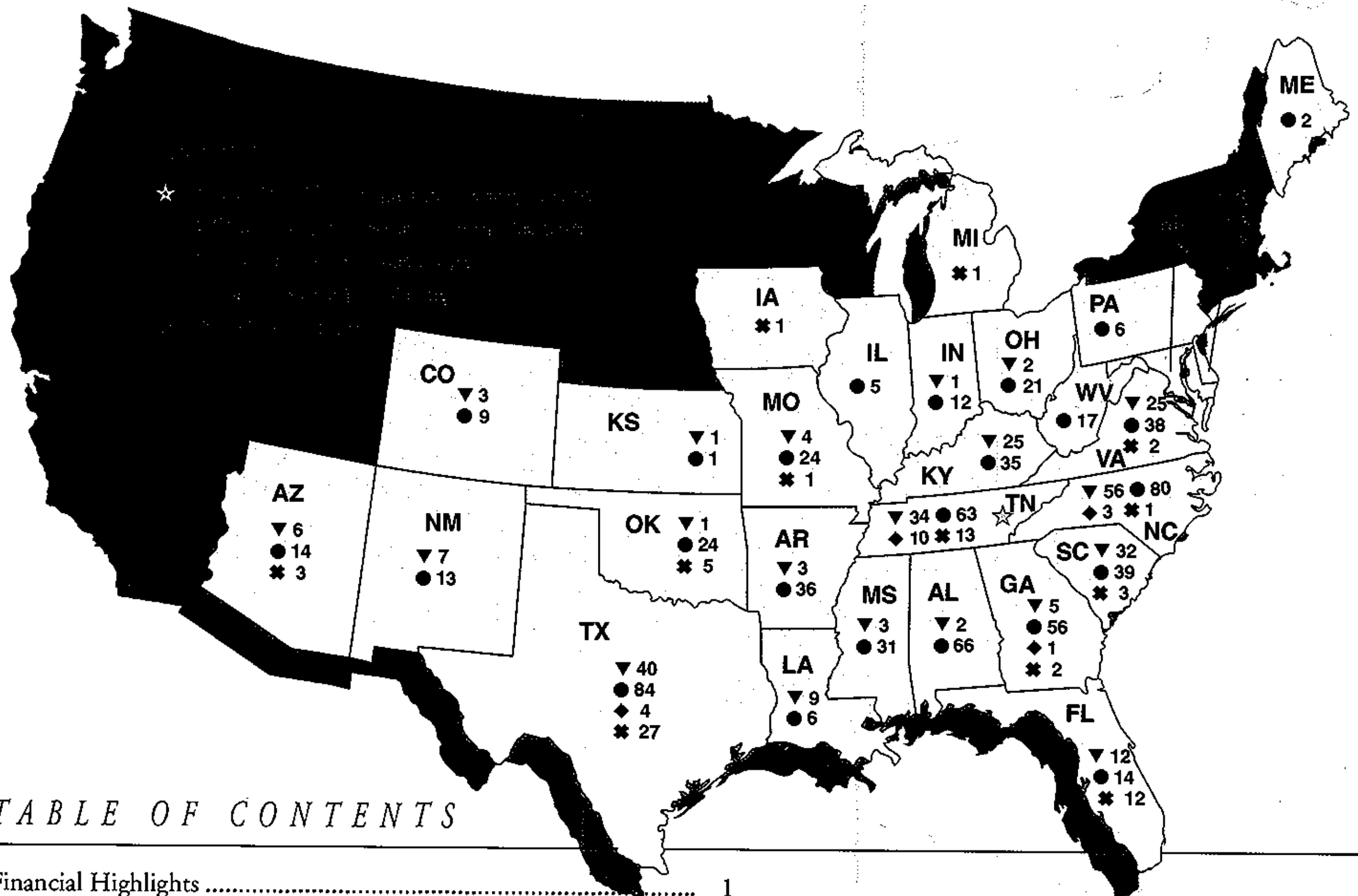
Financial Services provides financing and insurance for homebuyers of Company-owned and selected independent retail sales centers through Vanderbilt Mortgage and Finance, a wholly-owned subsidiary.

The ***Communities*** group owns and operates 71 manufactured housing communities with 18,964 home sites in 12 states.

OUR COVER

Owning your own home is the "Great American Dream." Last year your Company sold 32,358 homes, helping that many families realize their dreams.

A new multi-sectional home called "The Dream" features a cozy stacked-stone fireplace, garden tub with separate shower, and vaulted ceilings throughout.



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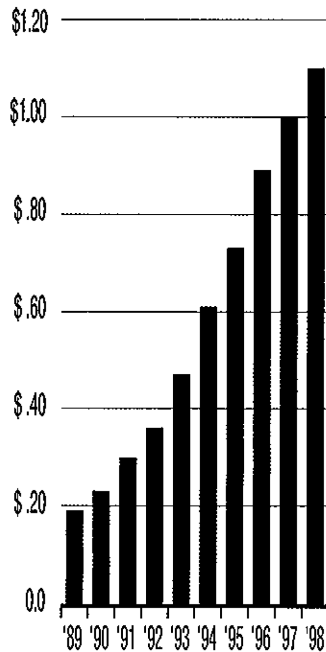
FINANCIAL HIGHLIGHTS

(dollars in thousands, except per share)	Year Ended June 30, **1998**	1997	Percent Change
Income Statement Data:			
Revenues	**$1,127,779**	$1,021,703	10%
Income before income taxes	**222,100**	192,700	15%
Net income	**137,700**	119,500	15%
Earnings per share:			
Basic	**1.16**	1.01	15%
Diluted	**1.15**	1.00	15%
Dividends per share	**$.080**	$.076	5%
Balance Sheet Data:			
Total assets	**$1,457,757**	$1,045,761	39%
Shareholders' equity	**$ 881,019**	$ 754,526	17%
Return on average shareholders' equity	**16.8%**	17.0%	
Portfolio Data:			
Loans serviced	**$2,925,000**	$2,044,000	43%
Delinquency % (over 30 days):			
Originated contracts	**2.0%**	2.0%	
All contracts	**3.3%**	2.1%	
Net losses as a % of average loans outstanding:			
Originated contracts	**0.8%**	0.0%	
All contracts	**0.8%**	0.2%	
Other Data:			
Total floors sold	**45,006**	43,290	4%
Total homes sold	**32,358**	32,714	-1%
National market share	**8.0%**	8.0%	
Manufacturing plants	**18**	17	6%
Independent retailers	**702**	663	6%
Company-owned retail centers	**273**	245	11%
Communities	**71**	67	6%
Community home sites owned	**18,964**	17,797	7%
Personnel Count	**6,703**	5,991	12%

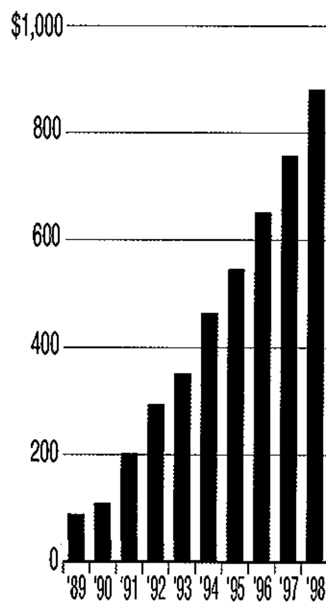
Where appropriate, data in this report has been adjusted for the five-for-four stock split paid December 11, 1996.

TO OUR SHAREHOLDERS

Earnings Per Share
(diluted)



Shareholders' Equity
(in millions)



We are pleased to report the 15th year for Clayton Homes as a public company and our 18th consecutive record year with $1,127,800,000 in revenues and $137,700,000 in net income. Net income has increased at a rate of 29 percent since the initial public offering in June 1983, while revenues have risen at an annual compound rate of 20 percent. Earnings per share have grown 23 percent annually. Shareholders who purchased 1,000 shares in June 1983 for $16,000 have 14,551 shares after 12 five-for-four stock splits worth $276,469 at June 30, 1998 – an annual return on investment of 21 percent.

The fourth quarter marked the Company's 48th consecutive record quarter, while achieving positive comparisons in 60 out of the 61 quarters since the initial public offering. Few public companies have delivered the predictable growth your Company has enjoyed during the last 15 years, which places us as number one in all of housing based on the most important indicator – net income.

The Company's 15 record years can be attributed to talented and focused team members who have worked diligently and prudently to steadily grow the operating groups in varying markets. Since June 1983, the expansion includes:

- *Company retailers from 39 to 273*
- *Independent retailers from 109 to 702*
- *Manufacturing plants from 3 to 18*
- *Communities from 0 to 71*
- *Annual mortgage originations from $14 million to $802 million*
- *Service portfolio from $27 million to $2.9 billion*
- *Capital investments from $405,000 to $62 million*
- *Shareholders' equity from $28 million to $881 million*
- *Market capitalization from $86 million to $2.3 billion*
- *Team members from 800 to 6,700*

Growth among the Company's four groups has varied from quarter to quarter and year to year, but the synergies involved in this very difficult to execute concept have allowed the Company to consistently achieve records. While one group transitions through a period of slower growth, another group enjoys high growth. The challenge of balancing and maintaining the model should not be underestimated – especially since other industry lenders have taken multiple charges to restate their securitization models. Your Company has taken a conservative approach to growth and risk management, as it will in the future. We will continue to refine and improve our structure and concept and will not focus exclusively on market share growth or the number of Company-owned stores.

We were disappointed that our target for retail stores this year was missed; we felt it was not in the long-term interest of our shareholders to pay unreasonably high premiums for new retail stores or other acquisitions. To facilitate growth for 1999, the Retail group was restructured into four zones, each supervised by a group vice president with 15 or more years of industry experience. Twenty regional managers will report to the four vice presidents who together have more than 40 years of distinguished service with Clayton.

During fiscal 1998, we leveraged the balance sheet to make strategic portfolio acquisitions and to improve the return on shareholders' equity. Debt obligations increased from $23 million to $248 million, representing primarily our five-year LIBOR-based revolving credit facility completed in

May. Return on equity was 17 percent for the year, even though shareholders' equity increased $126 million to $881 million at year end.

Clayton Homes' goals for 1999 include:

- *Growing the number of Company stores beyond 300*
- *Expanding our independent retailer network, especially in the Southwest*
- *Opening the Arizona plant in the second quarter and achieving profitability in the third quarter*
- *Strengthening the Communities operating team*
- *Developing attractive and profitable communities*
- *Rolling-out an interactive internet communications system*
- *Increasing Return On Equity*

Clayton Homes' operating philosophy is effectively captured in our mission statement: "We create and market high value products and services for the benefit of Clayton Stakeholders: Customers, Shareholders, and Team Members." The Company's value statement includes:

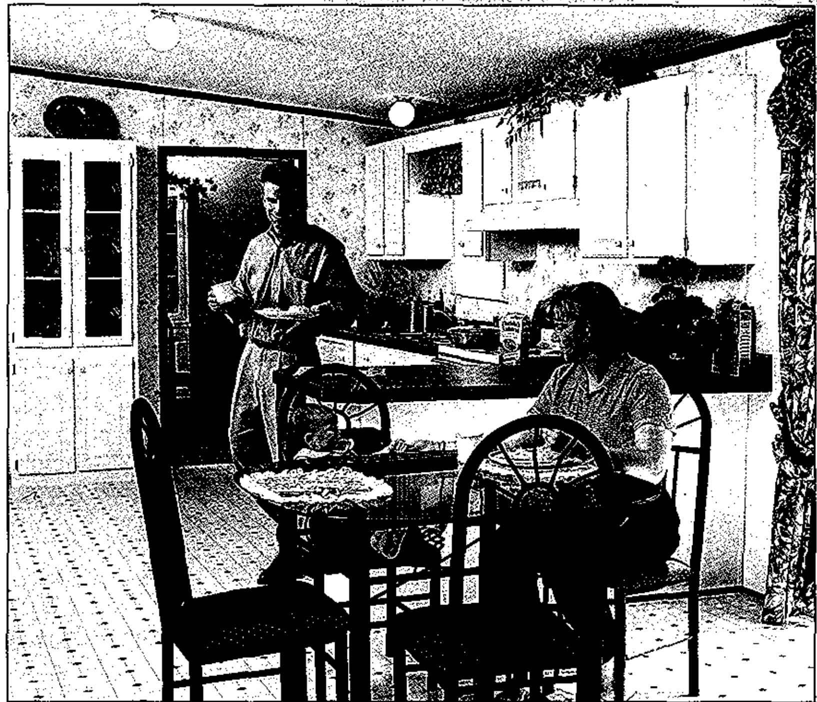
- *Striving to exceed customer expectations*
- *Delivering excellence through standardization and process improvement*
- *Embracing change and leveraging it as a strategic advantage*
- *Believing we can only expect what we are willing to inspect*
- *Supporting neighborhoods where we live and work*

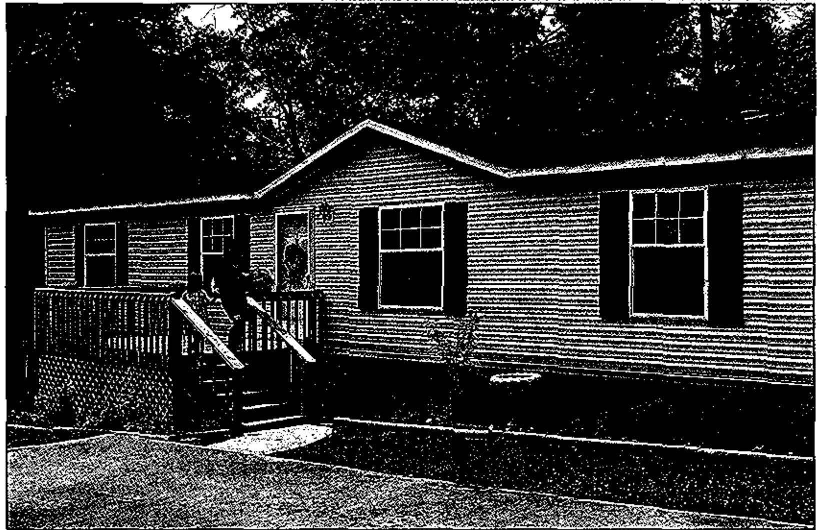
We want to express gratitude to our shareholders and team members who delivered record results for 1998 and for the last 15 years. We look forward to announcing new records in 1999 and beyond.

Sincerely,

James L. Clayton

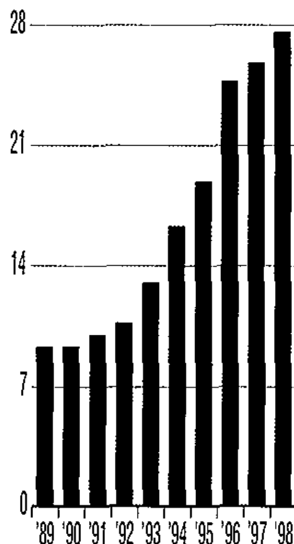
Kevin T. Clayton



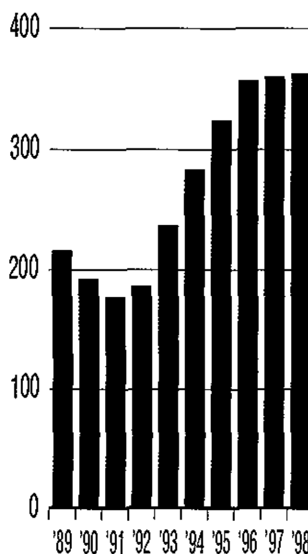


MANUFACTURING

Clayton Homes Built
(in thousands)



Industry Shipments
(in thousands)



Your Manufacturing group achieved record performance in sales revenue, productivity, quality, and income in 1998. Revenue grew to $600 million, up 15 percent from last year. The number of floors produced increased 14 percent to 39,892, and home production increased 7 percent to 27,640.

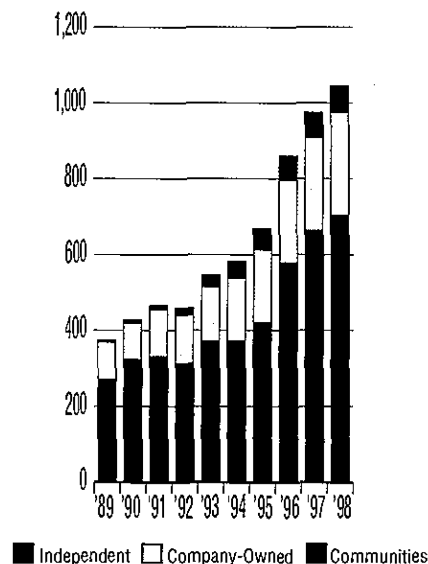
The Company's distribution now reaches 28 states via 1,046 highly valued, long-term retail partners including 702 independents, 273 Company-owned sales centers, and 71 communities. The feedback we receive from this geographically diverse family of retailers guides our rapid response product development and manufacturing teams in providing homes in tune with current market demands.

Multi-section homes represented 44 percent of our shipments for the fiscal year, up from 35 percent, as we keep pace with the industry's shift to multi-section homes. Single-section home production remains strong and will continue to be an important component of our strategic focus. New plants will be designed and located to support the growing multi-section segment.

The Sulphur Springs, Texas plant set new levels of accomplishment. Certification was achieved in August 1997, and the team exceeded expectations in terms of productivity, quality, and profitability. The plant was built within budget and was profitable in its second month of operation. The current production rate is 10 floors per day.

The newest and 19th plant, scheduled for completion in the second quarter, is 15 miles northwest of Phoenix in El Mirage, Arizona. High value, low priced, multi-section homes similar to those built at the Sulphut Springs and Appalachia plants will be manufactured there. Our interior design team will provide the distinctive visual features expected by

Distribution Centers



	June 30, 1998	1997	Pct Chg
Sales (in millions):			
Independent dealers	**$311.9**	$288.0	8%
Intercompany*	**287.4**	232.3	24%
Total	**$599.3**	$520.3	15%
Homes built (units):			
Single-section	**15,596**	16,697	-7%
Multi-section	**12,054**	9,133	32%
Total	**27,650**	25,830	7%
Intercompany*	**(12,922)**	(11,455)	13%
Independent retailers	**14,728**	14,375	2%

**Represents sales to the Company's Retail and Communities operations.*

homebuyers in the desert Southwest.

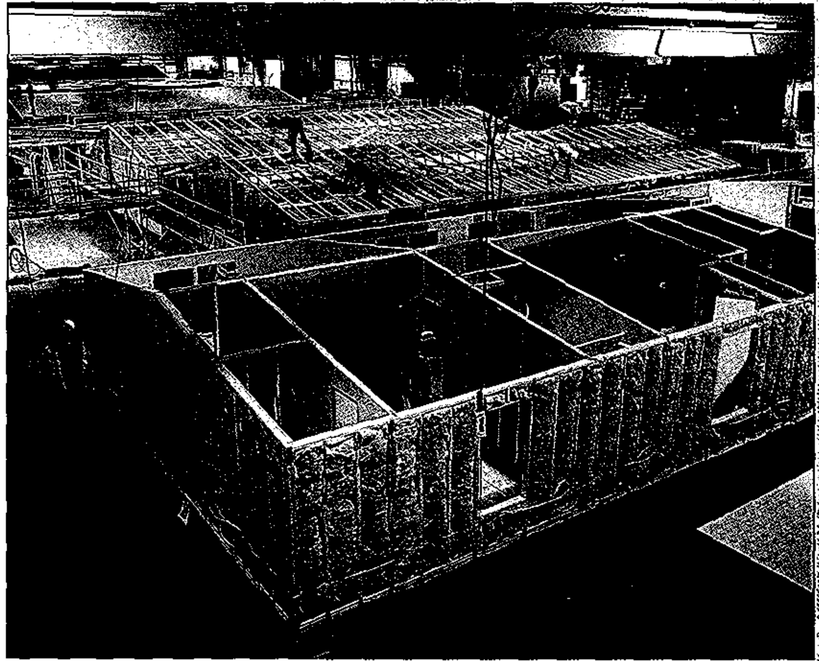
The Commercial Building Million Dollar Business Unit (MBU) experienced good growth in its start-up year. Referrals from satisfied customers, direct mail, advertisements in trade publications, and other marketing programs led to a book of business at year end that will ensure favorable growth for the MBU's second year. The internet delivered several productive leads for temporary classrooms and portable retail office space.

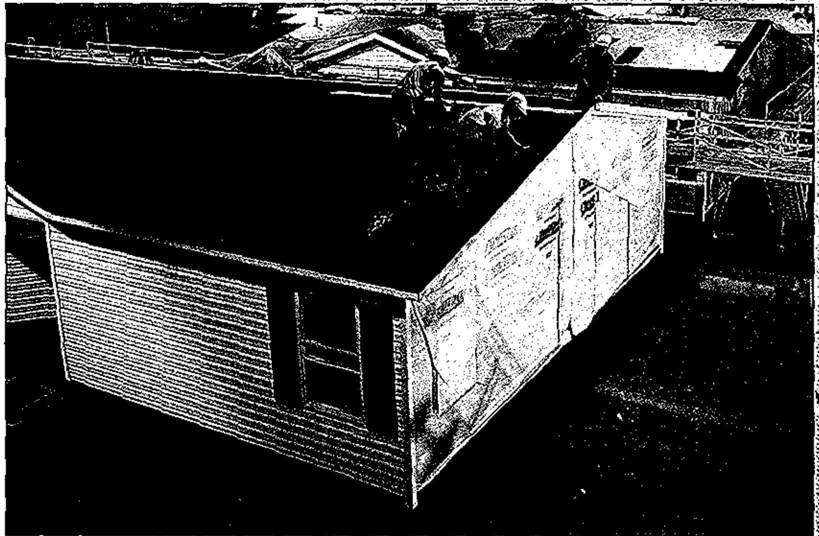
In December, our group launched a successful national home campaign called The Dream, reflecting the Clayton slogan, "We Build Dreams." The campaign promotes a high value, fully equipped multi-section home packaged with a unique financing program from Vanderbilt Mortgage. The Dream, supported with a comprehensive marketing program, is primarily directed toward the first-time buyer. Eight plants manufacture The Dream, blanketing our entire market area. When the success of the program was confirmed, a complementary single-section home called The Sensation was introduced. Currently, six plants are producing The Sensation, which is being enthusiastically received by our retailers and their customers.

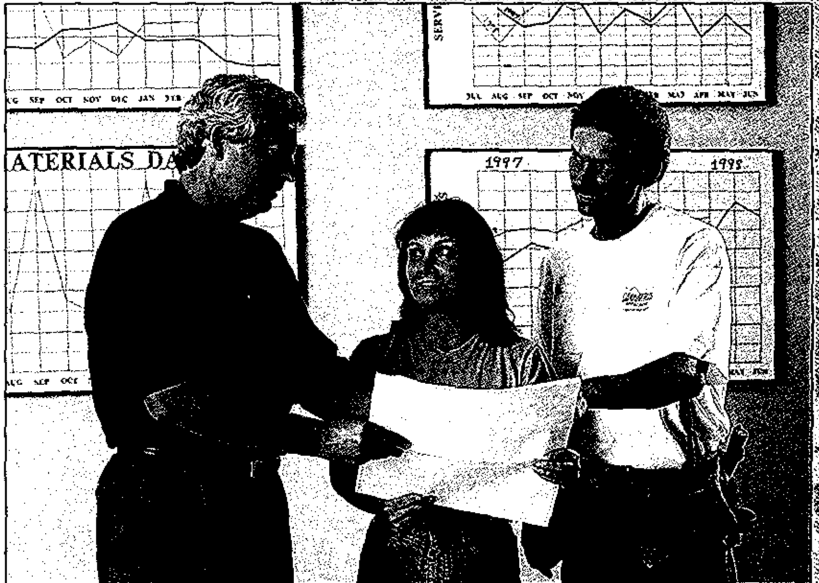
Material cost reduction through process improvement, component standardization, and partnering with our valued vendors will continue to be a priority. Our past focus on capital investment to improve productivity has resulted in increased operating capacity utilization to 86 percent at year end. Continued investments to improve operational efficiency and profitability will be made, while ergonomically improving the process facilities for our personnel.

The FastTrack Management Training Program introduced in early 1997 has delivered educated and experienced personnel who have accepted challenging roles in our new and expanded plants. Building bench strength from within enhances our cultural approach to patiently and consistently building new teams that support our long-term values and work ethic.

In fiscal year 1999, we will open the new El Mirage plant and expect to announce the site location of our 20th plant. Your Manufacturing group will continue to emphasize the Company's goal of building high quality housing at extremely attractive price points. With dedicated teams and excellent facilities, the group is well-positioned to rapidly respond to customer expectations while utilizing the Company's growing distribution base to capture an increasing share of the market.

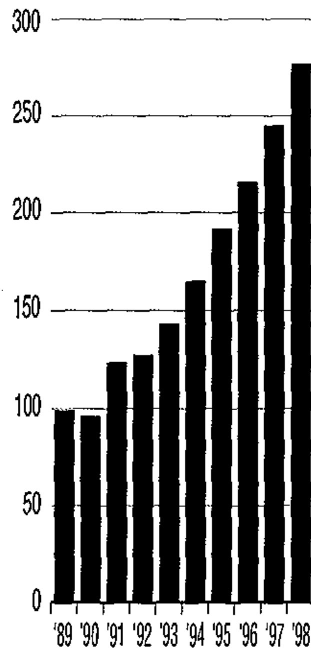




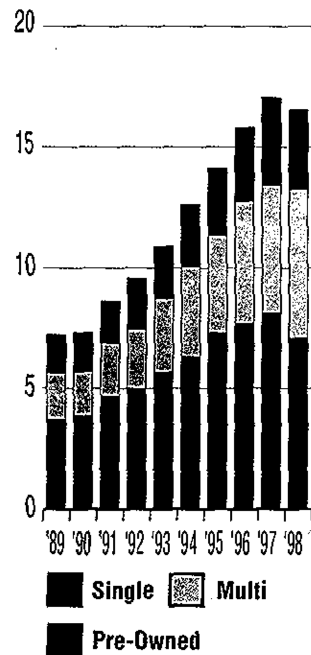


RETAIL

Company-Owned Retail Centers



Homes Retailed
(in thousands)



Fiscal 1998 represented another year of revenues and earnings growth for the Retail group. Our conservative, yet opportunistic approach is noteworthy, given industry trends that showed competitors venturing into areas and aligning themselves with partners outside their core competencies. During the year, analysts noted heightened industry activity among those seeking to emulate the Clayton vertical integration model. We chose a steady course, refusing to deviate from our long-term strategic goals.

During Clayton Homes' 15 years as a public company, the Retail group has navigated many market trends. In 1983, the group sold 3,354 homes, generating more than $42 million, while multi-section homes comprised only 19 percent of the product mix. Last year, our 21st consecutive year of record growth, produced revenues of $535 million from the sale of more than 16,500 homes. This year, the number of multi-section homes sold by the Company approached the level of single-section homes.

The heightened demand for multi-section homes is credited to several factors: affordability, lower interest rates, the increasing price of site-built homes, and the efforts of our dedicated sales representatives who strive to match the needs and expectations of our buyers. As the

	June 30, 1998	1997	Pct Chg
Sales (in millions):			
New homes	**$501.7**	$459.3	9%
Used homes	**33.2**	37.7	-12%
Total	**$534.9**	$497.0	8%
Homes sold (units):			
New single-section	**7,099**	8,113	-12%
New multi-section	**6,151**	5,312	16%
Total new	**13,250**	13,425	-1%
Used	**3,287**	3,621	-9%
Total	**16,537**	17,046	-3%

affordability and quality of manufactured housing continues to improve, the Retail group will respond to the ever-increasing demand for multi-section homes.

The Retail group opened 33 distribution outlets in 1998 and closed five under-performing outlets. Since 1983, the group increased the number of sales centers from 39 to 273. To ensure future expansion, the group has devoted additional resources to the development of new sales centers in attractive markets and to the acquisition of independent retailers when available at reasonable prices.

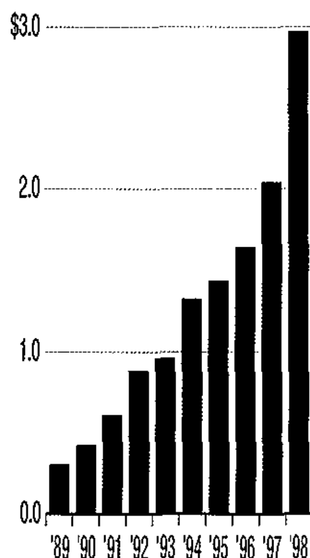
To facilitate managed growth, the Retail group realigned sales regions to better accommodate new and established sales centers. Additional regional managers were promoted to better support our steady growth, provide increased field training, and to ensure customer satisfaction.

The past year marked the introduction of Clayton Homes' first nationwide sales promotion. The campaign spotlights The Dream, a multi-section home, and its single-section counterpart, The Sensation, combining for the first time a furniture/appliance/decor package, standard pricing, and special financing options. This teaming success of the Retail, Manufacturing, and Financial Services groups distinguishes us from the competition and confirms our position as an industry leader.

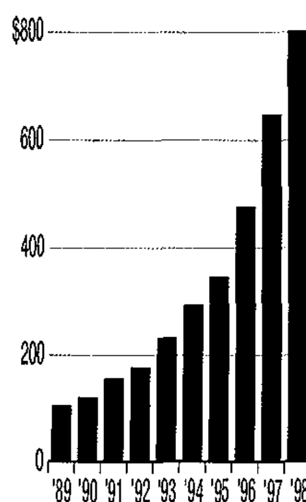
The road ahead will present ever-increasing challenges and opportunities for the Retail group. Selling good homes to good people on good sites continues to be our model for success.

F I N A N C I A L   S E R V I C E S

Loans Serviced
(in billions)



Loan Originations
(in millions)



1998 was an exciting year for the Financial Services group as new records for loan origination, servicing, securitization, and written insurance premiums were achieved. While recently added components to the group experienced substantial expansion during the year, particularly the Million Dollar Business Units (MBUs) and CMH Insurance, Financial Services evolved into a comprehensive structure that will continue to grow. Vanderbilt Mortgage and Finance's loan originations for 1998 totaled $802 million, of which the MBUs generated $269 million, and net written insurance premiums totaled $51 million.

In 1983, the year of our initial public offering, Vanderbilt's servicing portfolio totaled $27 million. Fifteen years later, the portfolio has grown to $2.9 billion. This was our second full year of quarterly securitizations as we sold $899 million in mortgage receivables in the public markets. The variable rate tranches totaled $278 million.

Portfolio acquisition activity was brisk in

	June 30, 1998	1997	Pct Chg
Loans serviced (in millions):			
Originated and purchased loans serviced	**$2,593**	$1,910	36%
Master servicing contracts	**332**	134	100+%
Total	**$2,925**	$2,044	43%
Loans serviced (# of loans in thousands):			
Originated and purchased loans serviced	**109**	87	25%
Master servicing contracts	**17**	15	13%
Total	**126**	102	24%
Originations (in millions):			
Company-owned	**$ 539**	$ 489	10%
Independent	**263**	158	66%
Total	**$ 802**	$ 647	24%
Acquisitions (in millions)	**$ 516**	$ 197	100+%

	June 30, 1998		1997
	***Inc. Access**	**Exc. Access**	
Delinquency (% over 30 days - VMF only):			
Contracts originated by VMF	**2.0%**	**2.0%**	2.0%
Contract portfolios purchased	**8.7%**	**3.3%**	2.7%
All contracts	**3.3%**	**2.2%**	2.1%
Net losses as % of average loans outstanding:			
Contracts originated by VMF	**0.8%**	**0.8%**	0.0%
Contract portfolios purchased	**1.8%**	**1.7%**	1.8%
Total contracts	**0.8%**	**0.8%**	0.2%
Number of repossessions on hand:			
Originated by VMF	**1,229**	**1,229**	885
Contract portfolios purchased	**453**	**114**	52
Total repossessions	**1,682**	**1,343**	937

**In the month of May, the Company purchased $245 million in loans from Access Financial Lending Corporation (Access) and contracted to service an additional $267 million – for a total of $512 million in servicing.*

1998. The largest acquisition occurred late in the fourth quarter when Vanderbilt Mortgage signed an agreement with Access Financial Lending Corporation regarding $512 million in manufactured housing loans. Vanderbilt purchased $245 million in loans from Access and began servicing a $267 million portfolio that Access had originated and securitized.

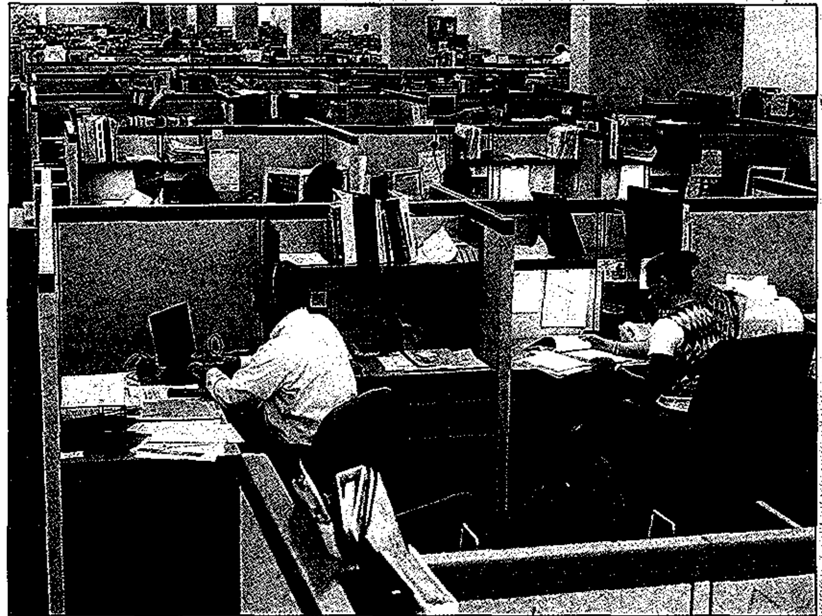
In 1998, Vanderbilt and the MBUs continued to enjoy a relatively low cost of funds attributable to their historical experience, reputation as a premier servicer, and to the low interest rate environment. The Company's diligent collection efforts resulted in a delinquency rate of 1.98 percent for the year, as the group again demonstrated its ability to provide effective mortgage servicing.

The MBUs produced one-third of the total loan originations last year, as their originations increased more than 70 percent. Financial Services now has six MBUs up and running: Direct Lending, Private Mortgages, Independent Lending, Commercial Units, Home Security, and Insurance Marketing. MBUs are modeled to leverage the core competencies of Financial Services and to produce profit potential of at least $1 million per year by the end of their third year. They must have a growth potential in excess of the Company's expected growth rate.

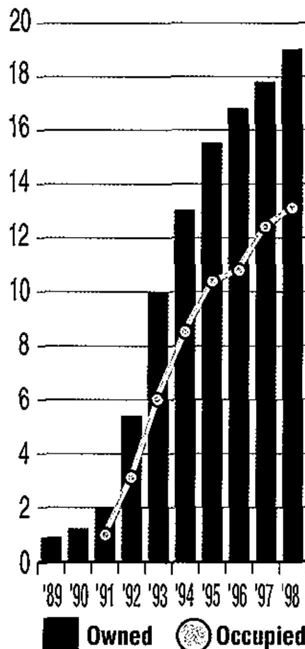
CMH Insurance included at least one insurance product with 90 percent of financed home sales. Total premiums for all insurance lines increased 18 percent above 1997's. The Insurance Marketing MBU was established in January and targets current customers for additional insurance product sales. Increased telemarketing efforts and strengthened relationships with both independent retailers and Vanderbilt's Direct Lending MBU should significantly contribute to the group's future growth.

Vanderbilt and the Retail group continue to capture the synergies that exist throughout the life cycle of all Company-originated loans. Retail managers share in the profit and loss of the loans they originate, keeping the entire team focused on maintaining a continuing relationship with the homebuyer throughout the life of the loan. The Retail group's loan production totaled $539 million in 1998, and Vanderbilt and Retail will continue their close alliance to create new and innovative ways to facilitate loan servicing while maintaining low overall delinquency levels.

The Financial Services group is proud of its financial diversity, vertical structure, and plans that are in place to ensure that historical income growth continues.



COMMUNITIES



In 1998, your Communities group increased by 1,167, or 7 percent, its number of home sites. Contributing to this growth was the acquisition of four communities in Virginia, South Carolina, and Florida that added 945 sites, while expansion in existing communities contributed 222 sites. Your Company now owns and operates 71 communities with 18,964 home sites in 12 states. Three states, Texas, Florida, and Tennessee, account for 73 percent of these home sites.

The Communities group purchased all outside partnership interests in six properties in Tennessee and Texas. Management will now have the flexibility to direct additional resources to these communities, which will provide improved resident services and add portfolio value. Investments to increase the portfolio size totaled $30 million. This included expansion of existing properties, land for new developments, and additional purchased communities.

The first phase of four communities in Texas and Tennessee is under construction, and two are slated for completion in the third quarter. Three expansion properties are in various stages of development and are in the high demand markets of Houston, Texas; Knoxville, Tennessee; and Jacksonville, Florida.

Operating rental revenues rose 21 percent to a record level in 1998. This was accomplished by the increase in occupied sites, along with a 7 percent increase in our average site rent. For properties owned at least one year, occupancy increased to 72 percent from 70 percent in 1997. Overall occupancy was also at 72 percent as three of the four communities purchased during the year had high occupancy levels.

Past due rental accounts were a focus item for our management and system personnel in 1998. As a result, delinquencies improved to 6 percent compared to 11 percent for the prior year end.

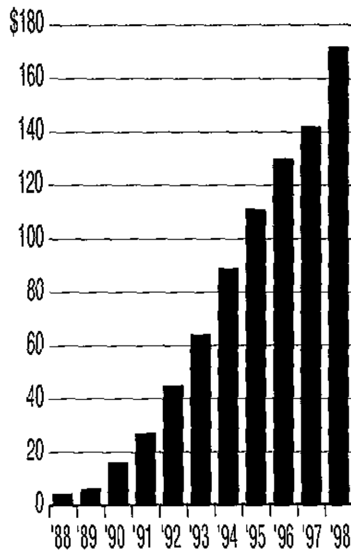
To focus all resources toward the key result areas of the business, management developed the SCOPE program early in the year. SCOPE – Sales, Collections,

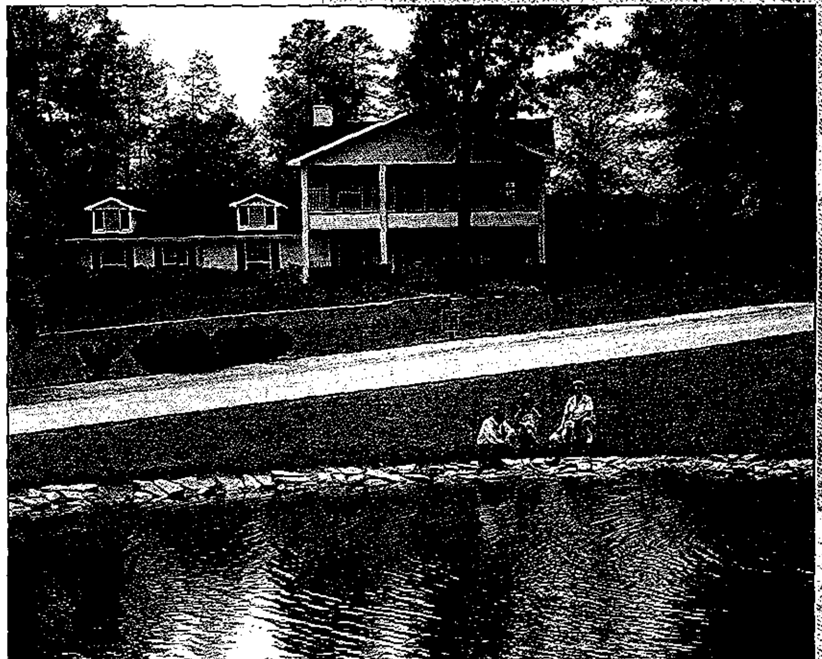
	June 30, **1998**	1997
Home sites owned	**18,964**	17,797
Occupancy rate	72%	70%

Occupancy, People, and Expense control – helped the Communities management in the identification and resolution of issues as they focused on results. This model fosters training, communication, and teamwork and is consistent with our buy or build-and-hold long-term strategy.

The Communities group is becoming a focused and disciplined property management team that understands the importance of sales and marketing. Every sale is amplified through the synergistic corporate structure and leveraged five times, as profit is earned when the home is purchased from Manufacturing, sold to a resident, financed and insured through Financial Services, and sited in the community.

The group's future success is assured as the SCOPE model is applied to expanding existing communities, greenfielding developments, purchasing existing communities where value can be added, and otherwise precisely executing the group's business plan.





ELEVEN YEAR REVIEW

(in thousands except per share and other data)

	1998	1997	1996	1995	1994	1993	1992	1991	1990	1989	1988
Income Statement Data:											
Revenues:											
Net sales	**$ 880,856**	$ 822,906	$762,396	$621,351	$510,153	$384,491	$296,849	$257,557	$219,443	$208,624	$196,110
Financial services and other income	**246,923**	198,797	166,345	136,741	118,083	91,750	74,330	62,392	40,316	33,270	28,671
	1,127,779	1,021,703	928,741	758,092	628,236	476,241	371,179	319,949	259,759	241,894	224,781
Costs and expenses:											
Cost of sales	**598,589**	559,274	521,200	431,826	357,698	267,201	206,049	176,374	153,786	147,982	138,468
SG&A	**302,598**	270,996	236,188	188,835	153,698	113,695	84,785	76,420	60,220	55,456	50,781
Financial services interest	**2,015**	2,885	3,649	5,533	8,196	11,819	16,585	18,198	11,595	9,911	10,127
Other expenses	**7,976**	1,000	0	0	0	0	3,300	3,772	2,213	1,539	2,010
	911,178	834,155	761,037	626,194	519,592	392,715	310,719	274,764	227,814	214,888	201,386
Operating income	**216,601**	187,548	167,704	131,898	108,644	83,526	60,460	45,185	31,945	27,006	23,395
Interest income (expense), net/other	**5,499**	5,152	4,596	3,902	(359)	(170)	(317)	(592)	(575)	(1,042)	(1,073)
Income before income taxes	**222,100**	192,700	172,300	135,800	108,285	83,356	60,143	44,593	31,370	25,964	22,322
Provision for income taxes	**(84,400)**	(73,200)	(65,500)	(48,800)	(39,000)	(29,600)	(20,800)	(16,000)	(11,500)	(9,714)	(8,370)
Income before accounting change	**137,700**	119,500	106,800	87,000	69,285	53,756	39,343	28,593	19,870	16,250	13,952
Cumulative effect of accounting change	**0**	0	0	0	3,000	0	0	0	0	0	0
Net income	**$ 137,700**	$ 119,500	$106,800	$ 87,000	$ 72,285	$ 53,756	$ 39,343	$ 28,593	$ 19,870	$ 16,250	$ 13,952
Net income per share:											
Basic	**$1.16**	$1.01	$ 0.90	$ 0.74	$ 0.64	$ 0.49	$ 0.38	$ 0.33	$ 0.26	$ 0.21	$ 0.18
Diluted	**$1.15**	$1.00	$ 0.89	$ 0.73	$ 0.61	$ 0.47	$ 0.36	$ 0.30	$ 0.23	$ 0.19	$ 0.17
Average shares outstanding:											
Basic	**118,770**	118,659	118,602	117,616	112,837	109,113	104,082	85,507	75,828	76,511	76,703
Diluted	**119,603**	119,477	119,346	118,628	119,900	119,285	113,680	100,973	96,174	95,945	96,207
Dividends per common share	**$ .080**	$ .076	$ .061	$ .038	—	—	—	—	—	—	—
Balance Sheet Data:											
Total assets	**$1,457,757**	$1,045,761	$886,350	$761,151	$701,148	$587,032	$554,780	$488,817	$339,099	$294,754	$275,835
Debt obligations	**247,591**	22,806	30,290	48,737	70,680	137,038	192,931	227,444	177,374	163,471	157,153
Shareholders' equity	**$ 881,019**	$ 754,526	$650,189	$544,187	$462,154	$348,630	$292,950	$200,992	$108,334	$ 87,462	$ 70,651
Key Financial Ratios:											
As a % of revenue:											
Operating income	**19.2%**	18.4%	18.1%	17.4%	17.3%	17.5%	16.3%	14.1%	12.3%	11.2%	10.4%
Net income	**12.2%**	11.7%	11.5%	11.5%	11.5%	11.3%	10.6%	8.9%	7.6%	6.7%	6.2%
Debt as a % of total capital	**21.9%**	2.9%	4.5%	8.2%	13.3%	28.2%	39.7%	53.1%	62.1%	65.1%	69.0%
Other Data:											
Company-owned sales centers	**273**	245	216	192	165	143	127	123	96	99	100
Independent retailers	**702**	663	580	421	372	371	312	330	322	269	245
Manufacturing plants	**18**	17	17	16	13	13	11	10	10	10	10
Communities	**71**	67	64	55	46	33	20	12	9	7	4

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

Results of Operations

The following table reflects the percentage changes in sales by the Company's retail and community sales centers and in wholesale sales to independent retailers. It also shows the percentage changes in the average number of Company-owned retail centers, communities and independent retailers, the average sales per location, and the average price per home sold in each category.

	Year Ended June 30, 1998 vs 1997	1997 vs 1996
Retail		
Dollar sales	**+7.6%**	+10.1%
Number of retail centers	**+12.4%**	+13.0%
Dollar sales per retail center	**-4.2%**	-2.6%
Price of home	**+10.9%**	+2.0%
Wholesale		
Dollar sales	**+8.3%**	+3.5%
Number of independent retailers	**+9.8%**	+24.2%
Dollar sales per independent retailer	**-1.4%**	-16.6%
Price of home	**+5.7%**	+1.3%
Communities		
Dollar sales	**-10.1%**	+15.7%
Number of communities	**+5.3%**	+10.1%
Dollar sales per community	**-14.6%**	+5.1%
Price of home	**+6.4%**	+6.6%

Fiscal 1998 compared to Fiscal 1997

Total revenues grew 10% on a 7% increase in Manufactured Housing sales and a 24% rise in Financial Services and other income.

Net sales of the Retail group rose 8% to $535 million. This growth was the result of a 12% increase in the average number of Company-owned retail centers and an 11% increase in the average price per home offset partially by a 3% decline in homes sold. Multi-section homes accounted for 46% of total new homes sold versus 40% last year.

During the year, the Company opened or acquired 33 retail locations and closed five under-performing retail centers. The Company constantly evaluates specific local markets and opens, acquires, or closes retail centers as conditions warrant. Of the 33 new openings, 22 were acquired and 11 were greenfield start-ups. Seven of the new retail centers were opened in the fourth quarter.

Net sales of the Manufacturing group to independent retailers increased 8% to $312 million and the number of homes sold rose 2%. The average wholesale price increased 6% principally due to a shift toward multi-section homes. Multi-section homes accounted for 44% of total shipments versus 35% last year.

Net sales of the Communities group declined 10% to $34 million as 15% less homes were sold while the average home selling price increased 6%. Four acquisitions brought the number of communities to 71 at year end.

Financial Services and other income grew 24%, mainly due to VMF, $34 million, and earned insurance premiums and commissions, $5 million.

Interest and loan servicing revenues increased 31% to $117 million. The average balance of receivables owned rose 72% to $386 million with a weighted average interest rate of 10.2%, down from 12.2%. The average balance of receivables sold rose 36% to $1.9 billion and the weighted average loan service spread was 3.6% compared to 3.5%.

Financial Services interest expense decreased $.9 million, or 30%, to $2 million. Debt collateralized by installment contract receivables dropped 29% to an average of $19 million and the weighted average interest rate declined to 10.1% from 11.1%. Loan covenants preclude prepaying these relatively higher cost obligations.

Gross profit margins remained consistent at 32%.

Selling, general, and administrative expenses were 34.4% and 32.9% of sales for the years ended June 30, 1998 and 1997, respectively. Expenses associated with the start-up of 33 new sales centers, acquired communities, and initial costs of the Financial Services' MBUs were primary causes of the increase.

Net losses as a percentage of loans outstanding for fiscal 1998 increased to .8% while delinquency rates on all loans increased to 2.2% (excluding Access).

The changes in inventory levels at June 30, 1998 compared to June 30, 1997 are shown below in millions:

	Increase
Manufacturing	
Raw materials	$ 3.9
Finished goods	0.6
Retail	
Net increase of 28 Company-owned sales centers	16.5
Increase in average inventory levels at 245 Company-owned sales centers	25.0
Communities	
Inventory at 4 manufactured housing communities acquired during the year	0.1
Increase in average inventory levels at 67 manufactured housing communities	1.6
	$47.7

Fiscal 1997 compared to Fiscal 1996

Total revenues grew 10% on an 8% increase in Manufactured Housing sales and a 20% rise in Financial Services and other income.

Net sales of the Retail group rose 10% to $497 million. This growth was the result of a 13% increase in the average number of Company-owned retail centers and a 3% decline in the average dollar sales per location.

During the year, the Company opened or acquired 31 retail locations and closed two under-performing retail centers. The Company constantly evaluates specific local markets and opens, acquires, or closes retail centers as conditions warrant. Of the 31 new openings, 14 were acquired and 17 were greenfield start-ups. Seventeen of the new retail centers were opened in the fourth quarter.

Net sales of the Manufacturing group to independent retailers increased 4% to $288 million and the number of homes sold rose 2%. The average wholesale price increased 1% due in part to a shift toward multi-section homes. Multi-section homes accounted for 35% of total shipments versus 32% last year.

Net sales of the Communities group rose 16% to $38 million principally as a result of a 9% rise in home sales and a 6% improvement in the average sales price per home. Four acquisitions brought the number of communities to 67 at year end.

Management's Discussion and Analysis of Financial Condition and Results of Operations *(Continued)*

Financial Services and other income grew 20% to $199 million, mainly due to VMF, $20 million, and earned insurance premiums and commissions, $7 million.

Interest and loan servicing revenues increased 10% to $78 million. The average balance of receivables owned rose 3% to $224 million with a weighted average interest rate of 12.2%, down from 12.8%. The average balance of receivables sold rose 28% to $1.4 billion and the weighted average loan service spread was 3.5% compared to 3.8%.

Financial Services interest expense decreased $.8 million, or 21%, to $2.9 million. Debt collateralized by installment contract receivables dropped 25% to an average of $26 million and the weighted average interest rate moved to 11.1% from 10.8%. Loan covenants preclude prepaying these relatively higher cost obligations.

Gross profit margins improved from 31.6% to 32.0%. The increase primarily results from a greater mix of Clayton manufactured product sold to the Retail group. Manufacturing sales to Retail were 54.9% of new retail sales compared to 54.5% in 1996.

Selling, general, and administrative expenses were 32.9% and 31.0% of sales for the years ended June 30, 1997 and 1996, respectively. Expenses associated with the start-up of 31 new sales centers, acquired communities, and initial costs of the Financial Services' MBUs were primary causes of the increase.

Net losses as a percentage of loans outstanding for fiscal 1997 decreased to 0.2% from 0.3% last year while delinquency rates on all loans increased slightly to 2.1%.

The changes in inventory levels at June 30, 1997 compared to June 30, 1996 are shown below in millions:

	Increase (decrease)
Manufacturing	
Raw materials	$ (1.4)
Finished goods	(1.2)
Retail	
Net increase of 29 Company-owned sales centers	11.8
Decrease in average inventory levels at 216 Company-owned sales centers	(14.1)
Communities	
Inventory at 4 manufactured housing communities acquired during the year	0.7
Decrease in average inventory levels at 63 manufactured housing communities	(0.6)
	$(4.8)

Fourth Quarter Results

The increase in revenues and net income during the fourth quarters of fiscal 1998 and 1997 are not indicative of future operating trends but rather reflect the seasonality of the manufactured housing industry. In recent years, approximately 31% of the Company's sales have occurred in the fourth quarter.

Liquidity and Capital Resources

During fiscal 1998, the Company originated and acquired approximately $1.3 billion of installment contract and mortgage loan receivables. The Company financed these originations and acquisitions primarily with $936 million in proceeds from the pooling and sale of installment contract and mortgage loan receivables as well as a revolving credit facility. Additional funding came from operating cash flow and collection of installment contract and mortgage loan receivables. Utilizing cash generated from operations, the Company invested approximately $23 million in the acquisition of land or existing manufactured housing communities and $8 million in related rental units, $15 million for the opening of Company-owned retail centers, $5 million including the construction of one new plant and the improvement of existing manufacturing facilities, and $11 million for other fixed assets.

The Company expects to invest approximately $25 million in fiscal 1999 in the acquisition or construction of manufactured housing communities, up to $10 million for new Company-owned retail centers, up to $12 million for the construction and improvement of manufacturing facilities, and to originate $900 million of installment contract and mortgage loan receivables. Cash needs for 1999 and thereafter are expected to be met with cash flows from operations, revolving credit lines, and sales of installment contract and mortgage loan receivables and GNMA certificates.

New Accounting Pronouncements

During fiscal 1997, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 130 (SFAS 130), *Reporting Comprehensive Income* and SFAS No. 131, *Disclosures About Segments of an Enterprise and Related Information.* SFAS 130 requires disclosure of comprehensive income and its components in a company's financial statements and is effective for fiscal years beginning after December 15, 1997. SFAS 131 requires new disclosures of segment information in a company's financial statements and is effective for fiscal years beginning after December 15, 1997. These statements will be effective for the Company in fiscal 1999. Adoption of these statements will not impact the Company's consolidated financial position, results of operations, or cash flows.

On June 15, 1998, the FASB issued SFAS No. 133, *Accounting for Derivative and Financial Instruments and Hedging Activities.* SFAS 133 establishes a new model for accounting for derivatives and hedging activities based on these fundamental principles: i) derivatives represent assets and liabilities that should be recognized at fair value on the balance sheet; ii) derivative gains and losses do not represent liabilities or assets and therefore, should not be reported on the balance sheet as deferred credits or deferred debits; and iii) special hedge accounting should be provided only for transactions that meet certain specified criteria, which include a requirement that the change in the fair value of the derivative be highly effective in offsetting the change in the fair value or cash flows of the hedged item. This statement is effective for fiscal years beginning after June 15, 1999 and is not expected to have a material effect on the Company's financial position or results of operations.

Effects of Inflation

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

Quarterly Results (Unaudited)

(in thousands except per share data)	First Sept. 30	Second Dec. 31	Third Mar. 31	Fourth June 30	Year
1998					
Revenues	**$262,695**	**$251,069**	**$268,375**	**$345,640**	**$1,127,779**
Operating income	**46,745**	**48,537**	**49,234**	**72,085**	**216,601**
Net income	**29,679**	**31,109**	**31,118**	**45,794**	**137,700**
Earnings per share:					
Basic	**$.25**	**$.26**	**$.26**	**$.39**	**$1.16**
Diluted	**$.25**	**$.26**	**$.26**	**$.38**	**$1.15**
Eqnivalent shares outstanding:					
Basic	**118,574**	**118,716**	**118,887**	**118,904**	**118,770**
Diluted	**119,347**	**119,600**	**119,728**	**119,739**	**119,603**
Price range of stock:					
High	**$18.75**	**$19.44**	**$21.31**	**$22.38**	**$22.38**
Low	**14.25**	**15.75**	**16.25**	**17.06**	**14.25**
Close	**18.56**	**18.00**	**20.25**	**19.00**	**19.00**
Dividends per common share	**$.020**	**$.020**	**$.020**	**$.020**	**$.080**
1997					
Revenues	$236,204	$234,672	$226,624	$324,203	$1,021,703
Operating income	40,099	41,953	42,014	63,482	187,548
Net income	25,603	26,676	26,298	40,923	119,500
Earnings per share:					
Basic	$.22	$.22	$.22	$.35	$1.01
Diluted	$.22	$.22	$.22	$.34	$1.00
Equivalent shares outstanding:					
Basic	118,952	118,768	118,457	118,457	118,659
Diluted	119,903	119,628	119,214	119,163	119,477
Price range of stock:					
High	$17.90	$17.20	$15.38	$15.25	$17.90
Low	13.80	12.60	13.00	12.63	12.60
Close	17.60	13.50	13.13	14.38	14.38
Dividends per common share	$.016	$.020	$.020	$.020	$.076

Year 2000

The Company recognizes the need to ensure its operations will not be adversely impacted by year 2000 software failures and has performed a review of its computer applications related to their continuing functionality for the year 2000 and beyond. Certain of the Company's existing systems have been upgraded and the Company expects to upgrade its remaining systems through modification or replacement by the end of fiscal 1999. As a result, the Company does not believe that it has material exposure to the year 2000 issue with respect to its own computer applications. The Company does not expect that the cost of the modifications will have a material impact on the Company's financial position, results of operations, or cash flows in future periods. The year 2000 issue may impact the operations of the Company indirectly by affecting the operations of its suppliers, business partners, customers, and other parties that provide significant services to the Company. The Company expects to complete during fiscal 1999 an assessment of potential year 2000 issues with these parties. The Company is currently unable to predict to what extent year 2000 software issues will affect these parties and, consequently, the Company.

Forward Looking Statements

Certain statements in this annual report are forward looking as defined in the Private Securities Litigation Reform Law. These statements involve certain risks and uncertainties that may cause actual results to differ materially from expectations as of the date of this report. These risks fall generally within three broad categories consisting of industry factors, management expertise, and government policy and economic conditions. Industry factors include such matters as potential periodic inventory adjustments by both captive and independent retailers, general or seasonal weather conditions affecting sales and revenues, catastrophic events impacting insurance reserves, cost of labor and/or raw materials and industry concentration trends creating fewer, but stronger competitors capable of sustaining competitive pricing pressures.

Management expertise is affected by management's overall ability to anticipate and meet consumer preferences, maintain successful marketing programs, continue quality manufacturing output, keep a strong cost management oversight, and project stable gain on sale accounting assumptions. Lastly, management has the least control over government policy and economic conditions such as prevailing interest rates, government monetary policy, stable regulation of manufacturing standards, consumer confidence, favorable trade policies, and general prevailing economic and employment conditions.

Consolidated Balance Sheets

Clayton Homes, Inc. and Subsidiaries

(in thousands)	June 30, 1998	1997
Assets		
Cash and cash equivalents	$ **1,731**	$ 89,695
Receivables, principally installment contracts and residual interests, net of reserves for credit losses and unamortized discount of $30,291 and $7,770, respectively	**837,197**	478,691
Inventories	**167,113**	119,434
Securities held-to-maturity, approximate value of $20,647 and $19,988	**20,361**	20,361
Restricted cash and investments	**86,176**	70,997
Property, plant and equipment, net	**261,549**	214,072
Deferred income taxes	**11,756**	—
Other assets	**71,874**	52,511
Total assets	**$1,457,757**	$1,045,761
Liabilities and Shareholders' Equity		
Accounts payable and accrued liabilities	$ **138,557**	$ 99,498
Debt obligations	**247,591**	22,806
Deferred income taxes	—	14,074
Other liabilities	**190,590**	154,857
Total liabilities	**576,738**	291,235
Shareholders' equity		
Preferred stock, $.10 par value, authorized 1,000 shares, none issued	—	—
Common stock, $.10 par value, authorized 200,000 shares, issued 118,816 at June 30, 1998 and 118,497 at June 30, 1997	**11,882**	11,850
Additional paid-in capital	**165,383**	166,153
Retained earnings	**703,754**	576,523
Total shareholders' equity	**881,019**	754,526
Total liabilities and shareholders' equity	**$1,457,757**	$1,045,761

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

Report of Independent Accountants

August 5, 1998

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income, shareholders' equity and cash flows present fairly, in all material respects, the financial position of Clayton Homes, Inc. and Subsidiaries at June 30, 1998 and 1997, and the results of their operations and their cash flows for each of the three years in the period ended June 30, 1998, in conformity with generally accepted accounting principles. 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 of these statements in accordance with generally accepted auditing standards which 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for the opinion expressed above.

PricewaterhouseCoopers LLP

Consolidated Statements of Income

Clayton Homes, Inc. and Subsidiaries

(in thousands except per share data)	Year ended June 30, 1998	1997	1996
Revenues:			
Net sales	**$ 880,856**	$ 822,906	$762,396
Financial services	**190,204**	148,515	115,987
Other income	**56,719**	50,282	50,358
	1,127,779	1,021,703	928,741
Costs and expenses:			
Cost of sales	**598,589**	559,274	521,200
Selling, general and administrative	**302,598**	270,996	236,188
Financial services interest	**2,015**	2,885	3,649
Provision for credit losses	**7,976**	1,000	—
	911,178	834,155	761,037
Operating income	**216,601**	187,548	167,704
Interest income (expense), net/other	**5,499**	5,152	4,596
Income before income taxes	**222,100**	192,700	172,300
Provision for income taxes	**(84,400)**	(73,200)	(65,500)
Net income	**$ 137,700**	$ 119,500	$106,800
Net income per common share:			
Basic	**$1.16**	$1.01	$.90
Diluted	**$1.15**	$1.00	$.89
Average shares outstanding:			
Basic	**118,770**	118,659	118,602
Diluted	**119,603**	119,477	119,346

Consolidated Statements of Shareholders' Equity

(in thousands except per share data)	Total Shareholders' Equity	Common Stock	Additional Paid-In Capital	Retained Earnings
Balance at June 30, 1995	$ 544,187	$ 11,807	$ 165,919	$ 366,461
Net income	106,800	—	—	106,800
Purchase of 125 shares of common stock	(1,893)	(16)	(1,877)	—
Dividends declared ($.061 per common share)	(7,223)	—	—	(7,223)
Issuances related to stock incentive, employee benefit plans, and other	8,318	95	8,223	—
Balance at June 30, 1996	650,189	11,886	172,265	466,038
Net income	119,500	—	—	119,500
Purchase of 840 shares of common stock	(11,349)	(84)	(11,265)	—
Dividends declared ($.076 per common share)	(9,015)	—	—	(9,015)
Issuances related to stock incentive, employee benefit plans, and other	5,201	48	5,153	—
Balance at June 30, 1997	754,526	11,850	166,153	576,523
Net income	**137,700**	—	—	**137,700**
Purchase of 570 shares of common stock	**(9,506)**	**(57)**	**(9,449)**	—
Dividends declared ($.080 per common share)	**(10,469)**	—	—	**(10,469)**
Issuances related to stock incentive, employee benefit plans, and other	**8,768**	**89**	**8,679**	—
Balance at June 30, 1998	**$881,019**	**$11,882**	**$165,383**	**$703,754**

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

Consolidated Statements of Cash Flows

Clayton Homes, Inc. and Subsidiaries

(in thousands)	Year ended June 30, 1998	1997	1996
Cash Flows from Operating Activities:			
Net income	**$137,700**	$119,500	$106,800
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	**14,733**	13,058	11,163
Gain on sale of installment contract receivables, net of amortization	**(31,699)**	(21,541)	(11,315)
Gain on sale of property	—	—	(4,828)
Provision for credit losses	**7,976**	1,000	—
Deferred income taxes	**(25,830)**	8,394	(3,702)
Increase in other receivables, net	**(25,700)**	(27,383)	(16,972)
Decrease (increase) in inventories	**(47,679)**	4,846	(35,825)
Increase in accounts payable, accrued liabilities, and other	**55,429**	39,249	25,633
Cash provided by operations	**84,930**	137,123	70,954
Origination of installment contract receivables	**(801,865)**	(646,624)	(476,467)
Proceeds from sales of originated installment contract receivables	**705,420**	614,588	394,087
Principal collected on originated installment contract receivables	**50,260**	39,668	35,199
Net cash provided by operations	**38,745**	144,755	23,773
Cash Flows from Investing Activities:			
Acquisition of installment contract receivables	**(520,912)**	(206,937)	(36,105)
Proceeds from sales of acquired installment contract receivables	**230,311**	167,138	36,007
Principal collected on acquired installment contract receivables	**27,703**	3,439	16,935
Acquisition of property, plant and equipment, net	**(62,210)**	(42,859)	(40,829)
Proceeds from sale of property	—	—	21,271
Increase in restricted cash and investments	**(15,179)**	(594)	(4,189)
Net cash used in investing activities	**(340,287)**	(79,813)	(6,910)
Cash Flows from Financing Activities:			
Dividends	**(10,469)**	(9,015)	(6,835)
Net borrowings on credit facilities	**227,873**	—	—
Repayment of long-term debt	**(3,088)**	(7,484)	(18,447)
Issuance of stock for incentive plans and other	**8,768**	5,201	8,318
Repurchase of common stock	**(9,506)**	(11,349)	(1,893)
Net cash provided by (used in) financing activities	**213,578**	(22,647)	(18,857)
Net increase (decrease) in cash and cash equivalents	**(87,964)**	42,295	(1,994)
Cash and cash equivalents at beginning of year	**89,695**	47,400	49,394
Cash and cash equivalents at end of year	**$ 1,731**	$ 89,695	$ 47,400
Supplemental disclosures of cash flow information:			
Cash paid during the year for:			
Interest	**$ 4,285**	$ 3,912	$ 4,016
Income taxes	**$ 93,832**	$ 62,269	$ 63,366

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

Notes to 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. CHI and its subsidiaries are collectively referred to as the Company. The Company is a vertically integrated manufactured housing company headquartered in Knoxville, Tennessee. Employing more than 6,700 people and operating in 28 states, the Company builds, sells, finances, and insures manufactured homes, as well as owns and operates residential manufactured housing communities. Significant intercompany accounts and transactions have been eliminated in the financial statements. See Note 11 for information related to the Company's business segments.

Income Recognition

Sales to independent retailers 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 84 to 240 months, are financed by Vanderbilt Mortgage and Finance, Inc. (VMF), the Company's mortgage banking subsidiary.

Premiums from physical damage, family protection, and home-buyer protection plan insurance policies reinsured by the insurance subsidiaries are recognized as income over the terms of the contracts. The policies represent single payment contracts with terms of one to 10 years. Claims and expenses are matched to recognize profits over the terms of the contracts. This matching is accomplished by means of deferral and recognition of unearned premiums and the deferral and amortization of policy acquisition costs.

Installment Contract Receivables and Mortgage Loan Receivables

Installment contract receivables and mortgage loan receivables originated or purchased by VMF are generally sold to investors through an asset backed securities facility, with VMF retaining servicing on the contracts. Certain purchased mortgage loan receivables are sold to financial institutions with servicing released. In 1998, $903 million in installment contract receivables and mortgage loan receivables were securitized with VMF retaining servicing, while $33 million in mortgage loan receivables were sold with servicing released. In May 1998, the Company purchased $245 million in loans from Access Financial Lending Corporation and contracted to service an additional $267 million portfolio. The purchased loans are presented net of an approximate $24 million reserve for credit losses in the accompanying financial statements.

Installment contract receivables held for sale of $622 million and $254 million in 1998 and 1997, respectively, are included in receivables and are carried at the lower of aggregate cost or market. 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 over the life of the related portfolio after giving consideration to anticipated prepayments. Adjustments between the reserve for credit losses and unamortized discount are made to reflect changes in the estimated collectibility of each portfolio purchased. Estimated principal receipts under installment contract receivables for each of the five fiscal years subsequent to 1998 and thereafter are as follows:

1999	$180,000,000	2002	$ 60,000,000
2000	86,000,000	2003	52,000,000
2001	70,000,000	Thereafter	174,000,000

The estimated principal receipts are based on the scheduled payments and estimated prepayments of principal of the installment contract receivables. Estimated principal receipts for the year ending June 30, 1999 include amounts relating to the sale of $240 million of installment contract receivables in August 1998. VMF provides servicing for investors in installment contract receivables. Total contracts serviced at June 30, 1998 and 1997, including contracts held for investment, were approximately $2,925 million and $2,044 million, respectively. Most of the installment contract receivables are with borrowers in the east, south and southwest portions 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.

Effective January 1, 1997, the Company adopted SFAS No. 125, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities.* SFAS 125 utilizes a financial components approach, requiring that the carrying amount of the receivables sold be allocated between the assets sold and the assets (liabilities) created, if any, at their fair value at the date of sale. The assets (liabilities) created are: 1) an interest-only strip valued as the discounted present value of the excess (deficiency) interest due the servicer (VMF) during the expected life of the contracts over: i) the stated investor yield; ii) the contractual servicing fee; and iii) estimated credit losses; and 2) servicing asset (liability), representing the discounted present value of the contractual servicing fee over the cost of servicing the contracts. Profit (loss) recorded at the time of the sale is computed as the difference between the allocated carrying amount of the receivables sold and the proceeds realized from the sale. The adjustment to income in 1997 was immaterial with respect to the adoption of this statement.

(in thousands)	**1998**	1997
Servicing asset beginning balance	**$ 5,644**	$ 0
Servicing asset recognized	**10,823**	7,080
Amortization	**(3,424)**	(1,436)
Servicing asset ending balance	**$13,043**	$5,644

The balance represents the estimated fair value of the aggregate servicing assets recognized during 1998. The estimate of fair value assumes: 1) discount rates which, at the time the asset was created, approximate current market rates; and 2) expected prepayment rates based on loan prepayment experience for similar transactions.

Cash Equivalents

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

Investment Securities

Effective July 1, 1994, the Company adopted SFAS No. 115, *Accounting for Certain Investments in Debt and Equity Securities.* Investments in certain debt and equity securities are classified as either Held-to-Maturity (reported at amortized cost), Trading (reported at fair value with unrealized gains and losses included in earnings), or Available-for-Sale (reported at fair value with unrealized gains and losses excluded from earnings and reported as a separate component of shareholders' equity).

Premiums and discounts on debt securities are recognized in interest income on the level interest yield method over the period to maturity.

Gains and losses on the sale of securities are determined using the specific identification method.

Inventories

New homes and raw materials are valued at the lower of cost or market, using the last-in, first-out (LIFO) method of inventory valuation. Previously-owned manufactured homes are valued at

estimated wholesale prices, which are not in excess of net realizable value.

Property, Plant and Equipment

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 over the estimated useful lives of the respective assets ranging from three to 27 1/2 years.

The Company evaluates the carrying values of property and equipment for impairment losses by analyzing the operating performance and future cash flows of the various business activities. The Company adjusts the net book value of the underlying assets if the sum of expected future cash flows is less than fair market value.

Reserves for Credit Losses and Contingent Liabilities

Reserves for credit losses are established related to installment contract receivables. Actual credit losses are charged to the reserves when incurred. The reserves established for such losses are determined based on the Company's historical loss experience after adjusting for current economic conditions. Management, in assessing the loss experience and economic conditions, adjusts reserves through periodic provisions. 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.

Interest Rate Swaps

Interest rate swaps are entered into as a hedge against interest exposure of variable rate debt. The differences to be paid or received on swaps are included in interest expense. The fair value of the Company's interest rate swap agreements is estimated using present value discounting techniques. These values represent the amounts the Company would receive or pay to terminate the agreements taking into consideration current interest rates.

Other

Per share and share data have been retroactively adjusted to reflect 5-for-4 stock splits in December 1996 and December 1995. Certain reclassifications have been made to the 1996 and the 1997 financial statements to conform to the 1998 presentation.

Restricted Cash and Investments

Restricted cash and investments primarily represent reserves required by: 1) trust account cash balances required by certain VMF servicing agreements, and 2) insurance reserves required by escrow or trust agreements.

Management Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

New Accounting Pronouncements

During fiscal 1997, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 130 (SFAS 130), *Reporting Comprehensive Income* and SFAS No. 131, *Disclosures About Segments of an Enterprise and Related Information.* SFAS 130 requires disclosure of comprehensive income and its components in a company's financial statements and is effective for fiscal years beginning after December 15, 1997. SFAS 131 requires new disclosures of segment information in a company's financial statements and is effective for fiscal years beginning after December 15, 1997. These statements will be effective for the Company in fiscal 1999. Adoption of these statements will not impact the Company's consolidated financial position, results of operations, or cash flows.

On June 15, 1998, the FASB issued SFAS No. 133, *Accounting for Derivative and Financial Instruments and Hedging Activities.* SFAS 133 establishes a new model for accounting for derivatives and hedging activities based on these fundamental principles: i) derivatives represent assets and liabilities that should be recognized at fair value on the balance sheet; ii) derivative gains and losses do not represent liabilities or assets and therefore, should not be reported on the balance sheet as deferred credits or deferred debits; and iii) special hedge accounting should be provided only for transactions that meet certain specified criteria, which include a requirement that the change in the fair value of the derivative be highly effective in offsetting the change in the fair value or cash flows of the hedged item. This statement is effective for fiscal years beginning after June 15, 1999, and is not expected to have a material effect on the Company's financial position or results of operations.

Note 2 - Inventories

Inventories at June 30, 1998, and 1997 are as follows:

(in thousands)	1998	1997
Manufactured homes:		
New	**$114,577**	$ 81,963
Previously-owned	**33,991**	22,805
Raw materials	**18,545**	14,666
	$167,113	$119,434

If the first-in, first-out (FIFO) method of inventory valuation had been used, inventories would have been higher by $18,331,000 and $18,196,000 at June 30, 1998 and 1997, respectively.

Note 3 - Securities Held-to-Maturity

At June 30, 1998 and 1997, manufactured housing contract senior/subordinate pass-through certificates have been classified in the consolidated financial statements according to management's intent. These securities can be reasonably expected to mature after 10 years.

Note 4 - Property, Plant and Equipment

Property, plant and equipment at June 30, 1998, and 1997 are as follows:

(in thousands)	1998	1997
Land and improvements	**$166,692**	$135,027
Buildings	**126,085**	104,560
Furniture and equipment	**34,964**	28,200
	327,741	267,787
Less: accumulated depreciation and amortization	**(66,192)**	(53,715)
	$261,549	$214,072

Depreciation charged to operations was $14,733,000, $13,058,000, and $11,163,000 for each of the years ended June 30, 1998, 1997, and 1996, respectively.

Note 5 - Debt Obligations

Debt obligations at June 30, 1998 and 1997, are summarized as follows:

Notes to Consolidated Financial Statements *(Continued)*

(in thousands)	**1998**	1997
Lines of credit	**$227,873**	$ —
Debt collateralized by installment contract receivables maturing in fiscal yeats through 1999 to 2004: weighted average rate of 10.14% at June 30, 1998	**15,557**	22,013
Other notes payable	**4,161**	793
Total	**$247,591**	$22,806

The Company has committed and uncommitted lines of credit totaling $150 million and $82.5 million for working capital needs of which $150 million and $77.9 million, respectively, were outstanding at June 30, 1998. These lines of credit do not require collateral and are priced based on LIBOR plus rates ranging from 0.10% to 0.45%. The $150 million line is a five-year revolving credit facility guaranteed by all material subsidiaries of the Company and is governed by various financial covenants which require maintenance of certain financial ratios.

Additionally, the Company has letters of credit of which $69 million was outstanding at year end, primarily related to insurance reserve requirements.

On July 1, 1998, the Company enteted into a short-term, committed line of credit for $200 million, primarily to facilitate the purchase and warehousing of a manufactured housing loan portfolio. This line is also subject to certain financial covenants.

Debt collateralized by installment contract teceivables and other notes payable are scheduled to mature as follows:

1999	$3,936,000	2002	$2,944,000
2000	3,253,000	2003	2,059,000
2001	3,144,000	Thereafter	4,382,000

Under certain interest rate swap agreements, the Company agrees with other parties to exchange, at specified intervals, the difference between fixed rate and variable rate interest amounts calculated by reference to an agreed-upon notional principal amount. The fair value of the interest rate swap agreements is estimated using present value discounting techniques and approximates the cash requirement at year end to cancel the agreements. At June 30, 1998, the Company's interest rate swap agreements had a notional amount of $150,000,000 with a fair value of $(649,500).

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, 1998, 1997, and 1996 is as follows:

(in thousands)	**1998**	1997	1996
Balance, beginning of year	**$ 8,051**	$7,766	$11,895
Provision	**7,976**	1,000	—
Losses, net of recoveries applicable to installment contract receivables:			
Purchased	**(2,762)**	(2,337)	(2,494)
Other	**(3,981)**	1,622	442
Reserves transferred from unamortized discount	**2,318**	—	—
Reserves associated with receivables purchased (sold)	**24,226**	—	(2,077)
Balance, end of year	**$35,828**	$8,051	$ 7,766
Reserves for credit losses	**$29,964**	$4,917	$ 4,787
Reserve for contingencies	**5,864**	3,134	2,979
	$35,828	$8,051	$ 7,766

The reserves for credit losses are netted against receivables and the reserve for contingencies is included in other liabilities on the consolidated balance sheets. 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, 1998		
$ 15,000	**30% - 88%**	**$ 4,000**
16,000	**11% - 25%**	**3,000**
157,000	**10% and below**	**16,000**
$188,000		**$23,000**
June 30, 1997		
$ 23,000	30% - 88%	$ 8,000
36,000	11% - 25%	7,000
182,000	10% and below	18,000
$ 241,000		$ 33,000

There were no proceeds from receivables sold with recourse in 1998 and 1997; and $12 million during 1996.

Note 7 - Shareholders' Equity

Stock Option Plan

In 1983, 1985, 1991, and 1997, the Company established Stock Option Plans for a total of 13,616,829 shares of common stock which provide for granting "incentive stock options" or "non-qualified options" and stock appreciation rights to officers and key employees of the Company. In addition, non-management members of the Board of Directors have, with shareholder approval of prices and provisions for exercise, been granted options to purchase shares of common stock. The option prices were established at not less than the fair market value as of the date of grant. 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	Weighted Avg Exercise Price	Stock Options Exercisable	Weighted Avg Excercise Price
Balance June 30, 1995	3,491,560	$ 1.16 - $12.93	$ 6.99	1,289,298	$4.95
Granted	840,373	$10.64 - $17.12	$12.64		
Exercised	(628,845)	$ 1.16 - $10.37	$ 4.28		
Canceled	(378,975)	$ 2.20 - $17.12	$ 8.69		
Balance June 30, 1996	3,324,113	$ 1.38 - $17.12	$ 8.74	1,145,403	$6.65
Granted	569,684	$12.90 - $16.00	$14.38		
Exercised	(161,144)	$ 1.38 - $10.37	$ 4.37		
Canceled	(199,095)	$ 1.78 - $17.12	$11.84		
Balance June 30, 1997	3,533,558	$ 1.38 - $17.12	$ 9.67	1,511,148	$7.90
Granted	**1,223,885**	**$10.24 - $15.75**	**$14.51**		
Exercised	**(954,556)**	**$ 1.38 - $17.12**	**$ 7.76**		
Canceled	**(360,457)**	**$ 1.76 - $17.12**	**$12.38**		
Balance June 30, 1998	**3,442,430**	**$ 1.76 - $17.12**	**$11.65**	**949,916**	**$9.11**

Options available for future grant at June 30, 1998 and 1997 were 4,894,590 and 803,019, respectively. Options were held by 717 persons at June 30, 1998.

Notes to Consolidated Financial Statements *(Continued)*

The following table summarizes information about the plan's stock options at June 30, 1998:

	Options Outstanding			Options Exercisable	
Range of Exercise Price	Number Outstanding at 6/30/98	Weighted Avg Remaining Contractual Life	Weighted Avg Excercise Price	Number Exercisable at 6/30/98	Weighted Avg Excercise Price
$ 1.76-$ 2.70	205,896	1.55 years	$ 1.90	101,044	$ 1.96
$ 4.55-$ 6.31	255,472	3.51 years	$ 5.07	112,884	$ 4.78
$ 9.02-$12.90	1,650,598	6.49 years	$ 10.36	623,542	$ 9.61
$ 14.32-$17.12	1,330,464	8.64 years	$ 16.01	112,446	$ 17.12

The Company has adopted the disclosure-only provisions of SFAS No. 123 *Accounting for Stock-Based Compensation.* Accordingly, no compensation cost has been recognized for the stock option plans. Had compensation cost for the Company's stock option plans been based on the fair value at the grant date for awards from 1998, 1997, and 1996 consistent with the provisions of SFAS 123, the Company's net earnings and earnings per share for 1998 would have been reduced to the pro forma amounts indicated below:

	June 30, 1998	1997	1996
Net income - as reported	**$137,700**	$119,500	$106,800
Net income - pro forma	**136,643**	118,481	106,309
Net income per diluted common share - as reported	**1.15**	1.00	0.89
Net income per diluted common share - pro forma	**1.14**	0.99	0.89

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions used for grants issued from 1996 to 1998: dividend yields ranging from 0.44% to 0.78% with a weighted average yield of 0.55%; expected volatility of 0.295%; risk-free interest rates ranging from 5.45% to 5.59% with a weighted average rate of 5.51%; and expected lives ranging from 7.50 to 9.75 years with a weighted average life of 7.98 years.

Note 8 - Income Taxes

Deferred income taxes reflect the net tax effect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The components of deferred tax assets and liabilities at June 30, 1998 and 1997 are as follows:

(in thousands)	**1998**	1997
Reserves for credit losses and contingencies and discounts	**$ 4,064**	$ 4,712
Insurance reserves	**9,162**	5,377
Unearned premiums	**6,355**	5,074
Residual interest in installment contract receivables	**5,652**	—
Total deferred tax assets	**$ 25,233**	$ 15,163
Residual interest in installment contract receivables	**$ —**	$(16,881)
Deferred costs	**(4,789)**	(3,904)
Other	**(8,688)**	(8,452)
Total deferred tax liabilities	**$(13,477)**	$(29,237)
Net deferred tax asset (liability)	**$ 11,756**	$(14,074)

The provision for income tax is composed of the following:

(in thousands)	**1998**	1997	1996
Current tax provisions:			
Federal	**$103,336**	$58,591	$63,274
State	**6,894**	6,215	5,928
Total current	**$110,230**	$64,806	$69,202
Deferred tax provision/ (benefit)	**(25,830)**	8,394	(3,702)
Total	**$ 84,400**	$73,200	$65,500

The provision for income tax reflected in the financial statements differs from income taxes calculated at the statutory federal income tax rate of 35% in 1998, 1997, and 1996 as follows:

(in thousands)	**1998**	1997	1996
Income taxes at the statutory rate	**$77,735**	$67,451	$60,305
State income taxes, net of federal benefit	**4,481**	4,040	4,150
Other, net	**2,184**	1,709	1,045
Total	**$84,400**	$73,200	$65,500

Note 9 - Employee Benefit Plans

The Company has a 401(k) profit-sharing plan covering all employees who meet participation requirements. 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 accrued were $2,488,000, $2,874,000, and $4,274,000 for the years ended June 30, 1998, 1997, and 1996, respectively.

Note 10 - Commitments and Contingencies

Leases

Certain operating properties are rented under non-cancelable operating leases which expire at various dates through 2009. Total rental expense under operating leases was $4,440,000 in 1998, $3,705,000 in 1997, and $2,722,000 in 1996. The following is a schedule of minimum rental commitments under non-cancelable operating leases, primarily for retail centers, in effect at June 30, 1998:

1999	$3,994,000
2000	3,055,000
2001	2,534,000
2002	1,818,000
2003	1,101,000
Thereafter	2,313,000

Repurchase Agreements

Institutions financing independent retailer purchases require the Company to execute repurchase agreements. As a result of these agreements, the Company is contingently liable for repurchasing homes 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.

Notes to Consolidated Financial Statements *(Continued)*

Note 11 - Industry Segment Information

The Company operates in three major business segments: Manufactured Housing, Financial Services, and Communities. The Manufactured Housing segment is engaged in the production, wholesale, and retail sale of manufactured homes. Financial Services includes retail financing of manufactured homes, reinsuring risk on family protection, physical damage, and homebuyer protection plan insurance policies, and certain specialty finance products. Communities is engaged in marketing and management of manufactured housing communities. Operating income consists of total revenues less cost of sales and operating expenses. 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 fixed assets.

Information concerning operations by industry segment follows:

(in thousands)	Manufactured Housing	Financial Services	Communities	Corporate	Total
1998					
Revenues	**$898,342**	**$ 158,697**	**$ 70,740**	**$ —**	**$1,127,779**
Operating income	**105,971**	**96,402**	**14,228**	**—**	**216,601**
Identifiable assets	**275,036**	**1,003,528**	**166,870**	**12,323**	**1,457,757**
Depreciation and amortization	**8,741**	**121**	**5,418**	**453**	**14,733**
Capital expenditures	**$ 20,868**	**$ 931**	**$ 31,316**	**$ 9,095**	**$ 62,210**
1997					
Revenues	$ 827,383	$ 124,076	$ 70,244	$ —	$ 1,021,703
Operating income	95,958	77,459	14,131	—	187,548
Identifiable assets	219,321	610,642	147,814	67,984	1,045,761
Depreciation and amortization	8,348	—	4,710	—	13,058
Capital expenditures	$ 21,404	$ —	$ 21,455	$ —	$ 42,859
1996					
Revenues	$ 761,111	$ 99,443	$ 68,187	$ —	$ 928,741
Operating income	89,504	62,600	15,600	—	167,704
Identifiable assets	197,938	493,622	142,331	52,459	886,350
Depreciation and amortization	6,671	—	4,492	—	11,163
Capital expenditures	$ 16,483	$ —	$ 24,346	$ —	$ 40,829

Note 12 - Other Assets and Liabilities

At June 30, 1998 and 1997, other assets and liabilities consisted of:

(in thousands)	**1998**	1997
Other Assets		
Interest receivable and future servicing rights	**$ 38,157**	$ 26,229
Prepaid expenses and other	**33,717**	26,282
	$ 71,874	$ 52,511
Other Liabilities		
Investors payable	**$ 86,804**	$ 69,847
Reserve for contingencies (Note 6)	**5,864**	3,134
Escrow deposits	**10,779**	15,220
Unearned insurance premiums	**65,048**	50,610
Other	**22,095**	16,046
	$190,590	$154,857

Note 13 - Fair Value Disclosure of Financial Instruments

SFAS No. 107, *Disclosures About Fair Value of Financial Instruments*, requires that CHI disclose the estimated fair values of its financial instruments. The following methodologies and assumptions were used by CHI to estimate its fair value disclosures for financial instruments.

Fair value estimates are made at a specific point in time, based on relevant market data and information about the financial instrument. The estimates do not reflect any premium or discount that could result from offering for sale in a single transaction CHI's entire holdings of a particular financial instrument. The lack of uniform valuation methodologies introduces a greater degree of subjectivity to these estimated fair values. Comparability to financial instruments between similar companies may not be reasonable because of varying assumptions concerning the estimates of fair value.

Cash and Cash Equivalents

The carrying values for cash and cash equivalents, including those restricted by agreement, approximate the fair value of the assets.

Residual Interests in Installment Contract Receivables

Residual interests in installment contract receivables are calculated using prepayment, default, and interest rate assumptions that the Company believes are appropriate at the time of the sale of the installment contract receivables. Projected performance is monitored after the sale. The fair value primarily assumes an appropriate discount rate to be applied to the asset as a whole.

Notes to Consolidated Financial Statements *(Continued)*

The Company used a discount rate and such other assumptions as it believed to be used for similar instruments. The Company has estimated the fair value of its residual interests in installment contract receivables to approximate its carrying value as of June 30, 1998 and 1997.

Contracts Held For Sale and as Collateral

Contracts held for sale are generally recent originations or purchased portfolios that will be sold with limited or no recourse during the following year. CHI does not charge fees to originate loans, and, as such, its contracts have origination rates in excess of rates on the securities into which they will be pooled. CHI estimates the fair value of the contracts held for sale using expected future cash flows of the portfolio discounted at the current origination rate.

The carrying values of contracts pledged as collateral to long-term lenders are estimated using discounted cash flow analyses and interest rates being offered for similar contracts. The carrying amount of contracts with a variable rate of interest is estimated to be at fair value. The carrying value of accrued interest adjusted for credit risk equals its fair value.

Debt Collateralized by Installment Contract Receivables

Debt collateralized by installment contract receivables consists primarily of notes collateralized by contracts with maturities that coincide with the underlying contract maturities. The fair value of these financial instruments is based on the current rates offered to CHI for debt of similar maturities using a discounted cash flow calculation. Loan covenants preclude prepayment.

The carrying amounts and estimated fair values of CHI's financial assets and liabilities are as follows:

	June 30, 1998		June 30, 1997	
(in thousands)	**Carrying Amount**	**Estimated Fair Value**	Carrying Amount	Estimated Fair Value
Financial assets:				
Cash and cash equivalents, including restricted investments and securities held-to-maturity	**$108,268**	**$108,554**	$181,053	$180,680
Residual interests in installment contract receivables	**127,705**	**127,705**	135,208	135,208
Contracts held for sale and as collateral, including accrued interest receivable	**673,847**	**661,069**	287,457	297,347
Financial liabilities:				
Debt collateralized by installment contract receivables	**$ 15,557**	**$ 16,469**	$ 22,670	$ 25,723

Note 14 - Earnings Per Share

Effective for the quarter ended December 31, 1997, the Company adopted SFAS No. 128, *Earnings per Share*. The statement simplifies the standards for computing earnings per share by replacing the presentation of primary earnings per share with a presentation of basic earnings per share. Prior years have been restated to reflect this change. Per share and share data have been retroactively adjusted to reflect 5-for-4 stock splits in December 1996 and December 1995. The following reconciliation details the numerators and denominators used to calculate basic and diluted earnings per share for the respective periods:

(in thousands except per share data)	**1998**	1997	1996
Net income	**$137,700**	$119,500	$106,800
Average shares outstanding:			
Basic	**118,770**	118,659	118,602
Add: common stock equivalents	**833**	818	744
Diluted	**119,603**	119,477	119,346
Earnings per share:			
Basic	**$1.16**	$1.01	$0.90
Diluted	**$1.15**	$1.00	$0.89

DIRECTORS & OFFICERS

BOARD OF DIRECTORS

Photo: Seated left to right, Kevin T. Clayton and James L. Clayton. Standing left to right, Wilma H. Jordan, C. Warren Neel, James D. Cockman, Thomas N. McAdams, B. Joe Clayton and Dan W. Evins.

James L. Clayton
Chairman of the Board and Chief Executive Officer, Clayton Homes, Inc.; Director, Dollar General Corporation and Chateau Communities, Inc.; Chairman of the Board, BankFirst

B. Joe Clayton
Chief Executive Officer, Clayton Automotive Group; Regional Director, First Tennessee Bank

Kevin T. Clayton
President and Chief Operating Officer; President, Financial Services

James D. Cockman (1)
Partner, WoofGang Brand Development

Dan W. Evins (1)
Chairman of the Board, Chief Executive Officer, Cracker Barrel Old Country Store, Inc.

Wilma H. Jordan (2)
Chief Executive Officer, The Jordan, Edmiston Group, Inc.; Director, LIN Television Corporation

Thomas N. McAdams (2)
Partner, Bernstein, Stair & McAdams L.L.P.; Director, Rafferty's, Inc.

C. Warren Neel (1)(2)
Dean, College of Business Administration, University of Tennessee; Director, O' Charleys, Inc., Proffitts', Inc., American Health Corp., Inc., and Promus Hotel Corporation

(1) Audit Committee (2) Compensation Committee

STOCKHOLDER INFORMATION

Form 10-K
Clayton Homes, Inc. Form 10-K Annual Report to the Securities and Exchange Commission is available without charge to shareholders upon written request to:
Investor Relations
Clayton Homes, Inc.
Box 15169
Knoxville, TN 37901

General Counsel
Bernstein, Stair & McAdams
Knoxville, Tennessee

S.E.C. Counsel
Baker, Donelson, Bearman and Caldwell
Nashville, Tennessee

Independent Accountants
PricewaterhouseCoopers LLP
Knoxville, Tennessee

Stock Exchange Listing
The Company's common shares are listed on the New York Stock Exchange, symbol CMH.

Shareholders
There were approximately 64,000 beneficial holders of common stock on June 30, 1998.

Registrar, Transfer Agent, and Dividend Reinvestment Plan Administrator
American Stock Transfer & Trust Company
40 Wall Street
New York, NY 10005
1.800.278.4353

Annual Meeting
The annual meeting of shareholders will be held on November 12, 1998, at 10:30 a.m. (EST) at the Clayton Homes Headquarters, 5000 Clayton Road, Maryville, TN 37804. Shareholders of record at close of business on September 14, 1998, will be entitled to vote.

CORPORATE OFFICERS

James L. Clayton
Chairman of the Board and Chief Executive Officer

Kevin T. Clayton
President and Chief Operating Officer
President, Financial Services

David M. Booth
Executive Vice President
President, Retail

Richard D. Strachan
Vice President
President, Manufacturing

Paul W. Boyd
Treasurer

Amber W. Krupacs
Vice President, Finance and Secretary

Greg A. Hamilton
Vice President and Controller

Clayton Homes, Inc.
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e-mail: info@clayton.net
Human resources: recruiting@clayton.net