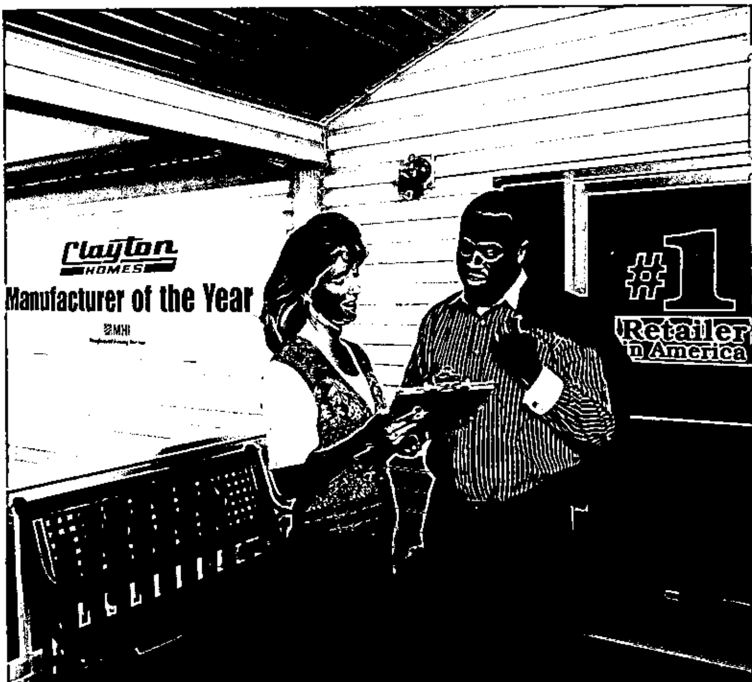
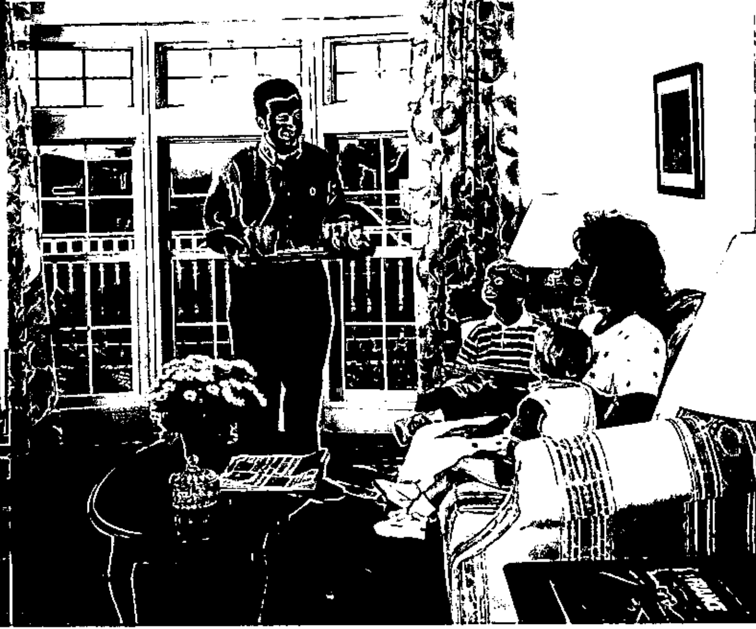


Clayton Homes, Inc.

ANNUAL
REPORT
2002



REPORT
2002

Company Profile

Headquartered in Knoxville, Tennessee, employing 6,800 people and operating in 33 states, Clayton Homes, Inc. builds, sells, finances and insures manufactured homes, and owns and operates residential manufactured housing communities. The Manufacturing Group is a leading producer of homes with 20 plants supplying 970 independent and Company-owned sales locations. The Retail Group sells, installs and services factory-built homes. As of June 30, 2002, Company-owned retail centers numbered 287 in 24 states. Financial Services provides financing and insurance for homebuyers of Company-owned and selected independent retail sales centers through Vanderbilt Mortgage and HomeFirst Insurance, wholly-owned subsidiaries. The Communities Group owns and operates 82 manufactured housing communities with 21,382 homesites in 12 states.

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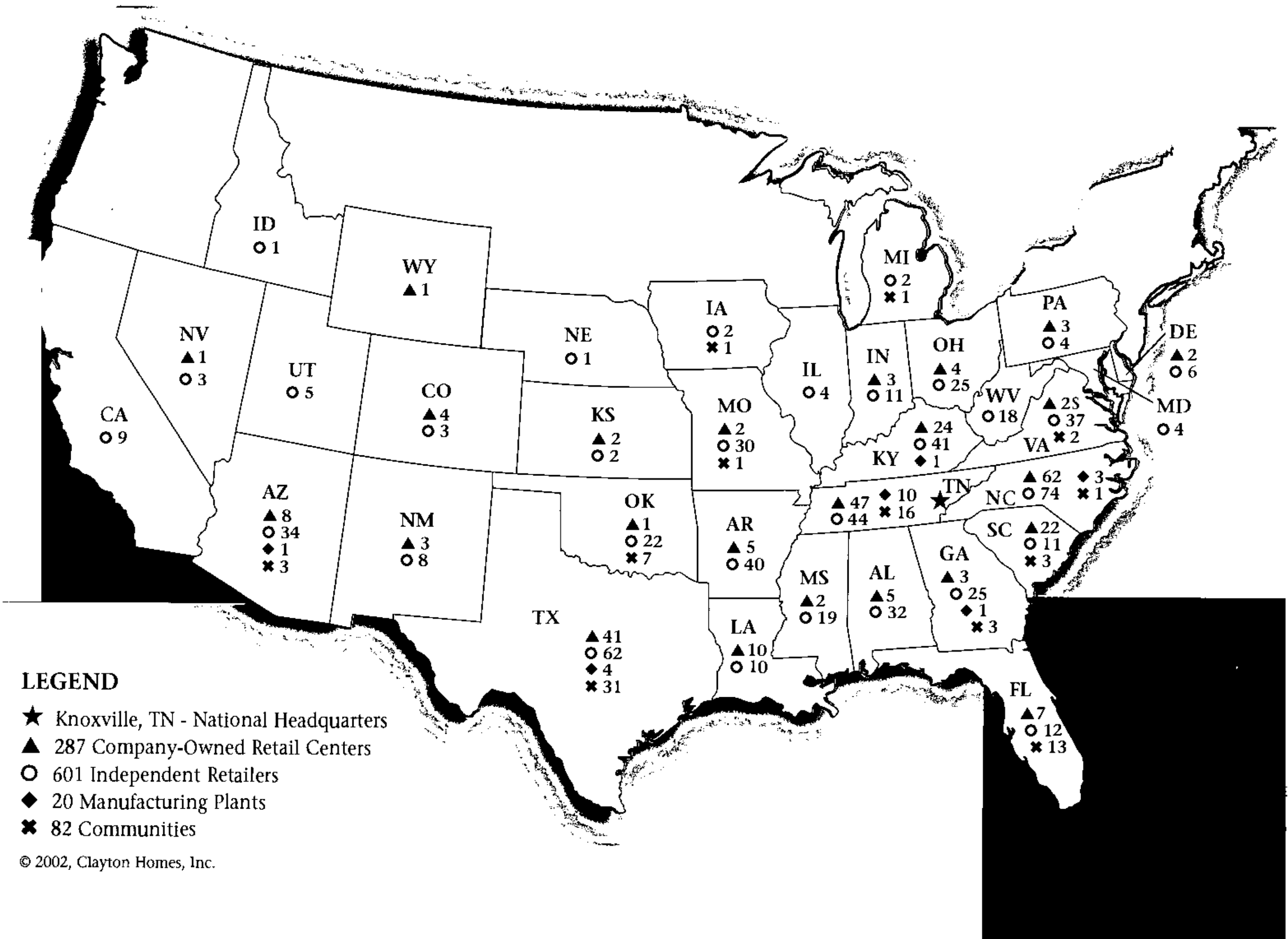

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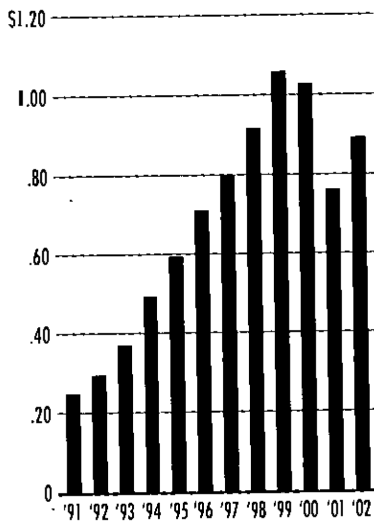
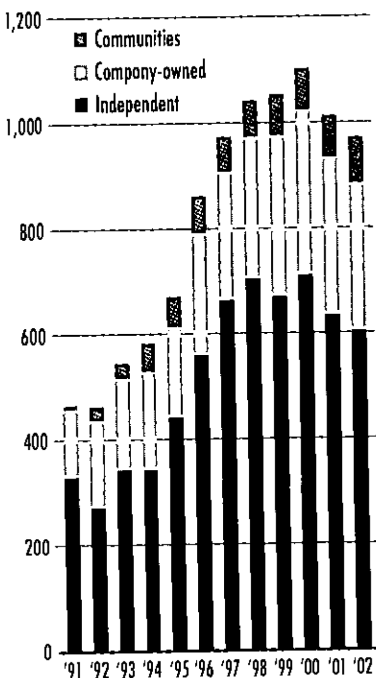
Financial Highlights

	(dollars in thousands, except per share)	Year ended June 30, 2002	2001	Percent Change
Income Statement Data	Revenues	$1,198,848	$1,150,956	4%
	Income before income taxes	197,046	169,351	16%
	Net income	124,146	106,651	16%
	Earnings per share			
	Basic	0.90	0.77	17%
	Diluted	0.89	0.77	16%
	Dividends per share	$.064	$.064	
Balance Sheet Data	Total assets	$1,828,403	$1,654,170	11%
	Shareholders' equity	$1,261,957	$1,147,478	10%
	Return on average shareholders' equity	10.3%	9.8%	
Portfolio Data	Loans serviced	$4,971,000	$4,309,000	15%
	Delinquency % (over 30 days)			
	Originated contracts	2.3%	2.1%	
	All contracts	2.8%	2.6%	
	Net losses as a % of average loans outstanding			
	Originated contracts	2.1%	1.7%	
	All contracts	2.2%	1.8%	
Other Data	Total floors sold	37,789	38,171	-1%
	Total homes sold	25,322	26,215	-3%
	National market share	11.6%	11.1%	
	Manufacturing plants	20	20	
	Independent retailers	601	634	-5%
	Company-owned retail centers	287	297	-3%
	Communities	82	81	1%
	Community home sites owned	21,382	21,121	1%
	Personnel count	6,784	6,554	4%

ANNUAL
REPORT
2002

To Our Shareholders



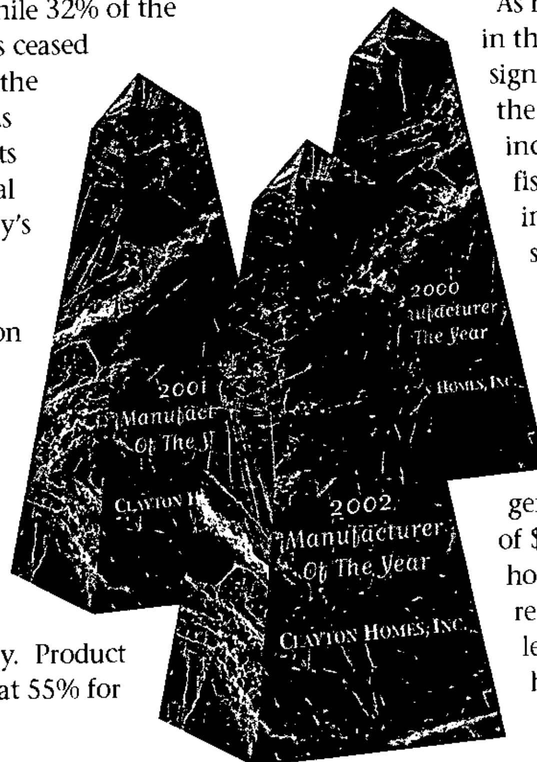


Clayton Homes set the industry benchmark in fiscal year 2002 by earning more than all public manufactured housing retailers and manufacturers combined. Clayton achieved its 28th consecutive profitable year, even as the manufactured housing industry experienced the third consecutive year of declining shipments. Revenues increased 4% to $1.2 billion, net income improved 16% to $124 million, and earnings per share grew 16% to $.89. Fourth quarter results were even more positive, with a 15% increase in revenues, a 31% gain in net income, and a 32% improvement in earnings per share. During the past ten years, tangible shareholders' equity has increased at a compound annual growth rate of 16%.

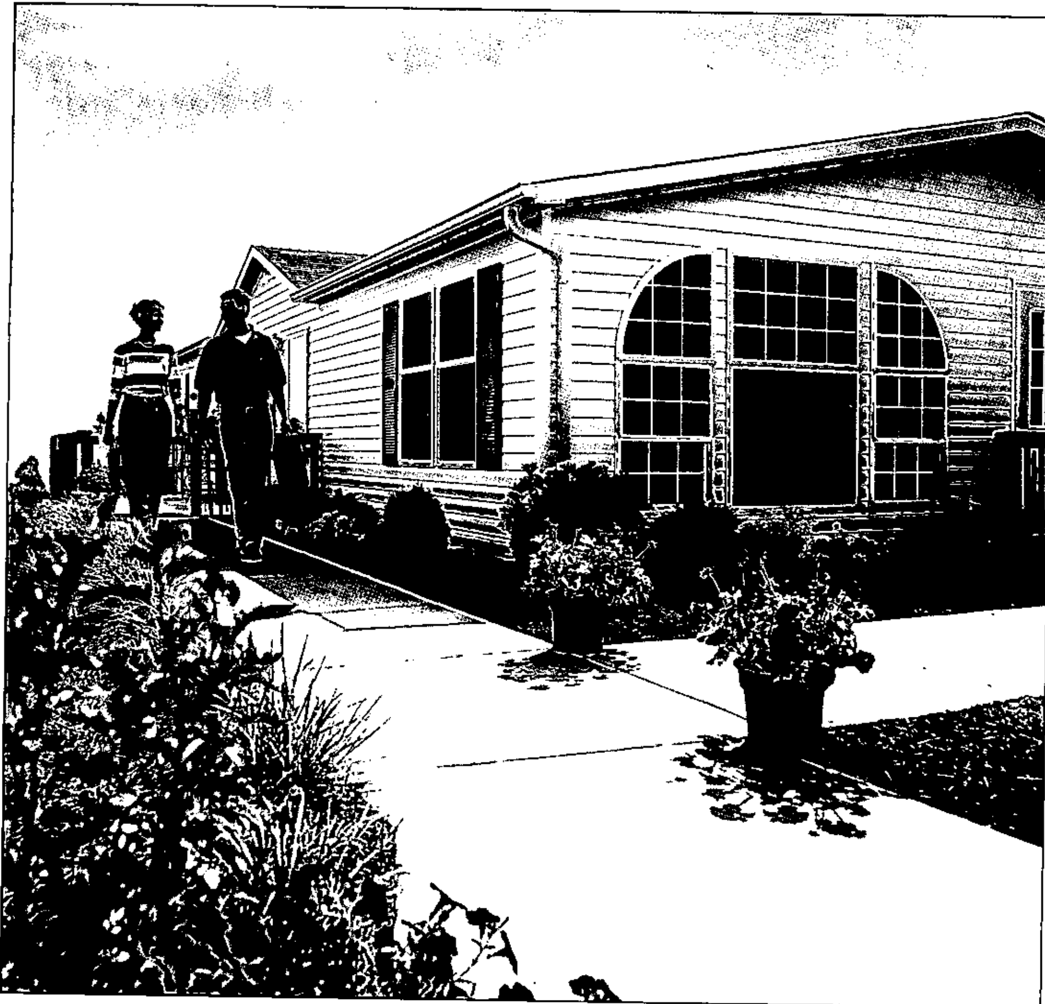
Market share in the top-ten industry states increased 2% to 14%, confirming the inherent strength of Clayton's unique open vertical integration model, which serves your Company especially well in market downturns. The Manufacturing Group delivered profitable results without closing a plant, while 32% of the industry's factories ceased to operate during the last three years. As industry shipments fell 6% in the fiscal year, the Company's home production increased 2.5%. Capacity utilization improved to 60% for the year, even as excess manufacturing capacity and high retailer inventories continued to strain the industry. Product mix was divided at 55% for multi-section homes versus 45% for single section, and Clayton is now the third largest manufacturer.

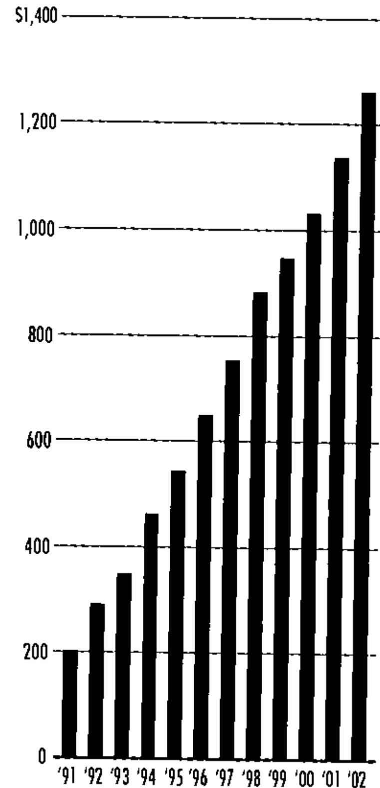
Retail distribution is the center point of Clayton's open vertical integration concept. Clayton's 20 plants serve 970 retailers in 33 states: 601 are independent and 369 are Company-owned. This stable cross section of quality retailers provides consistent demand through industry cycles and enables a rapid response to customer demands and preferences.

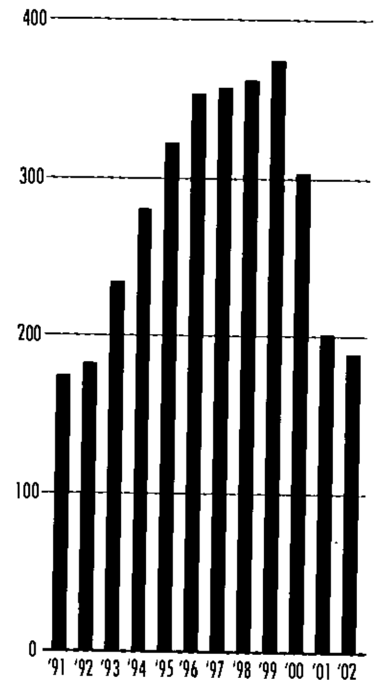
For the third consecutive year, the Manufactured Housing Institute named Clayton Homes "Manufacturer of the Year." This prestigious national honor is bestowed by industry peers and is a tribute to all Clayton team members for their consistent efforts to deliver quality homes and legendary customer satisfaction. Material suppliers increased their level of support as they adopted electronic ordering, just-in-time supply processes, and other technology enhancements, while continuing to provide quality components at favorable prices.



As most retail organizations in the industry suffered significant sales declines, the Clayton Retail Group increased sales 5% in fiscal 2002. Even more importantly, Clayton same-store sales dollars increased 12% for the year. Your Company now owns and operates 287 stores in 24 states, which sold 15,877 homes and generated sales revenues of $616 million. New home inventory per store remained at a conservative level of 17.3, and used home inventory declined





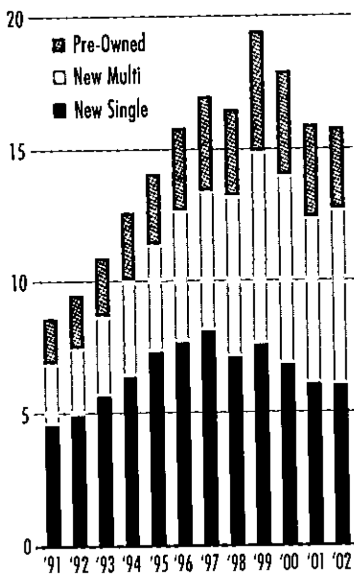


20% to 3.6 homes per store. Our internal key market survey indicates that the number of competitors has decreased 7% since last June and 38% since the number of industry stores peaked in June of 1999. Foreclosure levels remain a major concern in the manufactured housing industry; however Clayton reduced inventories by 7% during the year to 1,255 homes at Company stores — the second consecutive year of improvement.

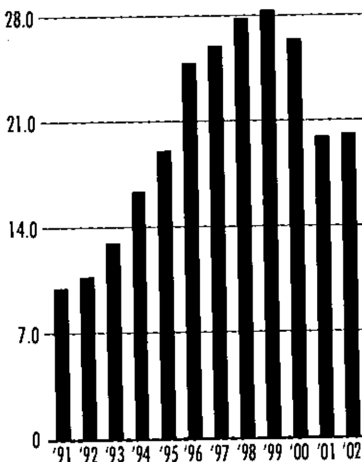
Texas laws regarding chattel lending changed on January 1, 2002, requiring a real estate transaction when the homebuyer also has legal title to the property. The new law contributed to an 11% shipment decline to the industry's number one state. The Retail Group proactively teamed with Vanderbilt Mortgage and the Texas Manufactured Housing Association to interpret and prepare for the new legislation. Training classes began in November and continued through the early winter months. The process was challenging, but the Clayton team outperformed the industry with a 5% same-store sales increase in Texas.

The Financial Services Group originated $913 million in mortgages and completed $1.2 billion in acquisitions for the year, growing the serviced portfolio by 15% to $5 billion. Vanderbilt's synergistic partnership with the Company's retail group again delivered favorable mortgage servicing results, achieving the year-end delinquency goal of 2.29%. This counterintuitive open vertically integrated concept provides complementary focus for the sales and finance teams, which are usually

Homes Retailed (in thousands)

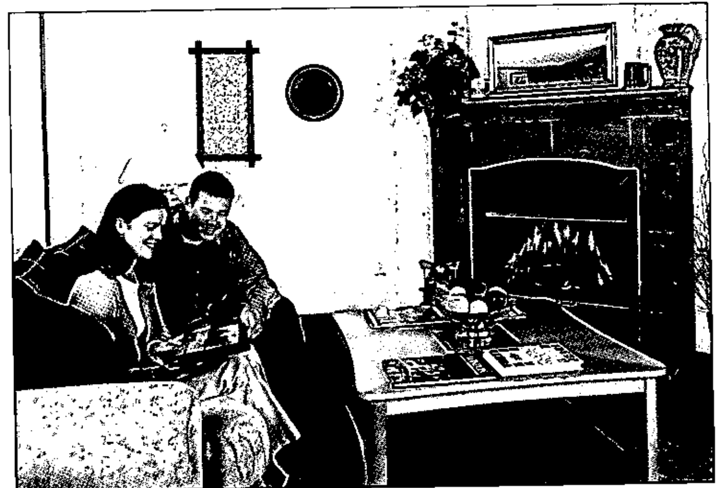


Clayton Homes Built (in thousands)



expected to clash. Not only are the sales staff accountable for pre-underwriting their mortgage applications, but they are responsible for the local field servicing of the accounts originated by the team. Of course the primary responsibility for the underwriting decision remains in the credit unit at Vanderbilt, where technology is increasingly utilized.

Clayton Homes retains its long-term approach to managing the Financial Services Group by applying rigid underwriting guidelines and servicing fundamentals, which ensures income generation through all phases of the industry cycle. Vanderbilt resists the temptation to follow the competition as credit standards are lowered during the top of industry and economic cycles. Recoveries from defaulted mortgages tend to be high and losses low during the peaks, but during the sometimes extended troughs, mortgages that were not underwritten and/or serviced properly result in very high losses. Many of our lending competitors failed to take into account the extent of this predictable phenomenon.

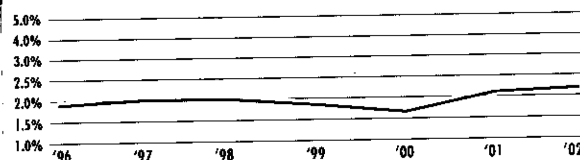


Mortgage and insurance product offerings deliver reliable streams of future income as more than 160,000 customers make their monthly mortgage payments and 105,000 families are protected through Company insurance policies. Within hours of occupancy, Clayton contacts homebuyers to verify that they are satisfied with their home and that the mortgage terms are accurately documented. Homeowner approval is reconfirmed six months later with another customer interview.

The Communities Group provided a valuable stream of revenues and income during a challenging year. In 2002, Communities expanded its portfolio to 82 properties with 21,382 sites. A new acquisition was finalized in Lavon, Texas, adding 111 sites in the initial phase, and another four communities were expanded by 150 sites. Same-store occupancy rates increased 2% while overall occupancy increased to 76%. Same-store rental revenue increased 2% for the year, as sales improved 2%. Clayton Communities are home to 16,129 families.

When a home is sold in a Clayton community, five levels of profit may be realized: manufacturing, retail, finance, insurance and site rental. This is a distinct Clayton conceptual advantage.

Loan Delinquency (Vanderbilt Loan Originations)



Summary operating highlights for the year included:

- Awarded Manufacturer of the Year by the Manufactured Housing Institute for the third consecutive year
- Operated all 20 plants profitably

- Increased Retail same-store sales by 12%
- Reduced Retail foreclosure inventory for the second consecutive year
- Expanded Vanderbilt's mortgage servicing to $5 billion
- Achieved Financial Services' year-end delinquency target of 2.29%
- Improved operating margins from 14.8% to 16.8% of revenues
- Increased tangible Shareholder Equity 10% to $1.26 billion.

Now our attention is focused on fiscal year 2003. Shareholder value will be enhanced by leveraging the Company's core competencies: producing and retailing affordable, high-value homes; well executed mortgage originations and servicing; prudent balance sheet management; and continuous improvement in team member selection, training, and retention.

Goals for 2003 include:

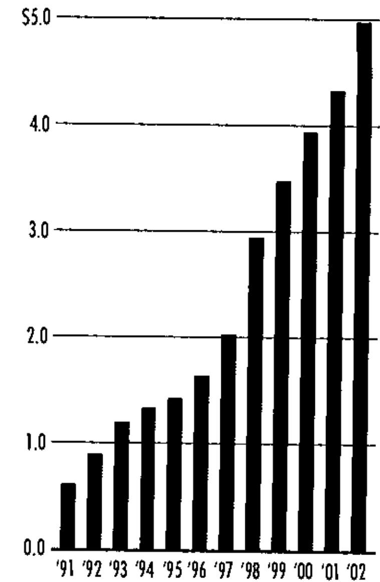
- Enhance customer and team member satisfaction programs
- Expand independent retailer base
- Increase same-store sales 10%
- Expand loan servicing to $5.5 billion
- Add two new communities
- Support neighborhoods where we live and work
- Improve return on equity.

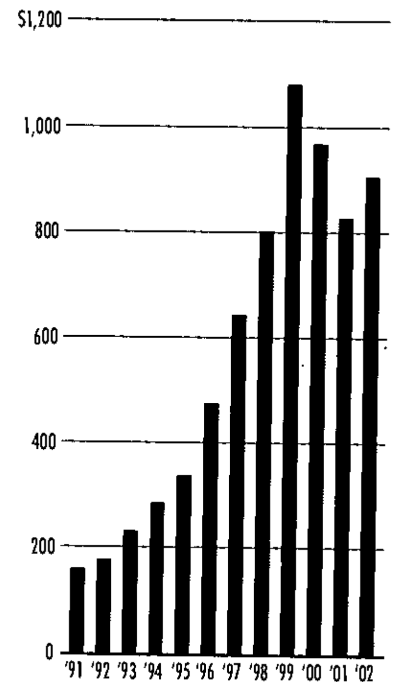
The Clayton business model works! With a proprietary brand of open vertical integration and a truly seasoned team, Clayton Homes is the best-positioned manufactured housing company for the expected industry recovery. With a conservative balance sheet of only 7% debt to capital, Clayton Homes is one of the few industry participants able to acquire attractive assets at value prices. Our strategic plan entails preserving the Company's strong fundamentals while capitalizing on opportunities that will materialize as the cycle matures. Culture, unique concept, and team member values make Clayton Homes different. As always, we thank Clayton shareholders for support as we continue leading the Company to maximize long-term results.

James L. Clayton
Chairman of the Board

Kevin T. Clayton
Chief Executive Officer and President

Retail Group	June 30, 2002	June 30, 2001	Percent Change
Sales (in millions)			
New homes	$571.7	$538.8	+6%
Used homes	44.5	47.5	-6%
Total	$616.2	$586.3	+5%
Homes Sold (units)			
New single-section	6,060	6,132	-1%
New multi-section	6,712	6,214	+8%
Total new	12,772	12,346	+3%
Used	3,105	3,556	-13%
Total	15,877	15,902	flat





(in thousands except per share and other data)	2002	2001	2000	1999	1998	1997	1996	1995	1994	1993	1992
INCOME STATEMENT DATA											
Revenues											
Net sales	**$ 871,108**	$ 849,157	$ 993,916	$1,040,668	$ 880,856	$ 822,906	$762,396	$621,351	$510,153	$384,491	$296,849
Financial services and other income	**327,740**	301,799	299,429	303,615	246,923	198,797	166,345	136,741	118,083	91,750	74,330
	1,198,848	1,150,956	1,293,345	1,344,283	1,127,779	1,021,703	928,741	758,092	628,236	476,241	371,179
Costs and expenses											
Cost of sales	**565,322**	562,267	660,429	705,128	598,589	559,274	521,200	431,826	357,698	267,201	206,049
SG&A	**406,655**	374,628	384,067	367,430	302,598	270,996	236,188	188,835	153,698	113,695	84,785
Financial services interest	**404**	706	1,032	7,981	2,015	2,885	3,649	5,533	8,196	11,819	16,585
Provision for credit losses	**25,100**	42,500	20,800	12,459	7,976	1,000	–	–	–	–	3,300
	997,481	980,101	1,066,328	1,092,998	911,178	834,155	761,037	626,194	519,592	392,715	310,719
Operating income	**201,367**	170,855	227,017	251,285	216,601	187,548	167,704	131,898	108,644	83,526	60,460
Interest income (expense), net/other	**(4,321)**	(1,504)	1,608	(5,317)	5,499	5,152	4,596	3,902	(359)	(170)	(317)
Income before income taxes	**197,046**	169,351	228,625	245,968	222,100	192,700	172,300	135,800	108,285	83,356	60,143
Provision for income taxes	**(72,900)**	(62,700)	(84,600)	(91,000)	(84,400)	(73,200)	(65,500)	(48,800)	(39,000)	(29,600)	(20,800)
Income before accounting change	**124,146**	106,651	144,025	154,968	137,700	119,500	106,800	87,000	69,285	53,756	39,343
Cumulative effect of accounting change	–	–	–	–	–	–	–	–	3,000	–	–
Net income	**$ 124,146**	$ 106,651	$ 144,025	$ 154,968	$ 137,700	$ 119,500	$106,800	$ 87,000	$ 72,285	$ 53,756	$ 39,343
Net income per share											
Basic	**$0.90**	$0.77	$1.03	$1.07	$0.93	$0.81	$0.72	$0.59	$0.51	$0.39	$0.30
Diluted	**$0.89**	$0.77	$1.03	$1.06	$0.92	$0.80	$0.72	$0.59	$0.49	$0.37	$0.29
Average shares outstanding											
Basic	**137,726**	137,702	139,474	145,211	148,463	148,324	148,253	147,020	141,046	136,391	130,103
Diluted	**138,872**	138,340	139,815	145,931	149,504	149,346	149,183	148,285	149,875	149,106	142,100
Dividends per common share	**$.064**	$.064	$.064	$.064	$.064	$.061	$.049	$.030	–	–	–
BALANCE SHEET DATA											
Total assets	**$1,828,403**	$1,654,170	$1,506,378	$1,417,245	$1,457,757	$1,045,761	$886,350	$761,151	$701,148	$587,032	$554,780
Debt obligations	**92,912**	141,862	99,216	96,477	247,591	22,806	30,290	48,737	70,680	137,038	192,931
Shareholders' equity	**$1,261,957**	$1,147,478	$1,036,375	$ 947,768	$ 881,019	$ 754,526	$650,189	$544,187	$462,154	$348,630	$292,950
KEY FINANCIAL RATIOS											
As a % of revenue											
Operating income	**16.8%**	14.8%	17.6%	18.7%	19.2%	18.4%	18.1%	17.4%	17.3%	17.5%	16.3%
Net income	**10.4%**	9.3%	11.1%	11.5%	12.2%	11.7%	11.5%	11.5%	11.5%	11.3%	10.6%
Debt as a % of total capital	**6.9%**	11.0%	8.7%	9.2%	21.9%	2.9%	4.5%	8.2%	13.3%	28.2%	39.7%
OTHER DATA											
Company-owned retail centers	**287**	297	318	306	273	245	216	192	165	143	127
Independent retailers	**601**	634	707	671	702	663	580	421	372	371	312
Manufacturing plants	**20**	20	20	19	18	17	17	16	13	13	11
Communities	**82**	81	76	75	71	67	64	55	46	33	20

Critical Accounting Policies

The Company believes the following represents its critical accounting policies:

Revenue Recognition

Retail sales are recognized when: 1) Cash payment is received, or down payment is received for credit sales and the home buyer enters into an installment sales contract, and 2) The home buyer has inspected and accepted the completed home at the home buyer's site, and 3) Title has passed to the home buyer.

Sales to independent retailers of homes produced by the Company are recognized as revenue upon shipment.

Revenue from rental of homesites and homes is accrued and recognized based on the terms of the resident's lease agreement with the Company.

Premiums from insurance policies represent short-duration contracts with terms of one to 10 years and are deferred and recognized as revenue over the terms of the policies.

Vanderbilt Mortgage and Finance, Inc. (VMF), the Company's financing subsidiary, originates and sells installment contract and mortgage loan receivables (receivables), retaining the servicing thereon. It also provides servicing for investors in receivables on a contract basis. Interest income on receivables held, either for sale or as an investment, is recognized in accordance with the terms of the underlying installment contracts. For receivables sold with servicing retained and receivables serviced under servicing agreements, service fee income is recognized as the service is performed. Interest income on interest-only residual interests is recognized in accordance with the consensus of the Emerging Issues Task Force in its Issue No. 99-20 (EITF 99-20), *Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Assets.* Accordingly, interest income is recognized through an effective yield method, with the yield computed prospectively over the life of the residual interests after adjustments in the estimated cash flows are made to reflect prepayments, defaults and other factors.

Valuation of Residual Interests

The Company engages in securitization activities in connection with certain of its businesses. Gains and losses from securitizations are recognized in the consolidated statements of income when the Company relinquishes control of the transferred financial assets in accordance with SFAS No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities.* The gain or loss on the sale of financial assets depends in part on the previous carrying amount of the assets involved in the transfer, allocated between the assets sold and the retained interests based upon their respective fair values at the date of the sale.

Interest-only securities are periodically valued using a discounted cash flow model. The future cash flows for the estimated life of each securitized pool are projected as the excess interest received from borrowers over the interest paid to the security holders, less contractual servicing fees and estimated credit losses, after giving effect to estimated prepayments. Estimates for prepayments, defaults, and losses are determined based on a model developed by the Company that considers both Company-specific experience and current economic conditions.

The residual interests in the installment receivables sold are classified as available-for-sale securities. Accordingly, changes in fair market value are recorded as other comprehensive income (loss) unless an other than temporary adverse change is determined. Those impairment charges are reflected in net income.

Reserves for Credit Losses and Contingent Liabilities

Reserves for credit losses and contingent liabilities are established for receivables held for sale or investment and certain inventory. 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.

Results of Operations

Fiscal 2002 compared to Fiscal 2001

Total revenues increased 4% to $1.2 billion, as manufactured housing sales increased 3% to $871 million, financial services income increased 11% to $252 million and rental and other income increased 2% to $75 million. Total units sold declined 3% to 25,322 from 26,215 last year as total floors shipped declined 1% to 37,789 from 38,171 in the prior year.

Gross profit margins on retail, manufacturing and communities sales increased to 35.1% from 33.8%, primarily due to a higher rate of internalization of retail sales, improved efficiencies, and higher average retail and wholesale selling prices. Selling, general and administrative expenses were 33.9% and 32.5% of revenues for the years ended June 30, 2002, and 2001, respectively. Additional costs associated with portfolio acquisitions contributed to the increase. The provision for credit losses was $25.1 million (excluding $40.2 million that has been included in Financial Services revenue for 2002 related to the losses on securitized mortgages), as compared to $42.5 million last year. This combined increase was primarily due to the additional contracts in foreclosure from the same period last year. Operating margin increased to 16.8% from 14.8% last year.

Interest and other expense increased to $4.3 million. This increase was partially due to an overall declining interest rate outlook which adversely impacted the value of the Company's interest rate swaps. During the fiscal year ended June 30, 2002, there was an unfavorable mark-to-market adjustment of $3.3 million relating to the swaps, as compared to a $2.1 million unfavorable adjustment in the same period last year. Income tax for the year ended June 30, 2002, was $72.9 million, which represents an effective tax rate of 37%.

Conditions in the manufactured housing industry remain highly competitive at both the retail and wholesale levels. For fiscal 2002, the industry was faced with manufacturing over-capacity and too many retail centers. This competitive environment, as well as an increase in industry foreclosures and aging retail inventory, has contributed to the idling and closing of manufacturing plants, and declining wholesale shipments resulting in significant closings of retail centers.

Retail. Within the Retail segment, the group experienced a 5% increase in net sales to $616 million as the total number of homes sold decreased slightly to 15,877 and the average home price increased 5%. The average number of homes sold per sales center increased 5% as same store sales dollars increased 12%. The average number of Company-owned retail centers declined 5%. Retail segment operating income increased 12% to $32 million from $29 million last year.

	Year ended June 30, 2002	2001	% Change
Dollar sales (in thousands)	$616,224	$586,261	5.1%
Number of retail centers (average)	292	308	-5.0%
Dollar sales per retail center (in thousands)	$ 2,110	$ 1,907	10.7%
Average price of home	$ 38,812	$ 36,867	5.3%
New homes sold	12,772	12,346	3.5%
Previously-owned homes sold	3,105	3,556	-12.7%
Percentage single-section/multi-section mix (new only)	47/53	50/50	

During the year, the Company opened seven retail centers and closed 17 under-performing retail centers. The Company continually evaluates specific markets and opens, acquires or closes retail centers as conditions warrant. Of the seven new openings, six were acquired and one was a startup. Four of the new retail centers were opened in the fourth quarter.

Manufacturing. Within the Manufacturing segment, the group experienced a 4% decline in net sales to independent retailers to $215 million, while the number of homes sold decreased 10% to 8,240. The average number of independent retailers decreased 8%. Manufacturing segment operating income increased 28% to $47 million from $37 million in the prior year. Capacity utilization increased to 60%, as compared to 57% last year. On June 30, 2002, the order backlog for the Manufacturing group (consisting of Company-owned and independent retailer orders) decreased 36% to $22 million, compared to $35 million last year.

	Year ended June 30, 2002	2001	% Change
Dollar sales (wholesale - in thousands)	$214,769	$223,476	-3.9%
Number of plants operating	20	20	–
Number of independent retailers (average)	618	671	-7.9%
Dollar sales per independent retailer (in thousands)	$ 348	$ 333	4.4%
Average price of home	$ 26,064	$ 24,507	6.4%
New homes sold to independent retailers	8,240	9,119	-9.6%
Percentage single-section/multi-section mix	39/61	45/55	

Financial Services. Financial Services revenues increased 12% to $206 million, primarily due to a larger servicing portfolio and improved spreads over last year. Insurance related revenues increased $4 million, primarily attributable to the impact of multi-year policies generated in prior periods. Receivable originations of $913 million and acquisitions of $1.2 billion were completed during the year, bringing the total serviced portfolio to $5.0 billion, an increase of 15% over the prior year. Loans sold through asset-backed securities totaled $1.9 billion, as compared to $886 million last year. Overall delinquency (past due over 30 days) increased slightly to 2.8% from 2.6% last year. Total Financial Services operating income increased 31% to $125 million.

The average outstanding balance of installment contract and mortgage receivables increased 19% to $520 million with a weighted average interest rate of 9.0%, down from 9.8%. The average outstanding balance of receivables sold rose 12% to $4.1 billion, and the weighted average loan service spread increased to 3.5% from 3.4%. Net credit losses, including losses on securitized mortgages, as a percentage of loans outstanding for fiscal 2002 increased to 2.2% from 1.8%.

Communities. Within the Communities segment revenues, net sales increased 2% to $40 million as the number of homes sold increased 1% and the average home selling price increased 1%. Communities rental income rose 2%. Segment operating income declined 1%. The Company added 261 sites during the year bringing the total to 21,382 sites at June 30, 2002.

	Year ended June 30, 2002	2001	% Change
Dollar sales (in thousands)	$40,115	$39,420	1.8%
Average number of communities	82	79	3.8%
Dollar sales per community (in thousands)	$ 492	$ 502	-2.0%
Average price of home	$33,290	$33,015	0.8%
New homes sold	724	755	-4.1%
Previously-owned homes sold	481	439	9.6%
Sites owned	21,382	21,121	1.2%
Sites rented	16,156	15,737	2.7%
Percent occupied	75.6%	74.5%	

Fiscal 2001 compared to Fiscal 2000

Total revenues decreased 11% to $1.2 billion, as manufactured housing sales decreased 15% to $849 million, financial services income decreased slightly to $228 million and rental and other income increased 4% to $74 million. Total units sold declined 17% to 26,215 from 31,520 last year as total floors shipped declined 16% to 38,171 from 45,384 in the prior year.

Gross profit margins on retail, manufacturing and communities sales increased to 33.8% from 33.6%. Selling, general and administrative expenses were 32.5% and 29.7% of revenues for the years ended June 30, 2001, and 2000, respectively. This increase was primarily due to a decline in overall sales volume and reduced capacity utilization in manufacturing. Additional costs associated with portfolio acquisitions and fixed costs being spread over lower revenues were also a factor. The provision for credit losses and contingent liabilities increased to $42.5 million in 2001 from $20.8 million in 2000, which was primarily due to the additional number of contracts in foreclosure as compared to the same period last year. Operating margin decreased to 14.8% from 17.6% last year.

Interest and other expense increased to $2 million. This increase was partially due to an overall declining interest rate outlook which adversely impacted the value of the Company's interest rate swaps. During the fiscal year ended June 30, 2001, there was an unfavorable mark-to-market adjustment of $2.1 million relating to the swaps. Income tax for the year ended June 30, 2001, was $62.7 million, which represented an effective tax rate of 37%.

Conditions in the manufactured housing industry remain highly competitive at both the retail and wholesale levels. For fiscal 2001, the industry was faced with manufacturing over-capacity and too many retail centers. This competitive environment, as well as an increase in industry foreclosures and aging retail inventory, has contributed to decreased industry and Company sales, and significant closings of retail centers.

Retail. Within the Retail segment, the group experienced a 13% decrease in net sales to $586 million as the total number of homes sold decreased 11% to 15,902 and the average home price decreased 1%. The average number of homes sold per sales center decreased 10% as same store sales dollars decreased 14%. The average number of Company-owned retail centers declined 1%. Retail segment operating income decreased 46% to $29 million from $54 million.

	Year ended June 30, 2001	2000	% Change
Dollar sales (in thousands)	$586,261	$670,038	-12.5%
Number of retail centers (average)	308	312	-1.4%
Dollar sales per retail center (in thousands)	$ 1,907	$ 2,148	-11.2%
Average price of home	$ 36,867	$ 37,365	-1.3%
New homes sold	12,346	14,022	-12.0%
Previously-owned homes sold	3,556	3,910	-9.1%
Percentage single-section/multi-section mix (new only)	50/50	49/51	

During the year, the Company opened seven retail centers and closed 28 under-performing retail centers. The Company continually evaluates specific markets and opens, acquires or closes retail centers as conditions warrant. All of the sales centers opened in fiscal 2001 were acquisitions. Two of the new retail centers were opened in the fourth quarter.

Manufacturing. Within the Manufacturing segment, the group experienced a 20% decrease in net sales to independent retailers to $223 million, while the number of homes sold decreased 26% to 9,119. The average number of independent retailers decreased 3%. Manufacturing segment operating income decreased 42% to $37 million from $63 million in the prior year. Capacity utilization decreased to 57%, compared to 77% last year. On June 30, 2001, the order backlog for the Manufacturing group (consisting of Company-owned and independent retailer orders) increased 118% to $35 million, compared to $16 million last year.

	Year ended June 30, 2001	2000	% Change
Dollar sales (wholesale - in thousands)	$223,476	$278,943	-19.9%
Number of plants operating	20	20	-
Number of independent retailers (average)	671	689	-2.7%
Dollar sales per independent retailer (in thousands)	$ 333	$ 405	-17.7%
Average price of home	$ 24,507	$ 22,776	7.6%
New homes sold to independent retailers	9,119	12,247	-25.5%
Percentage single-section/multi-section mix	45/55	51/49	

Financial Services. Interest and loan servicing revenues within the Financial Services segment increased $16 million. Insurance related revenues rose $6 million. Receivable originations of $815 million and acquisitions of $315 million were completed during the year, bringing the total serviced portfolio to $4.3 billion. Loans sold through asset-backed securities totaled $886 million, compared to $1.2 billion last year. Overall delinquency (past due over 30 days) increased to 2.6% from 2.2% last year. Total Financial Services operating income decreased 12% to $95 million.

The average outstanding balance of installment contract and mortgage receivables declined slightly to $437 million with a weighted average interest rate of 9.8%, down from 11.9%. The average outstanding balance of receivables sold rose 12% to $3.7 billion, and the weighted average loan service spread increased to 3.4% from 3.3%.

Net credit losses as a percentage of loans outstanding for fiscal 2001 increased to 1.8% from 1.4% while delinquency rates on all loans increased to 2.6% on a unit basis from 2.2%.

Communities. Within the Communities segment revenues, net sales decreased 12% to $39 million as 11% fewer homes were sold and the average home selling price decreased 1%. Communities rental income rose 8%. Segment operating income declined 13%. The Company added 953 sites during the year bringing the total to 21,121 sites at June 30, 2001.

	Year ended June 30, 2001	2000	% Change
Dollar sales (in thousands)	$ 39,420	$ 44,935	-12.3%
Average number of communities	79	76	4.0%
Dollar sales per community (in thousands)	$ 502	$ 595	-15.6%
Average price of home	$ 33,015	$ 33,509	-1.5%
New homes sold	755	862	-12.4%
Previously-owned homes sold	439	479	-8.4%
Sites owned	21,121	20,168	4.7%
Sites rented	15,737	15,177	3.7%
Percent occupied	74.5%	75.3%	

Liquidity and Capital Resources

The Company anticipates meeting cash requirements with proceeds from asset-backed securitizations, cash provided from operations, revolving credit lines, a sales facility and long-term debt. A principal strength of the Company is its ability to access global capital markets; continued access to the public and private capital markets is critical to the Company's ability to continue to fund its finance operations. During the year ended June 30, 2002, the Company raised $1.82 billion through asset securitizations as compared to $886 million in the prior year period. The origination and acquisition of installment contract receivables used $1.96 billion in 2002 and $1.14 billion in 2001.

Cash and cash equivalents at June 30, 2002, were $84 million as compared to $48 million at June 30, 2001. Cash provided by operating activities was $97 million for the year ending June 30, 2002, as compared to $50 million last year. Cash used for investing activities was $8 million, as compared to $82 million last year. In addition, $53 million in cash was used for financing activities, mostly for repayment of short-term lines of credit, as compared to $36 million provided by financing activities in the same period last year. The Company had restricted cash balances of $126 million at June 30, 2002, which includes trust account cash balances required by certain VMF servicing agreements, and insurance reserves required by ceding companies. The majority of the restricted cash balance represents funds held in accordance with certain servicing agreements that will be disbursed within 15 days of the end of the accounting period.

At June 30, 2002, and at June 30, 2001, the Company had debt outstanding of $93 million and $142 million, respectively. Debt outstanding principally consists of $75 million of privately issued senior notes, $2 million of installment paper collateralized debt and $15 million of tax-exempt bonds. The Company's debt to total capital ratio decreased to 7% as compared to 11% last year. Short-term debt available consists of $165 million committed and $71 million uncommitted lines of credit. These lines of credit do not require collateral and are priced on LIBOR rates. The committed credit lines are guaranteed by all significant subsidiaries of the Company and are governed by various financial covenants that require maintenance of certain financial ratios.

The Company has $75 million of 6.25% Senior Notes due December 30, 2003, which are primarily to facilitate the purchase, origination and warehousing of loan portfolios. The Senior Notes are guaranteed by all significant subsidiaries of the Company and are governed by various

financial covenants that require maintenance of certain financial ratios.

On December 21, 2001, the Company acquired manufactured housing installment contract receivables with an aggregate outstanding principal balance of $900 million. In conjunction with that transaction, the Company sold the receivables through a committed one-year sales facility of $500 million, while retaining the servicing rights and residual cash flows. This facility was not utilized at June 30, 2002, and was subsequently amended to $300 million of which $150 million is committed. In addition, a committed one-year $150 million participation facility is also available to facilitate the future sale of manufactured housing contracts. This participation facility was not utilized at June 30, 2002. In accordance with the agreements of the sales facility, utilization of any unfunded commitment is permitted as long as criteria, that includes credit rating, financial covenants, and performance triggers, are met. The Company owns its inventory; therefore, no inventory financing arrangements are necessary.

The following table summarizes the Company's significant contractual obligations and other contingencies as of June 30, 2002:

(in thousands)

Contractual Obligations (1)	Payments due by period						
	Total	FY03	FY04	FY05	FY06	FY07	Thereafter
Debt obligations	$ 92,912	$ 2,097	$ 75,325	$ 134	$ 35	$ -	$ 15,321
Capital leases	$ 532	$ 291	$ 241	$ -	$ -	$ -	$ -
Operating leases	$ 10,762	$ 3,620	$ 2,648	$ 1,826	$ 1,199	$ 688	$ 781

Other Contingencies (2)	Amount of contingency expiration per period						
	Total	FY03	FY04	FY05	FY06	FY07	Thereafter
Letters of credit	$127,203	$127,203	$ -	$ -	$ -	$ -	$ -
Guarantees	$416,661	$ 610	$ 2,154	$ 3,016	$26,539	$30,751	$ 353,591
Repurchase agreements	$ 59,600	$ 59,600	$ -	$ -	$ -	$ -	$ -

(1) Debt obligations consist primarily of $75 million Senior Notes due December 2003, and $15 million tax-exempt bonds due through 2030. Capital leases represent amounts due on computer-related equipment. Operating leases represent minimum rental commitments primarily for retail centers in effect on June 30, 2002.

(2) Letters of credit primarily relate to insurance reserves and guarantees relate to asset-backed securitizations. The Company believes the probability of having to make guarantee payments under the terms of the guarantees is remote. The repurchase agreements represent the maximum potential repurchase obligations in the event of a default by an independent retailer to the institution providing its floorplan lending. These agreements are customary in the manufactured housing industry, and the Company's losses in the past have not been significant.

In fiscal 2002, the Company repurchased 827,000 shares of Company common stock for $9.6 million. Under Board approved repurchase programs, all shares may be acquired, at management's discretion, over time on the open market. Shares repurchased are retired.

Acquisitions of property, plant and equipment were made of approximately $7 million to expand, develop, or improve manufactured housing communities, $6 million for opening and upgrading Company-owned retail centers, $6 million for construction and improvement of manufacturing facilities, and $1 million for other fixed assets.

In fiscal 2003, the Company expects to originate approximately $950 million of installment contract and mortgage loan receivables. It expects to invest approximately $12 million in acquisitions or construction of manufactured housing communities, up to $8 million for opening and upgrading Company-owned retail centers, up to $7 million for construction and improvement of manufacturing facilities, and up to $5 million for other fixed assets.

Market Risk

The Company is exposed to market risks related to fluctuations in interest rates on certain of its assets and liabilities. These instruments include certain installment contract receivables, residual interests in asset-backed securitizations and variable rate debt, which principally consists of revolving credit lines. The Company utilizes interest rate swaps to minimize interest rate risk on certain credit lines, effectively converting these to fixed rate debt. Foreign currency and commodity price risk are not considered to have a material impact on the Company.

The Company had variable interest rate installment contract receivables of approximately $5.6 million at June 30, 2002. Holding the outstanding principal amount constant, each one percentage point increase in interest rates occurring on the first day of the year would result in an increase in cash flow for the coming year of approximately $28,000.

Certain of the coupon rates on certificates payable to investors in asset-backed securities are based on variable interest rates. These certificates total $923 million at June 30, 2002. The balance of installment contract receivables with variable interest rate terms collateralizing these certificates was $757 million, with the remainder having fixed interest rate terms. Holding the receivable balances constant, each one percentage point increase in interest rates occurring on the first day of the year would result in a net decrease in cash flow for the coming year of approximately $5.3 million.

Of the $93 million outstanding debt as of June 30, 2002, $15 million had terms that included variable interest rates that reset weekly. The remaining $78 million of outstanding debt had fixed interest rate terms. Holding the variable rate debt constant, each one percentage point increase in interest rates occurring on the first day of the year would result in an increase in interest expense for the coming year of approximately $99,000, net of tax.

New Accounting Pronouncements

In June 2001, the FASB issued Statement No. 143 (SFAS 143), *Accounting for Asset Retirement Obligations.* SFAS 143 requires that obligations associated with the retirement of a tangible long-lived asset to be recorded as a liability when those obligations are incurred, with the amount of the liability initially measured at fair value. SFAS 143 will be effective for financial statements for fiscal years beginning after June 15, 2002. The Company evaluated the retirement of long-lived assets and determined the adoption of this statement will not have a material impact on the Company's reported results of operations, financial position or cash flows.

In August 2001, the FASB issued Statement No. 144 (SFAS 144), *Accounting for the Impairment or Disposal of Long-Lived Assets.* SFAS 144 supercedes SFAS 121 and applies to all long-lived assets (including discontinued operations) and consequently amends Accounting Principles Board Opinion No. 30 (APB 30), *Reporting Results of Operations Reporting the Effects of Disposal of a Segment of a Business.* SFAS 144 requires that

long-lived assets that are to be disposed of by sale be measured at the lower of book value or fair value less cost to sell. SFAS 144 is effective for financial statements issued for fiscal years beginning after December 15, 2001, and generally, its provisions are to be applied prospectively. The Company evaluated the disposal of long-lived assets and determined the adoption of this statement will not have a material impact on the Company's reported results of operations, financial position or cash flows.

In April 2002, the FASB issued Statement No. 145, *Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections.* This Statement rescinds FASB Statement No. 4, *Reporting Gains and Losses from Extinguishment of Debt*, and an amendment of that Statement, FASB Statement No. 64, *Extinguishments of Debt Made to Satisfy Sinking-Fund Requirements.* This Statement amends FASB Statement No. 13, *Accounting for Leases*, to eliminate an inconsistency between the required accounting for sale-leaseback transactions and the required accounting for certain lease modifications that have economic effects that are similar to sale-leaseback transactions. This Statement also amends other existing authoritative pronouncements to make various technical corrections, clarify meanings, or describe their applicability under changed conditions. The Company did not have any transactions applicable to the provisions of this statement in the current fiscal year. Therefore, the Company does not anticipate the adoption of this statement to have a material impact on the Company's reported results of operations, financial position or cash flows.

In June 2002, the FASB issued Statement No. 146 (SFAS 146), *Accounting for Costs Associated with Exit or Disposal Activities.* This Statement addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force (EITF) Issue No. 94-3, *Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity.* This Statement requires that a liability for a cost associated with an exit or disposal activity be recognized and measured initially at fair value only when the liability is incurred. SFAS 146 is effective for exit or disposal activities that are initiated after December 31, 2002, and the Company does not anticipate the provisions of this statement to have a material impact on the Company's reported results of operations, financial positions, or cash flows.

Effects of Inflation

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

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, availability of wholesale and retail financing, general or seasonal weather conditions affecting sales and revenues, catastrophic events impacting insurance costs, cost of labor and/or raw materials and industry consolidation trends creating fewer, but stronger, competitors capable of sustaining competitive pricing pressures.

Management expertise and experience affects its overall ability to anticipate and meet consumer preferences, maintain successful marketing programs, continue quality manufacturing output, keep a strong cost management oversight, and achieve stable results from its securitization activities.

Lastly, management has little control over government policy and economic conditions such as prevailing interest rates, capital market liquidity, government monetary policy, stable regulation of manufacturing standards, consumer confidence, favorable trade policies, and general prevailing economic and employment conditions.

QUARTERLY RESULTS *Unaudited*

		2002				2001			
(in thousands except per share data)		**First Sept. 30**	**Second Dec. 31**	**Third Mar. 31**	**Fourth June 30**	First Sept. 30	Second Dec. 31	Third Mar. 31	Fourth June 30
Revenues *(1)*		**$296,370**	**$296,820**	**$269,908**	**$335,750**	$300,807	$284,853	$272,070	$293,226
Operating income		**47,122**	**53,408**	**43,823**	**57,014**	45,408	45,468	38,620	41,359
Income before income taxes		**42,120**	**53,408**	**46,381**	**55,137**	45,982	43,565	37,752	42,052
Net income		**26,520**	**33,708**	**29,181**	**34,737**	28,982	27,465	23,752	26,452
Earnings per share	- Basic	**$0.19**	**$0.25**	**$0.21**	**$0.25**	$0.21	$0.20	$0.17	$0.19
	- Diluted	**$0.19**	**$0.24**	**$0.21**	**$0.25**	$0.21	$0.20	$0.17	$0.19
Price range of stock	- High	**$16.50**	**$17.41**	**$17.21**	**$19.28**	$10.00	$12.88	$14.50	$15.82
	- Low	**$10.75**	**$12.60**	**$14.49**	**$15.10**	$8.13	$8.75	$12.05	$11.55
Dividends per common share		**–**	**–**	**$0.064**	**–**	$0.016	$0.016	$0.016	$0.016

(1) Revenues for 2002 reflect losses related to securitized mortgages of approximately $9,700,000, $10,000,000, $10,800,000, and $9,700,000 for the quarters ending September 30, 2001, December 31, 2001, March 31, 2002, and June 30, 2002, respectively.

Report of Independent Accountants

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income, of shareholders' equity and of cash flows present fairly, in all material respects, the financial position of Clayton Homes, Inc. and Subsidiaries at June 30, 2002, and 2001, and the results of their operations and their cash flows for each of the three years in the period ended June 30, 2002, in conformity with accounting principles generally accepted in the United States of America. 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 auditing standards generally accepted in the United States of America 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 our opinion.

PricewaterhouseCoopers LLP
Knoxville, Tennessee
August 7, 2002

Consolidated Balance Sheets

(in thousands)	June 30, 2002	2001
Assets		
Cash and cash equivalents	$ 83,729	$ 47,763
Trade receivables	9,308	14,683
Other receivables, principally installment contracts, net of reserves for credit losses of $18,876 in 2002 and $20,560 in 2001	744,074	649,924
Inventory finance receivables	43,859	7,300
Residual interests in installment contract and mortgage receivables sold	129,348	124,994
Servicing assets from installment contract and mortgage receivables sold	51,996	45,128
Inventories, net	189,976	185,695
Securities available-for-sale	25,729	30,956
Restricted cash	126,155	111,060
Property, plant and equipment, net	310,764	309,438
Deferred income taxes	19,793	22,710
Other assets	93,672	104,519
Total assets	$ 1,828,403	$ 1,654,170
Liabilities and Shareholders' Equity		
Accounts payable and accrued liabilities	$ 139,308	$ 118,057
Debt obligations	92,912	141,862
Other liabilities	334,226	246,773
Total liabilities	566,446	506,692
Commitments and Contingencies (Notes 2, 6, 7, 11 & 16)		
Shareholders' equity		
Preferred stock, $.10 par value, authorized 1,000 shares, none issued	-	-
Common stock, $.10 par value, authorized 200,000 shares, issued 138,002 at June 30, 2002, and 137,991 at June 30, 2001	13,800	13,799
Additional paid-in capital	44,193	43,593
Retained earnings	1,196,146	1,081,137
Accumulated other comprehensive income	7,818	8,949
Total shareholders' equity	1,261,957	1,147,478
Total liabilities and shareholders' equity	$ 1,828,403	$ 1,654,170

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

Consolidated Statements of Income

(in thousands except per share data)	2002	Year ended June 30, 2001	2000
Revenues			
Net sales	$871,108	$849,157	$ 993,916
Financial services	252,499	227,916	228,642
Rental and other income	75,241	73,883	70,787
	1,198,848	1,150,956	1,293,345
Costs and expenses			
Cost of sales	565,322	562,267	660,429
Selling, general and administrative	406,655	374,628	384,067
Financial services interest	404	706	1,032
Provision for credit losses	25,100	42,500	20,800
	997,481	980,101	1,066,328
Operating income	201,367	170,855	227,017
Interest expense	(8,975)	(5,561)	(5,749)
Interest revenue/other	4,654	4,057	7,357
Income before income taxes	197,046	169,351	228,625
Provision for income taxes	(72,900)	(62,700)	(84,600)
Net income	$124,146	$106,651	$ 144,025
Net income per common share			
Basic	$0.90	$0.77	$1.03
Diluted	$0.89	$0.77	$1.03
Average shares outstanding			
Basic	137,726	137,702	139,474
Diluted	138,872	138,340	139,815

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

Consolidated Statements of Shareholders' Equity

(in thousands except share data)	Total Shareholders' Equity	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)
Balance at June 30, 1999	$ 947,768	$ 14,237	$ 85,236	$ 849,116	$ (821)
Net income	144,025	–	–	144,025	–
Other comprehensive income, net of tax of $82					
Unrealized loss on securities available-for-sale during the year	(627)	–	–	–	(627)
Realized loss on securities available-for-sale included in net income	767	–	–	–	767
Comprehensive income	144,165				
Purchase of 5,382,000 shares of common stock	(49,776)	(538)	(49,238)	–	–
Dividends declared ($.064 per common share)	(8,885)	–	–	(8,885)	–
Issuances related to stock incentive, employee benefit plans and other	3,103	51	3,502	(450)	–
Balance at June 30, 2000	1,036,375	13,750	39,500	983,806	(681)
Net income	106,651	–	–	106,651	–
Other comprehensive income, net of tax of $5,656					
Unrealized gain on residual interests	7,591	–	–	–	7,591
Unrealized gain on securities available-for-sale during the year	1,732	–	–	–	1,732
Realized loss on securities available-for-sale included in net income	307	–	–	–	307
Comprehensive income	116,281				
Purchase of 60,000 shares of common stock	(482)	(6)	(476)	–	–
Dividends declared ($.064 per common share)	(8,814)	–	–	(8,814)	–
Issuances related to stock incentive, employee benefit plans and other	4,118	55	4,569	(506)	–
Balance at June 30, 2001	1,147,478	13,799	43,593	1,081,137	8,949
Net income	124,146	–	–	124,146	–
Other comprehensive income, net of tax of ($665)					
Unrealized loss on residual interests	(2,134)	–	–	–	(2,134)
Unrealized gain on securities available-for-sale during the year	1,350	–	–	–	1,350
Realized gain on securities available-for-sale included in net income	(347)	–	–	–	(347)
Comprehensive income	123,015				
Purchase of 827,400 shares of common stock	(9,637)	(83)	(9,554)	–	-
Dividends paid ($.064 per common share)	(8,800)	–	–	(8,800)	-
Issuances related to stock incentive, employee benefit plans and other	9,901	84	10,154	(337)	-
Balance at June 30, 2002	$ 1,261,957	$13,800	$ 44,193	$ 1,196,146	$ 7,818

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

Consolidated Statements of Cash Flows

(in thousands)	Year ended June 30, 2002	2001	2000
Cash Flows from Operating Activities			
Net income	$ 124,146	$ 106,651	$ 144,025
Adjustments to reconcile net income to net cash provided by operating activities			
Depreciation and amortization	19,161	20,600	20,422
Amortization associated with sale of installment contract receivables	13,201	39,798	40,597
Gain on sale of installment contract receivables	(39,875)	(25,593)	(37,341)
Income accretion from residual interests in installment contract receivables	(75,543)	-	-
Provision for credit losses	25,100	42,500	20,800
Realized loss (gain) on securities available-for-sale	(550)	488	1,218
Deferred income taxes	3,582	(4,082)	(3,861)
Decrease (increase) in other receivables, net	(54,848)	1,200	5,720
Decrease (increase) in inventories	(4,281)	36,736	(37,987)
Increase (decrease) in accounts payable, accrued liabilities, and other	87,070	(54,074)	(59,490)
Cash provided by operations	97,163	164,224	94,103
Origination of installment contract receivables	(912,536)	(815,546)	(983,090)
Proceeds from sales of originated installment contract receivables	871,619	660,802	886,040
Principal collected on originated installment contract receivables	40,725	40,686	48,040
Net cash provided by operating activities	96,971	50,166	45,093
Cash Flows from Investing Activities			
Acquisition of installment contract receivables	(1,049,851)	(321,711)	(206,154)
Proceeds from sales of acquired installment contract receivables	944,253	225,654	229,412
Principal collected on acquired installment contract receivables	54,530	23,154	19,836
Proceeds from sales of securities available-for-sale	25,312	29,527	37,733
Proceeds from residual interests in installment contract receivables	52,972	-	-
Acquisition of property, plant and equipment	(20,487)	(24,559)	(34,398)
Decrease (increase) in restricted cash	(15,095)	(14,156)	3,223
Net cash provided by (used in) investing activities	(8,366)	(82,091)	49,652
Cash Flows from Financing Activities			
Dividends	(8,800)	(8,814)	(8,885)
Net borrowings (repayment) on credit facilities	(45,800)	45,800	-
Proceeds from debt obligations	-	-	6,000
Repayment of debt obligations	(3,150)	(3,154)	(3,261)
Increase (decrease) of cash in excess of bank balances	4,847	(1,692)	(694)
Issuance of stock for incentive plans and other	9,901	4,118	3,103
Purchase of common stock	(9,637)	(482)	(49,776)
Net cash provided by (used in) financing activities	(52,639)	35,776	(53,513)
Net increase in cash and cash equivalents	35,966	3,851	41,232
Cash and cash equivalents at beginning of year	47,763	43,912	2,680
Cash and cash equivalents at end of year	$ 83,729	$ 47,763	$ 43,912
Supplemental disclosures for cash flow information			
Cash paid during the year for			
Interest	$ 9,379	$ 6,267	$ 6,781
Income taxes	$ 60,421	$ 76,723	$ 97,903

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. (CMH) and its wholly- and majority-owned subsidiaries. CMH and its subsidiaries are collectively referred to herein as the Company. The Company is a vertically-integrated manufactured housing company headquartered near Knoxville, Tennessee. Employing approximately 6,800 people and operating in 33 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 12, *Business Segment Information,* for further details of intercompany activity.

Income Recognition

Sales to independent retailers of homes produced by CMH 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 home buyer enters into an installment sales contract; construction of the home is complete; the home buyer has inspected and accepted the home; and title has passed to the retail home buyer. Most of these installment sales contracts, which are normally payable over 84 to 360 months, are financed by Vanderbilt Mortgage and Finance, Inc. (VMF), the Company's financing subsidiary. The Company also accrues and recognizes revenue for rental of homesites and homes based on the terms of the resident's lease agreement with the Company.

The Company acts as agent on physical damage, family protection and home buyer protection plan insurance policies written by unaffiliated insurance companies (ceding companies) for the purchasers of manufactured homes. The insurance policies are in turn reinsured by certain subsidiaries of the Company. Premiums from policies represent short-duration contracts with terms of one to 10 years and are deferred and recognized as revenue over the terms of the policies. Claims expenses are recorded as insured events occur. Expenses are matched to revenue over the terms of the policies by means of deferral and amortization of policy acquisition costs; such costs include commissions, premium taxes and ceding fees, which vary with and are directly related to the production of insurance policies.

Installment Contract and Mortgage Receivables

Installment contract and mortgage loan receivables (receivables) originated or purchased by VMF are generally sold into asset-backed security vehicles, which, in turn, issue certificates to investors. VMF retains the servicing and the residual interest associated with these instruments.

Receivables held for sale are included in other receivables and are carried at the lower of aggregate cost or market. Certain of the receivables are purchased in bulk at a discount. The purchase discounts are allocated between discount and reserves for credit losses and contingent liabilities based on management's assessment of risks existing in the portfolio. Discounts are accreted over the life of the related portfolio using the interest method after giving consideration to anticipated prepayments. In the event such receivables are sold, discounts attributable to the sold receivables are recognized. Adjustments between the reserves for credit losses and contingent liabilities are periodically made to reflect changes in the estimated collectability of each portfolio purchased.

Most of the receivables are with borrowers in the east, south and southwest portions of the United States, and are collateralized by manufactured homes. Interest income on receivables held, either for sale or as an investment, is recognized in accordance with the terms of the underlying installment contracts. For receivables sold with servicing retained and receivables serviced under servicing agreements, service fee income is recognized as the service is performed. Interest income on interest-only residual interests is recognized in accordance with the consensus of the Emerging Issues Task Force in its Issue No. 99-20, *Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Assets* (EITF 99-20). Accordingly, interest income is recognized through an effective yield method, with the yield computed prospectively over the life of the residual interests after adjustments in the estimated cash flows are made to reflect prepayments, defaults and other factors.

The Company accrues for obligations related to cash collections arising from its own securitized receivables and receivables serviced under contract and remits these collections to the paying agent or trustee in accordance with the provisions of the servicing agreements. See Note 13, *Other Assets and Liabilities.*

Retained Interests

The Company follows the provisions of SFAS 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,* which utilizes a financial components approach to transfers and servicing of financial assets, requiring that the carrying amount of the receivables sold be allocated between the assets sold and the assets (liabilities) created, if any, based upon their estimated fair value at the date of sale. The assets (liabilities) created are: 1) an interest-only security and a residual liability valued as the discounted present value of the excess (deficiency) interest due the residual interest owner (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 excess of the contractual servicing fee over the cost of servicing the contracts plus a normal profit margin. Gain (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.

Servicing assets are periodically evaluated on a transaction basis for impairment based on the fair value of those assets. 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. The servicing asset or liability is amortized in proportion to and over the period of estimated net servicing income or net servicing loss.

Interest-only securities represent the right to receive future cash flows from securitization transactions. Such cash flows generally are equal to the value of the excess of the principal and interest to be collected on the underlying receivables collateralizing each transaction over the sum of the principal and interest to be paid to the holders of the securities sold net of estimated credit losses and contractual servicing fee. The Company carries interest-only securities at estimated fair value. As market quotes are generally not available, fair value is determined by discounting the projected cash flows over the expected remaining life of the securities outstanding, on a transaction basis, using current prepayment, default, loss and interest rate assumptions. Estimates for prepayments, defaults, and losses are determined based on

a model developed by the Company and refined to reflect Company-specific experience and trends as well as current market conditions. See Note 2, *Securitizations.*

The residual interests in the installment receivables sold are classified as available-for-sale securities as defined by Statement of Financial Accounting Standards No. 115, *Accounting for Certain Investments in Debt and Equity Securities* (SFAS 115). In accordance with EITF 99-20, declines in fair value are to be considered other than temporary when: i) the carrying value of the beneficial interests exceeds the fair value of such beneficial interests using current assumptions; and ii) the timing and/or extent of cash flows expected to be received on the beneficial interests has adversely changed - as defined - from the previous valuation date. During the three year period ended June 30, 2002, the Company did not determine any declines in fair value to be permanent.

The Company follows SFAS No. 134, *Accounting for Mortgage-Backed Securities Retained after the Securitization of Mortgage Loans Held for Sale by a Mortgage Banking Enterprise,* which requires that the Company classify mortgage-backed securities retained after a securitization in accordance with SFAS 115. Accordingly, these securities, aggregating at $20.1 million, are classified as available-for-sale, are stated at fair value, and can be reasonably expected to mature in 3-11 years. The Company also has certain other securities that are classified as available-for-sale and, accordingly, are stated at fair value. The fair value of these securities is estimated based on quoted market prices, when available. If not available, fair value is estimated using quoted market prices for similar financial instruments. Net unrealized holding gains and losses, determined using a specific identification cost basis, are reported as a separate component of accumulated other comprehensive income, net of tax, until realized. See Note 4, *Securities Available-for-Sale.*

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.

Inventories

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

Property, Plant and Equipment

Land and improvements, buildings, and furniture and equipment are recorded 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. Those assets' estimated useful lives are summarized as follows: Land and improvements, 8 to 20 years; Buildings, 7 to 20 years; and Furniture and all other equipment, 3 to 7 years.

The Company follows SFAS No. 121, *Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of,* which requires recognition of impairment losses for long-lived assets whenever events or changes in circumstances result in the carrying amount of the assets exceeding the sum of the expected future undiscounted cash flows associated with such assets. The measurement of the impairment losses recognized is based on the difference between the fair values and the carrying amounts of the assets. SFAS 121 also requires that long-lived assets held for sale be reported at the lower of carrying amount or fair value less cost to sell. The Company has not experienced any impairment losses.

Accounts Payable

Accounts payable includes checks written in excess of bank balances of $19,693,000 and $14,846,000 at June 30, 2002, and June 30, 2001, respectively.

Reserves for Credit Losses and Contingent Liabilities

Reserves for credit losses and contingent liabilities are established related to receivables held, either for sale or investment. 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.

Interest Rate Swaps

The Company uses interest rate swaps to assist in minimizing interest incurred on its short-term variable rate debt. The difference between amounts received and amounts paid under such agreements is recorded as a reduction of, or addition to, interest expense as incurred over the life of the swap.

The Company follows SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities,* which was subsequently amended by SFAS No. 138, *Accounting for Certain Derivative Instruments and Certain Hedging Activities.* SFAS No. 133 establishes accounting and reporting standards for derivative instruments embedded in other contracts and for hedging activities. See Note 6, *Debt Obligations.*

Restricted Cash

Restricted cash primarily represents: 1) trust account cash balances required by certain VMF servicing agreements, and 2) insurance reserves required by ceding companies. The majority of the restricted cash balance represents funds held in accordance with certain servicing agreements that will be disbursed within 15 days of the end of the accounting period.

Income Taxes

Deferred income taxes are recorded to 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.

Accumulated Other Comprehensive Income

Accumulated other comprehensive income is presented net of income taxes and is comprised of unrealized gains and temporary losses on securities available-for-sale, as described under *Retained Interests.*

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. Material estimates may

include, but are not limited to, certain revenue and expense accruals, timing and frequency of foreclosures, rates of recovery on foreclosures, the timing and rate of voluntary prepayments and interest rates. Actual results could differ from those estimates.

Other
Certain reclassifications have been made to the 2000 and the 2001 financial statements to conform to the 2002 presentation.

New Accounting Pronouncements

In June 2001, the FASB issued Statement No. 143 (SFAS 143), *Accounting for Asset Retirement Obligations.* SFAS 143 requires that obligations associated with the retirement of a tangible long-lived asset to be recorded as a liability when those obligations are incurred, with the amount of the liability initially measured at fair value. SFAS 143 will be effective for financial statements for fiscal years beginning after June 15, 2002. The Company evaluated the retirement of long-lived assets and determined the adoption of this statement will not have a material impact on the Company's reported results of operations, financial position or cash flows.

In August 2001, the FASB issued Statement No. 144 (SFAS 144), *Accounting for the Impairment or Disposal of Long-Lived Assets.* SFAS 144 supercedes SFAS 121 and applies to all long-lived assets (including discontinued operations) and consequently amends Accounting Principles Board Opinion No. 30 (APB 30), *Reporting Results of Operations Reporting the Effects of Disposal of a Segment of a Business.* SFAS 144 requires that long-lived assets to be sold be measured at the lower of book value or fair value less cost to sell. SFAS 144 is effective for financial statements issued for fiscal years beginning after December 15, 2001, and generally, its provisions are to be applied prospectively. The Company evaluated the disposal of long-lived assets and determined the adoption of this statement will not have a material impact on the Company's reported results of operations, financial position or cash flows.

In April 2002, the FASB issued Statement No. 145, *Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections.* This Statement rescinds FASB Statement No. 4, *Reporting Gains and Losses from Extinguishment of Debt,* and an amendment of that Statement, FASB Statement No. 64, *Extinguishments of Debt Made to Satisfy Sinking-Fund Requirements.* This Statement amends FASB Statement No. 13, *Accounting for Leases,* to eliminate an inconsistency between the required accounting for sale-leaseback transactions and the required accounting for certain lease modifications that have economic effects that are similar to sale-leaseback transactions. This Statement also amends other existing authoritative pronouncements to make various technical corrections, clarify meanings, or describe their applicability under changed conditions. The Company did not have any transactions applicable to the provisions of this statement in the current fiscal year, and the adoption of this statement should not have a material impact on the Company's reported results of operations, financial position or cash flows.

In June 2002, the FASB issued Statement No. 146 (SFAS 146), *Accounting for Costs Associated with Exit or Disposal Activities.* This Statement addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force (EITF) Issue No. 94-3, *Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity.* This Statement requires that a liability for a cost associated with an exit or disposal activity be recognized and measured initially at fair value only when the liability is incurred. SFAS 146 is effective for exit or disposal activities that are initiated after December 31, 2002, and the Company does not anticipate that the provisions of this statement will have a material impact on the Company's reported results of operations, financial positions, or cash flows.

Note 2 - Securitizations

The Company engages in securitization activities in connection with certain of its businesses. Subsequent to the securitization of receivables, the Company continues to maintain account relationships and provide servicing for those receivables transferred. As Seller and Servicer, the Company retains residual interests that are created as a result of its securitization activity. The Company estimates the fair value of the retained interests by using discounted expected future cash flows that incorporate key assumptions including prepayment speed and credit losses. The valuation of retained interests is affected by the projected level and timing of prepayments of principal and net credit losses. Should actual timing differ materially from the Company's projections, it could have a material effect on the valuation of the Company's retained interests.

There were four securitization transactions completed during 2002, and three transactions during 2001. Each transaction establishes a trust, which issues certificates representing ownership in that trust. Although there are some differences, structure provisions are generally the same for each issue. The structures call for time tranched senior and subordinated classes of securities. Additional credit support is provided by excess spread and, in some cases, over collateralization. The Company also provides additional credit support by placing a limited guarantee on certain of the subordinated certificates. See Note 11, *Commitment and Contingencies.*

The Company accounts for the transactions as sales and records any gains or losses in accordance with the provisions of SFAS 140. Certain data pertaining to securitizations completed during 2002 and 2001, including the key economic assumptions used to measure the retained interests created, are as follows:

($ in millions)	2002	2001
Number of transactions completed	4	3
Aggregate balance of certificates issued	$1,825	$ 886
Aggregate principal balance of contracts sold	$1,875	$ 896
Average balance of securitized contracts outstanding at June 30	$4,453	$3,702
Weighted average interest rate of contracts sold	10.41%	11.31%
Aggregate amount of net gain (loss) recognized*	$ 39.9	$ 25.6
Original Key Economic Assumptions		
Approximate assumed weighted average constant prepayment rate as a percentage of unpaid principal balance	20.01%	18.25%
Weighted average life (in years)	4.52	4.66
Weighted average expected credit losses	4.08%	2.48%
Weighted average residual cash flow discount rate**	11.44%	15.75%

** Net of issuance costs **Residual liability discounted at 4.38%*

At June 30, 2002, key economic assumptions used to determine the estimated fair value of the retained interests in securitizations and the sensitivity of the current fair value of residual cash flows to immediate 10% and 20% adverse changes in those assumptions are as follows:

	2002	2001
($ in thousands)		
Interest-Only (I/O) securities	$ 93,673	$ 95,461
Servicing assets	51,996	45,128
Residual liability	(52,161)	-
Retained corporate guarantee certificates	20,136	25,217
Carrying value (fair value) of retained interests	$ 113,644	$ 165,806
($ in millions)		
Weighted average life (in years)	4.27	4.49
Prepayment speed (constant prepayment rate)	10.7% - 24.10%	10.7% - 24.14%
Impact of 10% adverse change	($11.7)	($8.6)
Impact of 20% adverse change	($22.6)	($16.4)
Expected credit losses	2.43%	1.90%
Impact of 10% adverse change	($21.6)	($10.4)
Impact of 20% adverse change	($43.5)	($20.9)
Residual cash flow discount rate	13.70%	15.75%
Impact of 10% adverse change	($6.2)	($6.7)
Impact of 20% adverse change	($11.9)	($12.8)

The sensitivity analysis is hypothetical and should be used with caution. For instance, changes in fair value based on a 10% variation in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. In addition, the effect of a variation in a particular assumption on the fair value of the retained interest is calculated without changing any other assumption, when in reality, changes in any one factor may result in changes in another factor.

The following table summarizes certain cash flow activity with respect to securitizations in 2002 and 2001:

(in millions)	2002	2001
Cash Flow Activity		
Proceeds from new securitizations	$ 1,816	$ 887
Servicing fees received	$ 54	$ 49
Cash flow received from retained interests	$ 53	$ 71

Total contracts serviced at June 30, 2002, and 2001, including contracts held for investment, were approximately $5.0 billion and $4.2 billion, respectively. Managed receivables at June 30, 2002, and related receivables past due 90 days are as follows:

(in millions)	Total Principal Amount	Principal Amount 90 Days or More Past Due (a)
Held in portfolio	$ 783	$ 54
Securitized	4,193	60
	$4,976	$114

(a) Includes bankruptcies and foreclosures.

Changes related to the servicing assets during the years ended June 30, 2002, 2001, and 2000, are as follows:

(in thousands)	2002	2001	2000
Beginning balance	$ 45,128	$40,704	$27,024
Servicing assets recognized	19,605	15,994	23,781
Amortization	(12,737)	(11,570)	(10,101)
	$ 51,996	$45,128	$40,704

Note 3 - Inventories

Inventories at June 30, 2002, and 2001, are as follows:

(in thousands)	2002	2001
Manufactured homes		
New	$123,482	$114,874
Previously-owned	49,644	54,171
Raw materials	16,850	16,650
	$189,976	$185,695

If the first-in, first-out (FIFO) method of inventory valuation had been used, inventories would have been higher by $20,500,000 and $20,282,000 at June 30, 2002, and 2001, respectively.

Note 4 - Securities Available-For-Sale

Securities available-for-sale at June 30, 2002, and 2001, are as follows:

(in thousands)	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Residual interests in installment contract receivables	$ 85,012	$13,850	$(5,189)	$ 93,673
Retained securities held-for-sale	20,691	147	(702)	20,136
Other securities held-for-sale	1,291	4,302	-	5,593
Total June 30, 2002	$106,994	$18,299	$(5,891)	$119,402
Residual interests in installment contract receivables	$ 83,412	$14,869	$(2,820)	$ 95,461
Retained securities held-for-sale	27,510	-	(2,293)	25,217
Other securities held-for-sale	1,291	4,448	-	5,739
Total June 30, 2001	$112,213	$19,317	$(5,113)	$126,417

The unrealized gains and losses, net of tax, are recorded as an element of accumulated other comprehensive income. The residual interests of installment contract receivables do not include over collateralization of $35,675,000 and $29,533,000 for the years ended June 30, 2002, and June 30, 2001, respectively.

Note 5 - Property, Plant and Equipment

Property, plant and equipment at June 30, 2002, and 2001, are as follows:

(in thousands)	2002	2001
Land and improvements	$226,953	$215,910
Buildings	152,353	150,000
Furniture and all other equipment	53,008	50,422
	432,314	416,332
Less: accumulated depreciation and amortization	(121,550)	(106,894)
	$310,764	$309,438

The Company entered into capital lease arrangements in fiscal 2002 for computer related equipment valued at $568,000. The contractual obligation as of June 30, 2002, was $532,000 with $291,000 due in fiscal 2003 and $241,000 due in fiscal 2004.

Note 6 - Debt Obligations

Debt obligations at June 30, 2002, and 2001, are summarized as follows:

(in thousands)	2002	2001
Senior notes, 6.25%, due December 2003	$75,000	$ 75,000
Debt collateralized by installment contract receivables, average effective rate 10.12% at June 30, 2002, due through 2004	2,176	5,229
Tax-exempt bonds, effective rate of 1.35% at June 30, 2002, due through 2030	15,230	15,230
Lines of credit	-	45,800
Other notes payable	506	603
	$92,912	$141,862

Annual maturities of debt as of June 30, 2002, are: 2003 - $2,097,000; 2004 - $75,325,000; 2005 - $134,000; 2006 - $35,000; $15,321,000 after 2007.

In December 1998, the Company issued $75 million of 6.25% Senior Notes due December 2003 (the "6.25% Notes"), with interest payable each June and December. The 6.25% Notes are redeemable at the option of the Company, in whole, at 100% of the principal amount plus a make-whole premium at any time prior to December 30, 2003. The 6.25% Notes are not subject to any sinking fund requirements, are guaranteed by all significant subsidiaries of the Company, and are governed by various financial covenants which require maintenance of certain financial ratios.

On December 21, 2001, the Company acquired manufactured housing installment contract receivables with an aggregate outstanding principal balance of $900 million. In conjunction with that transaction, the Company sold the receivables through a committed one-year sales facility of $500 million, while retaining the servicing rights and residual cash flows. This facility was not utilized at June 30, 2002, and was subsequently amended to $300 million of which $150 million is committed. In addition, a committed one-year $150 million participation facility is also available to facilitate the future sale of manufactured housing contracts. This participation facility was not utilized at June 30, 2002. The sales facility's pricing is based on LIBOR rates; facility fees are payable quarterly on the committed portion of the facility. Utilization of any unfunded commitment is permitted as long as criteria, that include credit rating, financial covenants, and performance triggers, are met. This facility is not collateralized. The Company's tax-exempt manufacturing facilities' bonds carry no sinking fund requirements and bear interest at weekly adjustable rates.

In addition, the Company has committed and uncommitted lines of credit amounting to $236 million with several banks, which bear interest based on LIBOR rates. These lines were unused at June 30, 2002. These lines are subject to periodic review by each bank and may be canceled by the Company at any time.

Under certain interest rate swap agreements, the Company agrees with other parties to exchange the difference between fixed rate and variable rate interest amounts calculated by reference to an agreed upon notional principal amount. At June 30, 2002, the Company's interest rate swap agreements have an aggregate notional amount of $100 million. The interest rates on the notional amounts range from 5.42% to 5.62%.

Note 7 - Reserves for Credit Losses and Contingent Liabilities

Analysis of the reserves for credit losses on installment contract receivables and contingent liabilities for the years ended June 30, 2002, 2001, and 2000, is as follows:

(in thousands)	2002	2001	2000
Balance, beginning of year	$ 30,536	$ 35,725	$44,275
Additions to reserves	25,100	42,500	20,800
Charges, net of recoveries applicable to installment contract receivables			
Purchased	(14,880)	(13,105)	(12,199)
Other	(21,884)	(37,974)	(20,044)
Reserves transferred to unamortized discounts	-	(1,000)	(6,000)
Reserves associated with receivables purchased	5,668	4,390	8,893
Balance, end of year	$ 24,540	$ 30,536	$35,725

The reserves for credit losses are netted against receivables and the reserve for contingent liabilities is included in other liabilities on the consolidated balance sheets. The Company is contingently liable as guarantor on installment contract receivables sold with recourse. At June 30, 2002, and 2001, the outstanding principal balances of these receivables totaled approximately $68 million and $84 million, respectively. There were no receivables sold with recourse in 2002, 2001 and 2000.

Note 8 - Shareholders' Equity

Stock Option Plan

In 1983, 1985, 1991, and 1997, the Company established Stock Option Plans for a total of 17,021,036 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 are as follows:

	Shares	Stock Option Price Range	Weighted Avg Exercise Price	Stock Options Exercisable	Weighted Avg Exercise Price
Balance June 30, 1999	4,861,151	$ 1.41 - $15.75	$ 10.15	1,449,866	$ 8.13
Granted	762,325	$ 9.38 - $11.88	$ 9.91		
Exercised	(208,725)	$ 1.41 - $ 8.27	$ 2.65		
Canceled	(309,295)	$ 3.64 - $15.75	$ 11.11		
Balance June 30, 2000	5,105,456	$ 2.16 - $15.75	$ 10.36	1,655,984	$ 9.18
Granted	875,825	$ 8.38 - $ 9.31	$ 9.10		
Exercised	(278,401)	$ 2.16 - $13.70	$ 5.88		
Canceled	(242,418)	$ 7.22 - $15.75	$ 10.24		
Balance June 30, 2001	5,460,462	$ 3.83 - $15.75	$ 10.40	1,901,452	$ 9.84
Granted	1,121,390	$8.19 - $15.75	$ 13.82		
Exercised	(582,957)	$3.83 - $13.70	$ 8.40		
Canceled	(268,941)	$7.22 - $15.75	$ 11.29		
Balance June 30, 2002	5,729,954	$7.22 - $15.75	$ 11.23	1,835,540	$ 10.29

Options available for future grant at June 30, 2002, and 2001, were 3,317,696 and 4,299,675, respectively. 931 persons held options at June 30, 2002.

The following table summarizes information about the plans' stock options at June 30, 2002, including weighted average remaining life (Life) and weighted average exercise price (Price):

	Options Outstanding			Options Exercisable	
Range	Number	Life	Price	Number	Price
$ 7.22 - $10.32	2,421,085	4.9 years	$ 8.72	1,060,311	$ 8.49
$11.50 - $15.75	3,308,869	6.8 years	$13.06	775,229	$12.75

In accordance with the guidance provided by SFAS 123, *Accounting for Stock-Based Compensation* (SFAS 123), the Company has elected to continue following the intrinsic value based method as prescribed by Accounting Principles Board Opinion No. 25 (APB 25), *Accounting for Stock Issued to Employees*, and related interpretations in accounting for its stock option plans. Under the intrinsic value based method, compensation cost is computed as the excess, if any, of the quoted market price of the stock at grant date over the amount the grantee must pay to acquire the stock. Because all options' plans grant at market price, there is no intrinsic value in the stock options on the grant date, therefore no compensation cost is recognized. SFAS 123 describes the fair value method of measuring and recording compensation cost as an alternative to the intrinsic value based method. Under the fair value method, compensation cost is measured at the grant date based on the computed fair value of the grant and is recognized over the vesting period of the options. SFAS 123 also requires that companies using the intrinsic value based method must present pro forma disclosure of net income and earnings per share as if the fair value method had been applied. The pro forma results do not purport to indicate the effects on reported net income for recognizing compensation expense that is expected to occur in future years. If the options had been expensed in the current year, the pro forma results would have been:

(in thousands except per share data)	2002	June 30, 2001	2000
Net income - as reported	$124,146	$106,651	$144,025
Net income - pro forma	120,640	104,352	141,634
Net income per diluted common share - as reported	$0.89	$0.77	$1.03
Net income per diluted common share - pro forma	0.87	0.75	1.01

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 2000 to 2002: dividend yields ranging from 0.39% to 0.76% with a weighted average yield of 0.62%; expected volatility of 0.348; risk-free interest rates ranging from 3.96% to 6.54% with a weighted average rate of 5.16%; and expected lives ranging from 6.47 to 10.00 years with a weighted average life of 9.78 years. The weighted average grant date fair value of options granted in fiscal years 2002, 2001 and 2000 was $7.15, $4.53, and $4.66 per share, respectively.

Note 9 - Income Taxes

The components of deferred tax assets and liabilities at June 30, 2002, and 2001, are as follows:

(in thousands)	2002	2001
Reserves for credit losses and contingencies and discounts	$ 6,981	$ 8,388
Insurance reserves	12,086	10,850
Unearned insurance premiums	10,038	9,604
Residual interest in installment contract receivables	12,005	12,729
Total deferred tax assets	41,110	41,571
Deferred costs	(7,088)	(6,549)
Other comprehensive income	(4,591)	(5,256)
Other	(9,638)	(7,056)
Total deferred tax liabilities	(21,317)	(18,861)
Net deferred tax asset	$19,793	$22,710

The provisions for income taxes for each of the years ending June 30, 2002, 2001, and 2000, are composed of the following:

(in thousands)	2002	2001	2000
Current tax provisions			
Federal	$65,232	$64,010	$82,654
State	4,086	2,772	5,807
Total current	69,318	66,782	88,461
Deferred tax provision (benefit)	3,582	(4,082)	(3,861)
	$72,900	$62,700	$84,600

At June 30, 2002, 2001, and 2000, a deferred tax provision (benefit) of ($665,000), $5,656,000, and $82,000, respectively, was allocated directly to shareholders' equity for the unrealized gain (loss) on residual interests and securities available-for-sale. 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 2002, 2001 and 2000, as follows:

(in thousands)	2002	2001	2000
Income taxes at the statutory rate	$68,966	$59,273	$80,019
State income taxes, net of federal benefit	2,656	1,802	3,775
Other, net	1,278	1,625	806
	$72,900	$62,700	$84,600

Note 10 - Employee Benefit Plans

The Company has a 401(k) defined contribution 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. Company contributions accrued and paid were $4,708,000, $2,938,000, and $3,169,000 for the years ended June 30, 2002, 2001, and 2000, respectively.

Note 11 - Commitments and Contingencies

Certain operating properties are rented under non-cancelable operating leases which expire at various dates through 2010. Total rental expense under operating leases was $5,080,000 in 2002, $5,280,000 in 2001, and $5,340,000 in 2000. Minimum rental commitments under non-cancelable operating leases primarily for retail centers, in effect at June 30, 2002, were:

2003	$3,620,000	2006	$1,199,000
2004	$2,648,000	2007	$ 688,000
2005	$1,826,000	Thereafter	$ 781,000

The following table summarizes the Company's other contingencies as of June 30, 2002:

(in thousands)

Other Contingencies	Amount of contingency expiration per period						
	Total	FY03	FY04	FY05	FY06	FY07	Thereafter
Letters of credit	$127,203	$127,203	$ -	$ -	$ -	$ -	$ -
Guarantees	$416,661	$ 610	$ 2,154	$ 3,016	$26,539	$30,751	$ 353,591
Repurchase agreements	$ 59,600	$ 59,600	$ -	$ -	$ -	$ -	$ -

At June 30, 2002, the Company has letters of credit, primarily related to insurance reserves and performance guarantees related to asset-backed securitizations outstanding for which the Company provides a limited guarantee. The Company believes a significant loss from any such guarantee is remote. See Note 7 for discussion of guarantees on installment contract receivables.

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.

Note 12 - Business Segment Information

The Company has identified four major business segments: Retail, Manufacturing, Financial Services, and Communities. The Retail group purchases homes from the Company's manufacturing operations and third party manufacturers to sell to retail customers. The Manufacturing group builds homes for Company-owned and independent retailers. Financial Services provides retail financing of manufactured homes, reinsures risk on family protection, physical damage, and homebuyer protection plan insurance policies, and offers certain specialty finance products. Communities owns and operates manufactured housing communities. Income from operations consists of total revenues less cost of sales and operating expenses. Identifiable assets are used in the operation of each business segment.

The sales of units shipped to the Retail sales centers from the Manufacturing facilities are eliminated in the intersegment sales line of the Revenues section. The Eliminations/other line as represented below includes other intercompany eliminations required in accordance with generally accepted accounting principles. Information concerning operations by business segment follows:

(in thousands)	2002	2001	2000
Revenues			
Retail	$ 685,951	$ 651,133	$ 733,916
Manufacturing	536,006	496,154	624,586
Financial Services	206,061	184,253	188,365
Communities	92,170	89,699	92,492
Intersegment sales	(321,340)	(270,283)	(346,014)
	$1,198,848	$1,150,956	$1,293,345
Operating income			
Retail	$ 32,177	$ 28,712	$ 53,623
Manufacturing	46,761	36,637	62,729
Financial Services	124,909	95,469	108,792
Communities	13,938	14,022	16,130
Eliminations/other	(16,418)	(3,985)	(14,257)
	201,367	170,855	227,017
Interest			
Interest expense	(8,975)	(5,561)	(5,749)
Interest revenue/ other income	4,654	4,057	7,357
Income before taxes	$ 197,046	$ 169,351	$ 228,625
Identifiable assets			
Retail	$ 271,421	$ 255,793	$ 287,705
Manufacturing	79,102	82,616	100,112
Financial Services	1,210,460	1,080,416	902,913
Communities	191,147	191,802	185,784
Eliminations/other	76,273	43,543	29,864
	$1,828,403	$1,654,170	$1,506,378
Depreciation and amortization			
Retail	$ 4,753	$ 6,161	$ 5,639
Manufacturing	5,781	5,767	6,516
Financial Services	283	512	472
Communities	7,071	7,030	6,724
Eliminations/other	1,273	1,130	1,071
	$ 19,161	$ 20,600	$ 20,422
Capital expenditures			
Retail	$ 5,797	$ 5,211	$ 11,535
Manufacturing	5,834	4,346	9,558
Financial Services	87	88	454
Communities	7,033	13,920	12,059
Eliminations/other	1,736	994	792
	$ 20,487	$ 24,559	$ 34,398

Note 13 - Other Assets and Liabilities

At June 30, 2002, and 2001, other assets and liabilities consisted of:

(in thousands)	2002	2001
Other assets		
Interest and other receivables	$ 48,233	$ 63,442
Deferred insurance policy acquisition costs	20,529	19,716
Prepaid expenses and other	24,910	21,361
	$ 93,672	$104,519
Other liabilities		
Investors payable	$131,720	$101,379
Reserve for contingent liabilities	5,664	9,970
Escrow deposits	15,747	11,494
Unearned insurance premiums	100,712	96,555
Residual liability	52,161	-
Other	28,222	27,375
	$334,226	$246,773

Note 14 - Fair Value Disclosure of Financial Instruments

SFAS No. 107, *Disclosures About Fair Value of Financial Instruments,* requires that the Company disclose the estimated fair values of its financial instruments. The following methodologies and assumptions were used by the Company 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 the Company'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.

Contracts Held For Sale and as Collateral

Contracts held for sale are generally recent originations or purchased portfolios which will be sold with limited or no recourse during the following year. The Company 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. The Company 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 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 the Company for debt of similar maturities using a discounted cash flow calculation. Loan covenants preclude prepayment.

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

	June 30, 2002		June 30, 2001	
(in thousands)	**Carrying Amount**	**Estimated Fair Value**	Carrying Amount	Estimated Fair Value
Financial assets				
Cash and cash equivalents, including restricted cash	$200,028	$200,028	$158,823	$158,823
Contracts held for sale and as collateral, including accrued interest receivable	718,265	716,400	634,451	632,569
Residual interests in installment contract receivables	129,348	129,348	124,994	124,994
Securities available-for-sale	25,729	25,729	30,956	30,956
Financial liabilities				
Senior notes, 6.25%	75,000	74,705	75,000	73,642
Debt collateralized by installment contract receivables	2,176	2,462	5,229	5,645
Tax exempt bonds	15,230	15,230	15,230	15,230
Residual liability	52,161	52,161	-	-

Note 15 - Earnings Per Share

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)	2002	2001	2000
Net income	**$124,146**	$106,651	$144,025
Average shares outstanding			
Basic	**137,726**	137,702	139,474
Add: common stock equivalents (1)	**1,146**	638	341
Diluted	**138,872**	138,340	139,815
Earnings per share - Basic	**$0.90**	$0.77	$1.03
- Diluted	**$0.89**	$0.77	$1.03

(1) Common stock equivalents are principally stock options. Stock options to purchase 69,000, 2,414,826 and 3,500,784 shares of common stock for the years ended June 30, 2002, 2001, and 2000, respectively, were not included in the computation of diluted earnings per share because their inclusion would have been antidilutive.

Note 16 - Related Party Transactions

The Company maintains an agreement to purchase certain installment contract receivables originated or acquired by a finance company (the affiliate) in which the Company maintains a 50% ownership interest. Such receivables are subsequently securitized along with receivables originated and acquired by the Company. The Company is servicer for such receivables and maintains a servicing agreement with the affiliate to sub-service those receivables it sold to the Company. The amount paid to the affiliate in fiscal 2002 to sub-service those receivables was $25,400,000. The Company acquired approximately $190,000,000, $110,000,000, and $92,000,000 in installment contract receivables and received interest and other related fees totaling approximately $2,232,000, $1,880,000, and $1,618,000 during fiscal 2002, 2001 and 2000, respectively.

On December 21, 2001, the Company acquired approximately $900 million of installment contract receivables. The affiliate was contracted to service approximately $450 million of these installment contract receivables. At June 30, 2002 and 2001, the affiliate was servicing installment contract receivables totaling approximately $864,273,000 and $444,495,000, respectively.

BOARD OF DIRECTORS

James L. Clayton
Chairman of the Board, Clayton Homes, Inc.;
Director, Dollar General Corporation;
Director, Branch Banking & Trust Co. of North Carolina;
Chairman of the Board FSB Bancshares, Inc.

Kevin T. Clayton
Chief Executive Officer and President

C. Warren Neel (1)(2)
Commissioner, Finance and Administration,
State of Tennessee; Director, Sak's, Inc.;
Director, American Healthways, Inc.

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

Dan W. Evins (1)
Chairman of the Board, CBRL Group, Inc.

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

Wilma H. Jordan (1)(2)
Chief Executive Officer, Jordan, Edmiston Group, Inc.;
Director, LIN TV Corp.

(1) Audit Committee (2) Compensation Committee

OFFICERS

James L. Clayton
Chairman of the Board

Kevin T. Clayton
Chief Executive Officer and President

David M. Booth
Executive Vice President, Retail

Richard D. Strachan
Executive Vice President, Manufacturing

John J. Kalec
Executive Vice President and Chief Financial Officer

Allen Morgan
Vice President and General Manager, Communities

Amber W. Krupacs
Vice President, Finance

Greg A. Hamilton
Vice President and Treasurer

Carl O. Koella, III
Vice President, Investor Relations

Thomas D. Hodges
General Counsel and Corporate Secretary

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

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 44,000 beneficial holders of common stock on June 30, 2002.

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 October 30, 2002, at 10:30 a.m. (EST) at the Clayton Homes Headquarters, 5000 Clayton Road, Maryville, TN 37804. Shareholders of record at the close of business on August 15, 2002, will be entitled to vote.

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