

NOVEMBER 2007



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Marty's News & Notes

Featuring news about the Factory-Built Housing Industry
Contributing to the industry discussion...

POSITIVE REPORT

The October '07 HUDCode home shipments report came out with a positive number for the first time in many months. October 2006 saw a catastrophic 46% decrease in shipments. This October saw an increase of 0.7%, less than one percent, but at least a move in the right direction.

The 2007 annual shipments pace is only around 96,000 homes after October, running a range of between 95,000 and 97,500 homes, with November and December yet to be settled. There may be signs of a bottoming of the home shipments volume, but no signs at all of any bounce-back of any proportion whatsoever.

The real wild card in our near term prospects is the slow unraveling of the sub prime real estate mess. Looking back at 1989-1993 when I lived through another real estate bust, my impression is that this one has moved far slower. Still, it's scary enough so The Wall Street investor money markets have taken note and interest rates have risen, investor appetite for mortgage loans diminished, and the markets are in disarray. At the same time home values have plunged, at least in some markets.

Yet, the big expected influx of foreclosed properties has not hit. Yes, there has been some activity in sacrificed home sales, but, not yet a huge influx of repossessed homes. This has tended to move the unraveling process slower than I would have thought and has fooled me

as to what is the real scale of this episode. Is it really big or is the news media just talking it up?

Vulture

So I have been in contact with my guru on this matter. I won't identify him, but he is a "vulture investor," awaiting the disgorgement of bundles of bad paper to start in this cycle. In 1990-95 he bought hundreds of millions of dollars of "scratch and dent" mortgages for mere pennies and did very well during that episode. He has been rubbing his hands in anticipation of this one, and been doing so for a couple of years now.

I know he has been closely watching the current one unfold. He has expressed some frustration that it is moving slowly thus far. I've asked him whether he can be mistaken as to the scale of this episode. And his stock answer has been that the 1989-1993 RTC wipe-out will be "like a walk on a sunny day" in contrast to the downpour of troubled paper that will be disgorged this time, cheaply and with devastating results for the borrowers, loan investors, the economy and all innocent by-standers. It could be he will be seriously mistaken as to how bad it will get, but a recent incident gave a confirming nod to his position.

Old Friend

I spoke recently with a very long-time previous MH lender, whom I've

known since he was a very bright and very young man working with one of the former "Big Five" of the MH industry lenders. He has worked for a number of MH industry lending programs since, heading one. A couple of years back, after having so many MH lending horses shot out from under him, he escaped to the real estate finance world. I thought it a good move, after all, if we review the last 50 years, the real estate lending world has not entirely escaped its troubles, but compared to the continuous ravages visited on HUDville lending, it seemed a dream.

He had hardly got to his new office when the sub prime nature of their real estate loan portfolio became extremely evident. You know, "Manny being Manny." Well, "sub prime being sub prime," didn't disappoint. It acted just as one might expect. And why am I telling you this story? For those of you in the cloisters, believing this sub prime business will inure to the benefit of the factory built housing industry, let's go to the chalkboard.

My friend's company, a well-known mortgage lender and frequent buyer of troubled portfolios in the past, both real estate and MH, has recently been asked to meet certain money calls on some of their portfolios by investors and lenders. These calls for principle reduction are like calls on curtailments on homes in inventory. They are never easy to make, and assuming enough calls are made, one ultimately either goes extinct or bolts to the Chapter 11 office for shelter. This has happened throughout the sub prime lending world as most mortgage companies have closed, and those still open have taken a number as they wait their turn for salvation.

My, oh my

My friend's company suffered the same fate and now awaits a final disposition of what will occur to them. So what? This is an old story. Yes, it is, but can you quickly tell me the size of their portfolio and the average FICO score of their borrowers?

Answer. His company has a **\$50 billion dollar** portfolio. Note that their loan dollars outstanding could finance every single HUDCode home sold new and used for two full years. Also

note that at present all the MH industry lenders **combined** do not reach \$3 billion in loan volume, new and used, annually. We are talking pretty big numbers here, though they are hardly the largest mortgage company out there.

Now, for the olive in the martini, what is the average FICO score of this patch of loans held by this sub prime real estate lender? **638 FICO.** Yes, 638 FICO, is the average of the portfolio.

If we believe what the MH industry lenders tell us about their average FICO, they engage now primarily in the 720+ FICO lending game. They do this for several good reasons. It is true there is one exception, and that one industry lender probably has a FICO average 40-60 FICO points lower, but there are solid, unique reasons why their model works for them.

638 FICO for the portfolio? As to whether these types of borrowers can help MH, the first answer is that a great many of them, even if they don't default on their current sub prime loan, simply cannot be financed at HUDville. Either those types of loans, once originated, can't be resold, or they fall into risk categories too rich to touch. And if the borrowers have indeed defaulted on their sub prime real estate loan, our ability to help them ends.

So we start with the concept that manufactured housing lending cannot handle many sub prime borrowers (absent the infrequent 40% down payment loans). Even if these folks flee sub prime real estate and flood to us, we are in little position to fulfill their housing financing needs if they try to buy HUDCode housing.

Competition

But wait! It gets worse! My friend's company represents only a very small amount of the potential **trillions of dollars** out there in what is now or soon will be troubled sub prime portfolios. As these loans default, these site built homes will come on to the resale marketplace. Hundreds of thousands of repossessed homes may flood the market. Most will be in the high housing demand areas where we've had some recent success as an industry. They will be available for sale at greatly depressed prices, often with extremely favorable financing. These are our desired customers buying many homes from others whom we wanted to buy homes from us.

So, this sub prime mess seems little likely to help us. How could it? And waiting for this train to stop at our station seems less than rational. Still, many continue to hold out this hope, though the number believing that hope seems to be fading recently.

As we go into the seasons of "cheer," we seem light on that commodity in factory built housing. The industry continues "Chris Stinebert Light" as its operating mode, still trying for government help as the main elixir, where instead a substantial model change is needed. That is not forthcoming, little attention being paid to the; . . . gasp! Customer!

Don't believe me? Look at the December 3, 2007 "MHI Members Report" and see if you get the feeling Washington, D.C. is where it is at, not Main Street. Do you think that is where salvation lies?

And the leader...

I am frequently cited as pessimistic instead of realistic. So I am going with the higher home shipments pace to put the best light on it. In that case the pace hovers around 97,500 home shipments for 2007 total, and we have people who predicted close to that level. The leader at present for the **MHL Corp Annual Shipments** contest is **Austin Baidas, the "big guy" at Four Seasons Housing**, who predicted 97,875 homes to be shipped, way back in January, which now seems like a long time ago. We appear to be snuggling into a year of less than 100,000 homes shipped, with continued weak prospects at present for shipments increases in November and December. Those shipments are yet to be released, but it will be hard to finish the year at 100,000 homes or better. This even as 2006 saw 117,500 homes shipped. Again, another strong decrease year over year.

And modular homes have not been able to help, though less affected. 2005 saw around 43,000 mods shipped, 2006 around 37,000, and the grim prediction is for a 33,000-35,000 finish in 2007. A challenging state of affairs, to say the least.

Final

I prepared a paper with a series of predictions as to the probable future course of the HUDCode housing industry over the next 5-10 years. After reading it, I was so dismayed that I will not make a general release of the document. If you email me directly requesting a copy, I will send you a copy, if I decide to release the document at all. It's grim and disheartening. In spite of this the industry Pollyannas keep "talking it up," as though all it is going to take is positive rhetoric.

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