Chattel Lending Today

IS IT DEAD OR ALIVE?

By Martin V. Lavin

Chattel lending for manufactured housing has undergone a substantial change over the last 15 years. As Wall Street analysts and others have released more and better information about loan performance, evidence of four distinct periods of chattel lending have emerged.

THE FOUR PERIODS OF CHATTEL LENDING

The first period stretches from 1987 through 1994. By most accounts, securitized loans from this period performed well and sold into the marketplace as asset-backed securities (ABS)—the industry's preferred method of procuring money. All parties got what they bargained for and the initial performance of these loans undoubtedly spurred the enormous success of the industry in increasing HUD-Code home deliveries from 171,000 in 1991 to 303,932 in 1994.

The second period began in 1995 and closed in 1997. This was the beginning of free-wheeling retail lending terms, when many long-time industry loan prohibitions were discarded. Repayment terms of up to 30 years became standard and low down payments of 5 percent were common. It took a while to show, as the originating lenders may have been doing some skilled footwork to conceal the truth, but we now know performance was rapidly deteriorating. Meanwhile, shipments rose from 339,601 in 1995 to 354,000 in 1997.

The third period arose in 1998 and closed in 2001. There is no way to gloss over this highly destructive period of retail chattel lending other than to say that is appears that little was done right and much was done poorly. The horrific losses will hopefully never be repeated in the industry. It led to failed companies and a crisis in liquidity. Its results are still with the industry today.

The final period started in 2002. By then a significant improvement in loan quality became evident. It is here that the industry is now positioned. This period is marked by poor industry liquidity for retail loans, a far downsized industry, and a greater percentage of loans secured by real estate with an emphasis on larger, better and more expensive homes.

While it is heartening that manufactured home lender performance is much better, there has not yet been sufficient loan origination volume for a long enough time to confirm a positive change. Industry pundits herald the changes, but the money markets are slow to buy in—still sitting on the sidelines with their arms crossed, unconvinced.

MEETING THE CHALLENGE OF CHANGE

With the retail lenders taking the lead, the Manufactured Housing Institute (MHI) has championed and adopted a number of initiatives to encourage and direct a consistently better lending culture. Truth in Invoicing Practices Statement (TIPS), Lender Best Practices (LBP), MARI (a database of bad actors), MHI Industry Database (MLS+), Community Attributes System (CAS) and Community/Lender Agreement (risk sharing) are all either already adopted or well along toward implementation. These industry enhancements have all received high marks from Wall Street and others and are setting the stage for an industry lending rebound.

While the increased emphasis on better lending has moved modular homes and larger homes to new industry heights of activity, especially with conforming financing, the industry does not and cannot give up the volume of homes going into land-lease communities. For a variety of reasons, that segment was most hurt by the loss of chattel loan liquidity. This has led to a reduction of HUD-Code home sales, estimated by analysts to be a loss of 100,000 new homes annually or even more. It is here where the most help will be needed to jumpstart industry success.

With the poor loan performance of homes in land-lease communities a new chattel loan strategy has arisen—or more properly, has returned. Shorter repayment terms now prevail, along with verification of loan details, a requirement for better credit and enhanced underwriting. Together, they have significantly

Experts **SPEAK OUT** About the Future

Interviews with chattel lenders provide interesting insights into manufactured home lending.

DON GLISSON, the energetic young CEO of **Triad Financial** noted that he foresees greater industry liquidity in 2005, but little change in relaxing tightened industry underwriting. He remarked that industry lenders are better disciplined and execute originations on chattel loans in a better fashion. He further stated that the chattel loan program at Triad is its most popular program and always has been.

JOE CORONA, the youthful, but highly experienced hand at **HomeOne Credit**, a Fleetwood Enterprises lending subsidiary, notes how successful the MHI initiatives have been, especially Lender Best Practices (LBP), of which Joe is the current committee chairman. Corona is delighted with the very positive press coverage and investor reception accorded LBP since its inception. LBP has just undergone a significant overhaul, making the designation and certification even more restrictive and the reporting requirement to investors more transparent.

TOM FRANCO, the CEO of old industry returnee **GreenTree Servicing Inc.**, is looking forward to their substantial re-emergence into manufactured home lending. Tom remarked that they are basing much of their early return to lending with the use of "special agreements with our large, national [community] owner relationships that we believe will positively impact our chattel lending program." Franco is another lender who sees merit in the MHI-approved Community/Lender Agreement.

DAVID RAND, senior vice-president at Origen Financial, and incoming chairman of the MHI Financial Services Division, was very much in synch with the remarks made by others. His response to the question about the other enhancements MHI and the industry should implement was interesting. Rand felt that every industry lender, along with MHI, should encourage better training for retailers and their staffs. Rand and Origen believe better training will spur increased consumer value and lead to an industry rebound. He wrote, "To that end we (Origen) have been offering training programs to retail partners." Origen has been an industry leader in many areas and has been a frequent visitor to Wall Street recently as it tries to revive that loan funding conduit.

ANDY GRIGGS, of San Antonio Credit Union, again a wise old hand at chattel lending, is in charge of this new chattel lender. Griggs echoed the refrain from other lenders, saying, "We intend to provide the liquidity needed to make the loan provided the customer meets our underwriting criteria." The sense from all chattel lenders being that there is ample liquidity now for chattel lending for every "loan that should be bought."

improved loan quality. Additionally, industry chattel lenders continue to refine their originations—building ever more knowledgeable and rational lending bases.

In a move predicted by some in the industry, smaller, less expensive single-section homes, which tend to be located in land-lease communities, have recently regained much of the vigor they lost after chattel lending changes in 1996. Those changes allowed buyers to afford more expensive homes because of the lengthened loan repayment terms which favor up-scale multi-section homes. With the return of more restrictive and reduced repayment terms, the industry has tuned its focus back to lower-priced homes in order to regain affordability. Many expect this single-section, lower-cost trend to continue.

NEW APPROACH TO RISK

In a new move, some community owners, many of them large, sophisticated organizations, have quietly launched their own internal lending programs. Experience has shown them that financing borrowers in their own communities, coupled with a hands-on approach, can successfully open buyer segments which have been problematic for stand-alone chattel lenders. Expect this very positive trend to continue as results are corroborated over time.

It also seems a foregone conclusion that lender and community, or lender and manufacturer, or even all three, will unite to reduce the risk-potential of in-community chattel lending. This is a very positive move for the industry, which is not content to give up the significant number of chattel-financed homes which are now missing.

THE VERDICT FOR CHATTEL LENDING

In preparing for this article, a questionnaire was sent to each of the industry chattel lenders asking them to comment on the state of chattel lending in the industry today.

There were certain threads constantly woven through the lender responses. No one thought chattel lending was a dead financing vehicle. Quite the contrary, every leader is exploring the methods that they can adapt in their underwriting, originating and servicing to successfully increase chattel lending over the coming years.

Lenders are very interested in doing a better job of financing home resales, particularly in communities. Most noted the need for better resale financing to decrease home depreciation and increase customer value, a component the industry and MHI both view as an imperative.

To that end, things like a Manufacturers Suggested Retail Price (MSRP), Invoice Database, MHI Industry Database, Community Attributes System and other enhancements and protections were highly favored. As Tom Franco of GreenTree remarked, "We've got to lend in a fashion which will restore the confidence of the money markets to re-enter our industry." The enhancements enacted by MHI were seen as tools to reach that goal.

Where was the lender concurrence?

1. Most thought credit underwriting would change little in 2005.

2. There was a sense that for the time being, the challenge was to bring better liquidity and lower interest rates to retail chattel lending.

3. Few expected irrational lending to rear its ugly head anytime soon.

4. Most thought the worse was over for defaults and repossessed homes.

5. There was little expectation of new chattel lenders quickly entering the market.

6. The greatest challenges seen by lenders were first the liquidity challenge and then extending the liquidity to the 600-650 FICO credit tier, where so much demand for manufactured housing springs.

It looks like the better news is that 2005 will see better chattel lending availability than in previous years. The challenge remains to find a way to make survivable loans in communities to a greater cross-section of customers. Year 2005 seems poised to somewhat expand the universe of originations.

And finally, as interest rates for conforming mortgages rise to more normal levels and the interest-rate differential between manufactured and site-built homes closes, competitiveness for the better credit tiers seems certain to increase. Many believe all the foregoing trends will mark a much better 2005, leading to a final stemming of industry losses and the foundation upon which a better-behaved industry can return to growth and success. ■

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