INVESTOR'S BUSINESS DAILY®

Thursday, January 15, 2004

The New America

ACCREDITED HOME LENDERS HOLDING CO. *San Diego, California*

Lender Upbeat Despite Signs Of Slowdown

BY LAURA MANDARO
INVESTOR'S BUSINESS DAILY

Ask Ray McKewon to name the biggest risks facing Accredited Home Lenders Holding Co. this year, and interest rates don't even make the top three.

This despite the fact that his company makes mortgage loans – a product whose popularity generally ebbs and flows with the economic and interest-rate cycle.

Why the lack of concern over interest rates?

"(Because) that's the one we know the most about," said McKewon, who serves as Accredited's vice president and co-founded the company 13 years ago.

Of greater concern are a couple matters over which Accredited has less control: local regulation of the mortgage industry, and what McKewon calls "irrational competition."

Subprime lenders are battling legislative efforts from New Jersey to California that put special conditions on makers of high-rate loans in a bid to curb predatory practices.

Meanwhile, Accredited says it's resisting a growing trend among rivals to make loans at below-market prices.

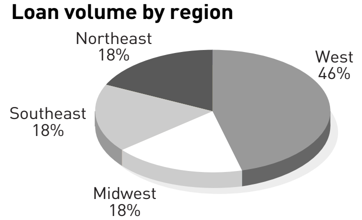
Since August, McKewon says, he's seen some lenders undercut market prices to keep volumes high in the face of waning origination volumes.

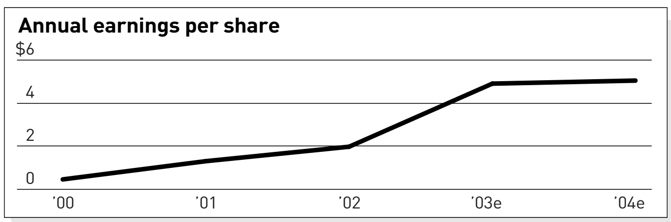
Holding Steady – For Now

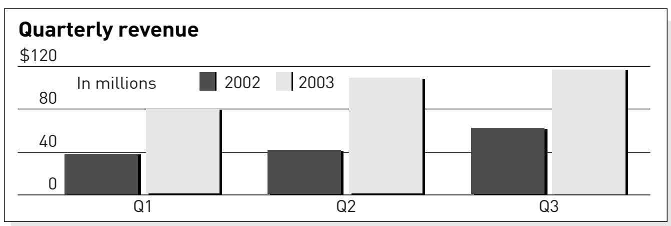
Total U.S. mortgage productions are slated to fall by 50% next year. Subprime mortgages, Accredited's main product, might fall by only 10% to 20%.

Lending Spree

Accredited Home Lenders saw a dramatic spike in business last year, thanks in part to the strong housing and refinancing markets. Profit growth is expected to slow this year, however. Most of the company's business comes from Western states, with the rest evenly split between other regions







Sources: First Call, company reports

"If the marketplace works for less margin, we have three responses: hold more loans, grow more slowly and cut costs."

Ray McKewon, *vice-president and co-founder, Accredited Home Lenders Inc.*

"If there's anything that keeps me up at night with Accredited, it's the irrationality of pricing," said analyst Kevin Maynard of Veredus Asset Management, which owned 2.6% of Accredited as of Sept. 30.

Accredited has managed to hold its rates steady. In case it needs to lower them, the firm is keeping an eye on costs.

Among other things, it looks to reduce origination expenses, currently at an average 2% a loan.

"If the marketplace works for less margin, we have three responses: hold more loans, grow more slowly and cut costs," McKewon said.

For now, Accredited maintains a positive bottom-line outlook.

In early December, the company raised its 2003 earnings guidance to a range of $4.85 to $4.95 a share, up from its earlier forecast of $4.50 to $4.75.

The hike was partly due to better-than-anticipated production volumes and lower-than-expected costs to originate the loans.

Accredited earned $1.40 a share during its most recent quarter, up 82% from the prior year. Revenue gained 89% to $116.2 million.

The company expects 2004 earnings of $5 to $5.25 a share. Though that's not a huge increase, it is an increase – not bad, considering that the industry itself is expected to contract.

After three years of a refinance-related boom, mortgage applications have started to slow and should continue to trend down next year.

In the week ending Jan. 9, the Mortgage Bankers Association's applications index was 40% below its year-ago level. The refinance application index was 62% lower.

But Accredited and subprime rivals Saxon Capital Inc., New Century Financial Corp. and NovaStar Financial Corp. claim at least one advantage: They don't have to rely on refinance business.

During the first nine months of 2003, only 9% of Accredited's $5.6 billion in loans were refinance-related.

The bulk of originations came from a debt consolidation product that exchanges a borrower's existing credit, other high-rate loans and current mortgage for a longer-term mortgage with Accredited.

How big is this market?

The industry rule of thumb is that 25% of a metropolitan market such as Chicago is facing a credit challenge, McKewon says.

According to SMR Research Corp., 34% of households that have applied for a mortgage would be considered subprime borrowers, but only 10% of all residential mortgages are subprime.

The gap suggests there's a pool of borrowers eligible for subprime loans and ripe for lenders such as Accredited.

The REIT Stuff?

Whatever the market's size, Accredited's 2.4% share gives it plenty of room to grow.

"They're a very small player, and I think they have the advantage of approaching a much bigger market," said Alan Fournier, general partner at Chatham, N.J.-based Pennant Capital Management, which owned 4.5% of the firm in September.

He says Pennant bought stock in Accredited because of its management's experience and the attractiveness of the subprime market.

Fournier is watching whether Accredited – or one its rivals – follows a smaller competitor and becomes a real estate investment trust, or REIT.

In mid-December, Fieldstone Investment Corp. closed a $703 million common stock private offering that put a portfolio of its loans in a REIT structure.

The market's positive reaction to the offering – coupled with the expected slowdown in origination volumes – has fueled the notion that other subprime lenders might follow suit.

Some companies might be attracted to a REIT because as originations slow down, they might not need as much capital to grow the business.

Through the REIT structure, they can funnel that to shareholders in the form of a dividend.

And the higher dividend yield could give them a higher market valuation.

Fournier figures that for some, the move to a REIT structure could drive up their shares by 50%.

Top Performer

It's not as though Accredited's stock needs a lot of help right now. It debuted in February, then became one of the top new issues of 2003, rising from an opening price of 8 to a Dec. 31 close of 30.50.

McKewon says a REIT conversion is on a list of capital management options Accredited is studying – including a secondary equity offering, a convertible debt offering, a commercial paper conduit "or nothing."

"If we can do something that lowers our cost of capital or enhances our capital structure to the marketplace, (we'll consider it)," he said.

The backbone of Accredited's business model is that customers will pay back their mortgages.

Periods of higher unemployment, while stoking more demand for debt reduction products, also weigh on borrowers' abilities to pay back their loans.

Accredited has a "positive outlook in regard to its loans," McKewon said, citing higher quality borrowers and better collection efforts.

"We're less confident that the industry as a whole is doing a good job of assessing and pricing risk," McKewon said. "We have to make sure we don't do what our competitors do."

Accredited Home Lenders Co.
accredhome.com

Ticker	LEND
Share price	Near 35
12-month sales	$364 mil
5-year profit growth rate	148%

IBD SmartSelect Corporate Ratings

Earnings Per Share	99
Relative Price Strength	94
Industry Group Relative Strength	C+
Sales+Profit Margins+ROE	A
Accumulation/Distribution	B-

See investors.com for more details

ACCREDITED℠
HOME LENDERS

CONTACT INFORMATION

Rick Howe
Director of Corporate Communications
Telephone: 858.676.2148
rhowe@accredhome.com

Mitzi Gimenez
Investor Relations/PR Coordinator
Telephone: 858.676.2155
mgimenez@accredhome.com

15090 Avenue of Science, San Diego, CA 92128 T 800.690.6000 F 858.676.2170 www.accredhome.com