Financial News

Investor's Business Daily

Demand For Low-Interest Loans Keeps This Firm In The Money

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By Marilyn Alva

Home loan officers are among the busiest workers in America these days, and those who work at Accredited Home Lenders Holding Co. (NasdaqNM:LEND - News) are no exception.

The firm deals mostly in subprime loans to customers who don't qualify for conventional loans or who want to cash out some of the equity in their homes to consolidate debt.

Buoyed by a strong mortgage market, Accredited generated a record $1.5 billion in loan originations in the first quarter - almost double the prior year's total. Loan volume in 2002 totaled $4.3 billion.

The sheer volume has made for some long workdays. Still, many loan officers would rather work longer hours than give up their share of their team's profits to a new member, says Ray McKewon, Accredited's co-founder and executive vice president.

Profit incentives are part of the company's culture. Loan officers are rewarded for accurately assessing and pricing risk and keeping costs within reason - down to phone and FedEx bills.

"We give them profit and loss responsibility, decision-making authority and real-time monitoring of their unit's profit and loss performance," McKewon said.

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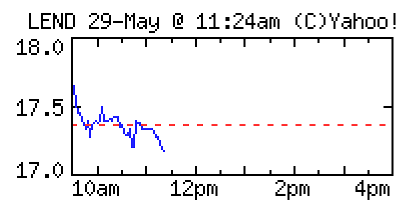

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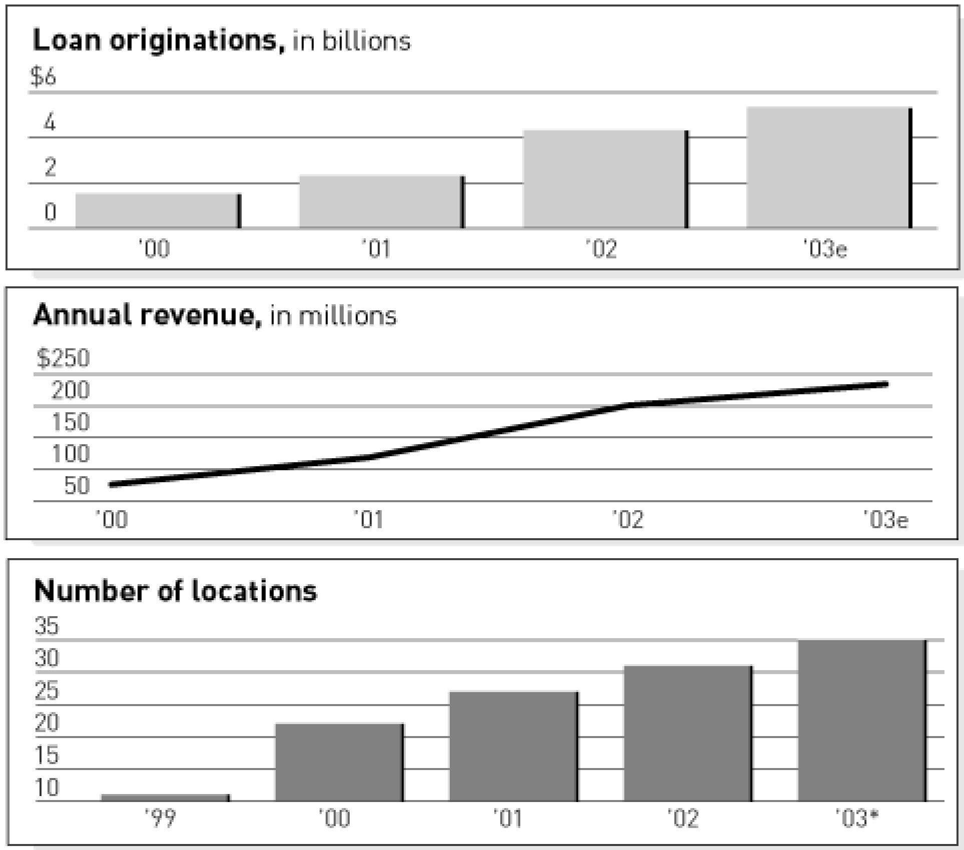
Working Overtime

Continued demand for its subprime mortgage loans has helped fatten Accredited Home Lenders' top line and led the firm to open more locations



Sources: Company reports, Friedman Billings Ramsey *as of March 31

He said the company spends "extraordinary amounts of time" screening recruits, training them and supporting them with technology tools.

The profit- and performance-based culture has helped keep delinquency rates relatively low and earnings strong.

At the end of the last quarter, Accredited's delinquency rate was less than 3% - well below the 10% rate of many subprime lenders. Its average credit score last year was also better than the average for subprime lenders.

The company posted first-quarter earnings of 85 cents a share, up 124% from a year earlier. Revenue more than doubled to $79.1 million.

The focus on a strong bottom line has gone on for some time, McKewon says.

"We've been behaving like a public company from the beginning," he said. "We've always maximized shareholder value, controlled salaries and left profits in the company."

Accredited didn't go public until February, however, 13 years after its founding. Since the initial public offering, the stock has roughly doubled.

McKewon says some proceeds of the $39 million the company netted in the IPO will be used to hire more people, and perhaps open new offices.

Accredited has 35 locations around the U.S., with a third of them in California.

"That is not really many locations," McKewon said. "We can grow where we're not and we can grow where we are."

Execs have no plans to grow through acquisitions, however.

Meanwhile, the company faces a number of risks, says analyst Todd Pitsinger of Friedman Billings Ramsey, the lead investment bank on Accredited's IPO. Among other things, he points to the chance that real-state values will decline and interest rates will rise.

But earnings volatility tops the list. Accredited's quarterly earnings are driven primarily by origination volumes and loan sales to the secondary markets, Pitsinger notes. Changes in those two areas would impact the company's profit.

To build a more consistent source of earnings, Accredited recently increased the amount of loans it retains on its balance sheet and reduced the number it sells to the secondary market.

The move hurts profit in the short-term, but increases interest income for the long term.

Last year, the firm kept $749 million in loans on its balance sheet. It held nearly $243 million worth of loans in the first quarter.

Accredited still sells more loans than it keeps, McKewon says.

"There are times when it's smarter to keep than sell," McKewon said. "Now the secondary markets are great. We're getting $104 for every $100. That's $4 of gross profit."

With interest rates still near all-time lows, the market for mortgages remains hot. The Mortgage Bankers Association of America - which not long ago predicted volume would drop in the second half of the year to an annualized rate of less than $2 trillion - recently raised its estimate to $3 trillion.

The brisk loan-volume pact might lead to another record year for Accredited, McKewon says. At the same time, he concedes, financial fortunes can turn on a dime.

"This is a business where you move an awful lot of money around and in a fairly volatile rate environment," he said. "You have to be vigilant all the time. We remain focused on the moment to moment, day to day, month to month, quarter to quarter - and the long term."

The short-term outlook looks positive. Analysts polled by First Call expect Accredited to earn $2.65 a share this year, up from $1.98 in 2002.

The long-term picture is a little murkier, however, with First Call predicting an 8% decline in 2004 earnings.

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