CAVCO INDUSTRIES INC
Form 10-Q
August 08, 2017

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q
(Mark One)
ý QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended July 1, 2017
OR
¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to

Commission File Number 000-08822

Cavco Industries, Inc.
(Exact name of registrant as specified in its charter)

Delaware	56-2405642
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

1001 North Central Avenue, Suite 800
Phoenix, Arizona 85004
(Address of principal executive offices, including zip code)
602-256-6263
(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last year)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý No ¨
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý No ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a small reporting company. See definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	¨	Accelerated filer	ý
Non-accelerated filer	¨ (Do not check if a smaller reporting company)	Smaller reporting company	¨
Emerging Growth Company	¨		

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ¨

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No ý

As of August 4, 2017, 9,019,445 shares of Registrant's Common Stock, $.01 par value, were outstanding.

CAVCO INDUSTRIES, INC.
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PART 1. FINANCIAL INFORMATION
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CAVCO INDUSTRIES, INC.
CONSOLIDATED BALANCE SHEETS
(Dollars in thousands, except per share amounts)

	July 1, 2017 (Unaudited)	April 1, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$ 129,509	$132,542
Restricted cash, current	13,323	11,573
Accounts receivable, net	34,490	31,221
Short-term investments	12,386	11,289
Current portion of consumer loans receivable, net	33,159	31,115
Current portion of commercial loans receivable, net	7,380	7,932
Inventories	99,080	93,855
Prepaid expenses and other current assets	27,317	28,033
Deferred income taxes, current	—	9,204
Total current assets	356,644	356,764
Restricted cash	725	724
Investments	30,440	30,256
Consumer loans receivable, net	65,220	64,686
Commercial loans receivable, net	18,910	17,901
Property, plant and equipment, net	57,587	56,964
Goodwill and other intangibles, net	80,129	80,021
Total assets	$ 609,655	$607,316
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 25,003	$24,010
Accrued liabilities	111,226	109,789
Current portion of securitized financings and other	6,149	6,417
Total current liabilities	142,378	140,216
Securitized financings and other	51,440	51,574
Deferred income taxes	11,429	21,118
Stockholders' equity:		
Preferred stock, $.01 par value; 1,000,000 shares authorized; No shares issued or outstanding	—	—
Common stock, $.01 par value; 40,000,000 shares authorized; Outstanding 9,018,820 and 8,994,968 shares, respectively	90	90
Additional paid-in capital	243,524	244,791
Retained earnings	159,963	148,141
Accumulated other comprehensive income	831	1,386
Total stockholders' equity	404,408	394,408
Total liabilities and stockholders' equity	$ 609,655	$607,316

See accompanying Notes to Consolidated Financial Statements

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CAVCO INDUSTRIES, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Dollars in thousands, except per share amounts)
(Unaudited)

	Three Months Ended	
	July 1, 2017	July 2, 2016
Net revenue	$206,816	$185,141
Cost of sales	164,850	151,889
Gross profit	41,966	33,252
Selling, general and administrative expenses	26,305	24,687
Income from operations	15,661	8,565
Interest expense	(1,048)	(1,161)
Other income, net	1,038	1,026
Income before income taxes	15,651	8,430
Income tax expense	(3,898)	(2,987)
Net income	$11,753	$5,443
Comprehensive income:		
Net income	$11,753	$5,443
Unrealized loss on available-for-sale securities, net of tax	(555)	(55)
Comprehensive income	$11,198	$5,388
Net income per share:		
Basic	$1.30	$0.61
Diluted	$1.28	$0.60
Weighted average shares outstanding:		
Basic	9,006,999	8,937,265
Diluted	9,162,491	9,085,042

See accompanying Notes to Consolidated Financial Statements

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CAVCO INDUSTRIES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in thousands)
(Unaudited)

	Three Months Ended	
	July 1, 2017	July 2, 2016
OPERATING ACTIVITIES		
Net income	$ 11,753	$ 5,443
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	974	946
Provision for credit losses	27	85
Deferred income taxes	(62)	(91)
Stock-based compensation expense	513	370
Non-cash interest income, net	(254)	(315)
Incremental tax benefits from option exercises	—	(1,946)
Gain on sale of property, plant and equipment, net	(64)	(22)
Gain on sale of loans and investments, net	(2,110)	(2,171)
Changes in operating assets and liabilities:		
Restricted cash	(1,798)	(296)
Accounts receivable	(1,974)	791
Consumer loans receivable originated	(34,389)	(25,622)
Principal payments on consumer loans receivable	3,135	3,007
Proceeds from sales of consumer loans	29,252	25,800
Inventories	(3,727)	17
Prepaid expenses and other current assets	2,426	(1,176)
Commercial loans receivable	(469)	(1,572)
Accounts payable and accrued liabilities	(3,280)	4,953

Net cash (used in) provided by operating activities	(47)		8,201	
INVESTING ACTIVITIES				
Purchases of property, plant and equipment	(594)		(1,890)	
Payments for Lexington Homes, net	(564)		—	
Proceeds from sale of property, plant and equipment	387		25	
Purchases of investments	(1,646)		(2,440)	
Proceeds from sale of investments	1,809		3,093	
Net cash used in investing activities	(608)		(1,212)	
FINANCING ACTIVITIES				
Payments from exercise of stock options	(1,780)		(2,287)	
Incremental tax benefits from exercise of stock options	—		1,946	
Proceeds from secured financings and other	1,505		294	
Payments on securitized financings	(2,103)		(2,214)	
Net cash used in financing activities	(2,378)		(2,261)	
Net (decrease) increase in cash and cash equivalents	(3,033)		4,728	
Cash and cash equivalents at beginning of the period	132,542		97,766	
Cash and cash equivalents at end of the period	$ 129,509		$ 102,494	
Supplemental disclosures of cash flow information:				
Cash paid during the year for income taxes	$ 2,118		$ 3,734	
Cash paid during the year for interest	$ 767		$ 904	

See accompanying Notes to Consolidated Financial Statements

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CAVCO INDUSTRIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation

The accompanying unaudited Consolidated Financial Statements of Cavco Industries, Inc., and its subsidiaries (collectively, the "Company" or "Cavco"), have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC") for Quarterly Reports on Form 10-Q and Article 10 of SEC Regulation S-X. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles ("GAAP") have been condensed or omitted pursuant to such rules and regulations.

In the opinion of management, these statements include all of the normal recurring adjustments necessary to fairly state the Company's Consolidated Financial Statements. Certain prior period amounts have been reclassified to conform to current period classification. The Company has evaluated subsequent events after the balance sheet date through the date of the filing of this report with the SEC; there were no disclosable subsequent events. These Consolidated Financial Statements should be read in conjunction with the audited Consolidated Financial Statements and the Notes to Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the year ended April 1, 2017, filed with the SEC on June 13, 2017.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the Consolidated Financial Statements and the accompanying Notes. Actual results could differ from those estimates. The Consolidated Statements of Comprehensive Income and Consolidated Statements of Cash Flows for the interim periods are not necessarily indicative of the results or cash flows for the full year. The Company operates on a 52-53 week fiscal year ending on the Saturday nearest to March 31 of each year. Each fiscal quarter consists of 13 weeks, with an occasional fourth quarter extending to 14 weeks, if necessary, for the fiscal year to end on the Saturday nearest to March 31. The Company's current fiscal year will end on March 31, 2018.

The Company operates principally in two segments: (1) factory-built housing, which includes wholesale and retail systems-built housing operations, and (2) financial services, which includes manufactured housing consumer finance and insurance. The Company designs and builds a wide variety of affordable modular homes, manufactured homes and park model RVs in 20 factories located throughout the United States, which are sold to a network of independent retailers, through the Company's 42 Company-owned retail stores and to community owners and developers. Our financial services group is comprised of a mortgage subsidiary, CountryPlace Acceptance Corp. ("CountryPlace"), and an insurance subsidiary, Standard Casualty Co. ("Standard Casualty"). CountryPlace is an approved Federal National Mortgage Association ("FNMA" or "Fannie Mae") and Federal Home Loan Mortgage Corporation ("FHLMC" or "Freddie Mac") seller/servicer, and a Government National Mortgage Association ("GNMA" or "Ginnie Mae") mortgage-backed securities issuer which offers conforming mortgages, non-conforming mortgages and chattel loans to purchasers of factory-built and site-built homes. Standard Casualty provides property and casualty insurance to owners of manufactured homes.

On April 3, 2017, the Company acquired Lexington Homes, Inc. ("Lexington"), which produces manufactured homes distributed in the Southeastern United States. This operation includes a manufactured housing production facility in Lexington, Mississippi and provides for further operating capacity, increased home production capabilities and further distribution into certain markets. The acquisition was accounted for as a business combination and the results of operations have been included since the date of acquisition. Our purchase price allocation is preliminary and subject to revision as more detailed analyses are completed and additional information about fair value of assets and liabilities becomes available, including additional information relating to tax matters and finalization of our valuation of identified intangible assets. Pro forma results of operations for the acquisition during the current period has not been presented because the effects of the business combination were not material to our consolidated results of operations.

Recent Accounting Pronouncements. In November 2015, the FASB issued ASU 2015-17, Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes ("ASU 2015-17"). ASU 2015-17 became effective in fiscal year 2018. Therefore, we presented all deferred tax liabilities and assets as noncurrent on the balance sheet instead of separating deferred taxes into current and noncurrent amounts. Prior period was not retrospectively adjusted. In addition, in March 2016, the FASB issued ASU 2016-09, Compensation- Stock Compensation (Topic 718) ("ASU 2016-09"), which also became effective in fiscal year 2018. As a result of this required implementation, excess tax benefits are recorded on exercises of stock options as a reduction of income tax expense in the consolidated statement of comprehensive income, whereas they were previously recognized in equity.

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers (Topic 606) ("ASU 2014-09"), which outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The standard requires entities to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The new guidance also includes a cohesive set of disclosure requirements intended to provide users of financial statements with comprehensive information about the nature, amount, timing and uncertainty of revenue and cash flows arising from a company's contracts with customers. In August 2015, the FASB issued ASU 2015-14, Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date, which deferred the effective date of the new revenue standard. Accordingly, the updated standard is effective for us beginning with the first quarter of the Company's fiscal year 2019. The standard allows for either "full retrospective" adoption, meaning the standard is applied to all of the periods presented, or "modified retrospective" adoption, meaning the standard is applied only to the most current period presented in the financial statements. The Company is currently evaluating the effect ASU 2014-09 will have on the Company's Consolidated Financial Statements and disclosures.

In January 2016, the FASB issued ASU 2016-01, Financial Instruments (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities ("ASU 2016-01"). ASU 2016-01 will be effective beginning with the first quarter of the Company's fiscal year 2019. The amendments require certain equity investments to be measured at fair value, with changes in the fair value recognized through net income. The Company is currently evaluating the effect ASU 2016-01 will have on the Company's Consolidated Financial Statements and disclosures.

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842) ("ASU 2016-02"). ASU 2016-02 will be effective beginning with the first quarter of the Company's fiscal year 2020, with early adoption permitted. The amendments require the recognition of lease assets and lease liabilities on the balance sheet for most leases, but recognize expenses in the income statement in a manner similar to current accounting treatment. In addition, disclosures of key information about leasing arrangements are required. Upon adoption, leases will be recognized and measured at the beginning of the earliest period presented using a modified retrospective approach. The Company is currently evaluating the effect ASU 2016-02 will have on the Company's Consolidated Financial Statements and disclosures.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments ("ASU 2016-13"). ASU 2016-13 changes the impairment model for most financial assets and certain other instruments, which requires a new forward-looking impairment model based on expected losses rather than incurred losses. The guidance also requires increased disclosures. ASU 2016-01 will be effective beginning with the first quarter of the Company's fiscal year 2021. The Company is currently evaluating the effect ASU 2016-13 will have on the Company's Consolidated Financial Statements and disclosures.

In November 2016, the FASB issued ASU 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash (a consensus of the FASB Emerging Issues Task Force ("ASU 2016-18"), which provides guidance on the presentation of restricted cash or restricted cash equivalents in the statement of cash flows. ASU 2016-18 will be effective beginning with the first quarter of the Company's fiscal year 2019. The adoption of ASU 2016-18 is not expected to have a material impact on the consolidated financial statements and will only change the presentation of the Consolidated Statement of Cash Flows.

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In March 2017, the FASB issued ASU 2017-08, Receivables — Nonrefundable Fees and Other Costs (Subtopic 310-20), Premium Amortization on Purchased Callable Debt Securities ("ASU 2017-08"), which requires the premium on callable debt securities to be amortized to the earliest call date as opposed to the contractual life of the security. ASU 2017-08 will be effective beginning with the first quarter of the Company's fiscal year 2020. The Company is currently evaluating the effect ASU 2017-08 will have on the Company's Consolidated Financial Statements and disclosures.

From time to time, new accounting pronouncements are issued by the FASB and other regulatory bodies that are adopted by the Company as of the specified effective dates. Unless otherwise discussed, management believes that the impact of recently issued standards, which are not yet effective, will not have a material impact on the Company's Consolidated Financial Statements upon adoption.

For a description of other significant accounting policies used by the Company in the preparation of its Consolidated Financial Statements, please refer to Note 1 of the Notes to Consolidated Financial Statements in the Form 10-K.

2. Restricted Cash

Restricted cash consists of the following (in thousands):

	July 1, 2017	April 1, 2017
Cash related to CountryPlace customer payments to be remitted to third parties	$11,706	$9,998
Cash related to CountryPlace customer payments on securitized loans to be remitted to bondholders	1,344	1,391
Cash related to workers' compensation insurance held in trust	354	354
Other restricted cash	644	554
	$14,048	$12,297

Corresponding amounts are recorded in accounts payable and accrued liabilities for customer payments, deposits and other restricted cash.

3. Investments

Investments consist of the following (in thousands):

	July 1, 2017	April 1, 2017
Available-for-sale investment securities	$24,934	$24,162
Non-marketable equity investments	17,892	17,383
	$42,826	$41,545

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The following tables summarize the Company's available-for-sale investment securities, gross unrealized gains and losses and fair value, aggregated by investment category (in thousands):

	July 1, 2017			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury and government debt securities	$350	$ —	$ (1)	$349
Residential mortgage-backed securities	5,838	3	(90)	5,751
State and political subdivision debt securities	6,920	165	(114)	6,971
Corporate debt securities	1,694	7	(9)	1,692
Marketable equity securities	6,058	1,463	(112)	7,409
Certificates of deposit	2,762	—	—	2,762
	$23,622	$ 1,638	$ (326)	$24,934

	April 1, 2017			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury and government debt securities	$650	$ —	$ (1)	$649
Residential mortgage-backed securities	5,646	3	(90)	5,559
State and political subdivision debt securities	7,195	145	(117)	7,223
Corporate debt securities	1,698	4	(23)	1,679
Marketable equity securities	5,752	2,430	(130)	8,052
Certificates of deposit	1,000	—	—	1,000
	$21,941	$ 2,582	$ (361)	$24,162

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The following tables show the gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position (in thousands):

	July 1, 2017					
	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Treasury and government debt securities	$349	$ (1)	$ —	$ —	$349	$ (1)
Residential mortgage-backed securities	3,292	(30)	2,320	(60)	5,612	(90)
State and political subdivision debt securities	1,688	(21)	2,077	(93)	3,765	(114)
Corporate debt securities	884	(9)	—	—	884	(9)
Marketable equity securities	794	(81)	94	(31)	888	(112)
	$7,007	$ (142)	$ 4,491	$ (184)	$11,498	$ (326)

	April 1, 2017					
	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Treasury and government debt securities	$349	$ (1)	$ —	$ —	$349	$ (1)
Residential mortgage-backed securities	3,449	(38)	1,962	(52)	5,411	(90)
State and political subdivision debt securities	1,948	(36)	2,084	(81)	4,032	(117)
Corporate debt securities	1,424	(23)	—	—	1,424	(23)
Marketable equity securities	1,393	(90)	157	(40)	1,550	(130)
	$8,563	$ (188)	$ 4,203	$ (173)	$12,766	$ (361)

Based on the Company's ability and intent to hold the investments for a reasonable period of time sufficient for a forecasted recovery of fair value, the Company does not consider any investments to be other-than-temporarily impaired at July 1, 2017.

As of July 1, 2017 and April 1, 2017, the Company's investments in marketable equity securities consist of investments in common stock of industrial and other companies.

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The amortized cost and fair value of the Company's investments in debt securities, by contractual maturity, are shown in the table below (in thousands). Expected maturities differ from contractual maturities as borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	July 1, 2017	
	Amortized Cost	Fair Value
Due in less than one year	$2,230	$2,215
Due after one year through five years	3,736	3,682
Due after five years through ten years	2,764	2,703
Due after ten years	6,072	6,163
	$14,802	$14,763

Realized gains and losses from the sale of securities are determined using the specific identification method. Gross gains realized on the sales of investment securities for the three months ended July 1, 2017 were approximately $165,000. Gross losses realized were approximately $61,000 for the three months ended July 1, 2017. Gross gains realized on the sales of investment securities for the three months ended July 2, 2016 were approximately $453,000. Gross losses realized were approximately $149,000 for the three months ended July 2, 2016.

4. Inventories

Inventories consist of the following (in thousands):

	July 1, 2017	April 1, 2017
Raw materials	$33,745	$31,506
Work in process	11,765	11,768
Finished goods and other	53,570	50,581
	$99,080	$93,855

5. Consumer Loans Receivable

The Company acquired consumer loans receivable during the first quarter of fiscal 2012 as part of the Palm Harbor transaction. Acquired consumer loans receivable held for investment were acquired at fair value and subsequently are accounted for in accordance with Accounting Standards Codification ("ASC") 310-30, Loans and Debt Securities Acquired with Deteriorated Credit Quality ("ASC 310-30"). Consumer loans receivable held for sale are carried at the lower of cost or market and construction advances are carried at the amount advanced less a valuation allowance. The following table summarizes consumer loans receivable (in thousands):

	July 1, 2017	April 1, 2017
Loans held for investment (acquired on Palm Harbor Acquisition Date)	$58,373	$60,513
Loans held for investment (originated after Palm Harbor Acquisition Date)	12,927	11,108
Loans held for sale	19,283	18,570
Construction advances	9,187	6,957
Consumer loans receivable	99,770	97,148
Deferred financing fees and other, net	(1,154)	(1,095)
Allowance for loan losses	(237)	(252)
Consumer loans receivable, net	$98,379	$95,801

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The allowance for loan losses is developed at a loan level and allocated to specific individual loans or to impaired loans. A range of probable losses is calculated after giving consideration to, among other things, the loan characteristics, and historical loss experience. The Company then makes a determination of the best estimate within the range of loan losses. The allowance for loan losses reflects the Company's judgment of the probable loss exposure on its loans held for investment portfolio.

As of the date of the Palm Harbor acquisition, management evaluated consumer loans receivable held for investment by CountryPlace to determine whether there was evidence of deterioration of credit quality and if it was probable that CountryPlace would be unable to collect all amounts due according to the loans' contractual terms. The Company also considered expected prepayments and estimated the amount and timing of undiscounted expected principal, interest and other cash flows. The Company determined the excess of the loan pool's scheduled contractual principal and contractual interest payments over all cash flows expected as of the date of the Palm Harbor transaction as an amount that includes interest that cannot be accreted into interest income (the non-accretable difference). The cash flow expected to be collected in excess of the carrying value of the acquired loans includes interest that is accreted into interest income over the remaining life of the loans (referred to as accretable yield). Interest income on consumer loans receivable is recognized as net revenue.

	July 1, 2017	April 1, 2017
	(in thousands)	
Consumer loans receivable held for investment – contractual amount	$136,927	$142,391
Purchase discount		
Accretable	(54,912)	(56,686)
Non-accretable	(23,437)	(25,032)
Less consumer loans receivable reclassified as other assets	(205)	(160)
Total acquired consumer loans receivable held for investment, net	$58,373	$60,513

Over the life of the acquired loans, the Company continues to estimate cash flows expected to be collected by CountryPlace. As of the balance sheet date, the Company evaluates whether the present value of expected cash flows, determined using the effective interest rate, has decreased from the value at acquisition and, if so, recognizes an allowance for loan loss. The present value of any subsequent increase in the loan pool's actual cash flows expected to be collected is used first to reverse any existing allowance for loan loss. Any remaining increase in cash flows expected to be collected adjusts the amount of accretable yield recognized on a prospective basis over the loan pool's remaining life. The weighted averages of assumptions used in the calculation of expected cash flows to be collected are as follows:

	July 1, 2017	April 1, 2017
Prepayment rate	13.9%	13.8 %
Default rate	1.0 %	1.1 %

Assuming there was a 1% unfavorable variation from the expected level, for each key assumption, the expected cash flows for the life of the portfolio, as of July 1, 2017, would decrease by approximately $1.8 million and $4.6 million for the expected prepayment rate and expected default rate, respectively.

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The changes in accretable yield on acquired consumer loans receivable held for investment were as follows (in thousands):

	Three Months Ended	
	July 1, 2017	July 2, 2016
Balance at the beginning of the period	$56,686	$69,053
Accretion	(2,210)	(2,515)
Reclassifications (to) from non-accretable discount	436	(254)
Balance at the end of the period	$54,912	$66,284

The consumer loans held for investment have the following characteristics:

	July 1, 2017	April 1, 2017
Weighted average contractual interest rate	8.82%	8.87 %
Weighted average effective interest rate	9.65%	9.35 %
Weighted average months to maturity	165	165

The Company's consumer loans receivable balance consists of fixed-rate, fixed-term and fully-amortizing single-family home loans. These loans are either secured by a manufactured home, excluding the land upon which the home is located (chattel personal property loans), or by a combination of the home and the land upon which the home is located (real property mortgage loans). The real property mortgage loans are primarily for manufactured homes. Combined land and home loans are further disaggregated by the type of loan documentation: those conforming to the requirements of Government-Sponsored Enterprises ("GSEs"), and those that are non-conforming. In most instances, CountryPlace's loans are secured by a first-lien position and are provided for the consumer purchase of a home. Unsecuritized consumer loans held for investment include chattel personal property loans originated under the Company's chattel lending programs. Accordingly, CountryPlace classifies its loans receivable as follows: chattel loans, conforming mortgages, non-conforming mortgages and other loans.

In measuring credit quality within each segment and class, CountryPlace uses commercially available credit scores (such as FICO®). At the time of each loan's origination, CountryPlace obtains credit scores from each of the three primary credit bureaus, if available. To evaluate credit quality of individual loans, CountryPlace uses the mid-point of the available credit scores or, if only two scores are available, the Company uses the lower of the two. CountryPlace does not update credit bureau scores after the time of origination.

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The following table disaggregates CountryPlace's gross consumer loans receivable for each class by portfolio segment and credit quality indicator as of the time of origination (in thousands):

	July 1, 2017					
	Consumer Loans Held for Investment					
	Securitized 2005	Securitized 2007	Unsecuritized	Construction Advances	Consumer Loans Held For Sale	Total
Asset Class						
Credit Quality Indicator (FICO® score)						
Chattel loans						
0-619	$621	$ 392	$ 382	$ —	$ —	$1,395
620-719	11,230	7,917	6,399	—	388	25,934
720+	12,230	7,386	5,931	—	4,143	29,690
Other	51	—	429	—	—	480
Subtotal	24,132	15,695	13,141	—	4,531	57,499
Conforming mortgages						
0-619	—	—	160	—	93	253
620-719	—	—	1,715	5,662	9,875	17,252
720+	—	—	246	3,525	4,784	8,555
Subtotal	—	—	2,121	9,187	14,752	26,060
Non-conforming mortgages						
0-619	85	429	1,305	—	—	1,819
620-719	1,225	4,775	3,292	—	—	9,292
720+	1,510	2,878	408	—	—	4,796
Other	—	—	297	—	—	297
Subtotal	2,820	8,082	5,302	—	—	16,204
Other loans						
Subtotal	—	—	7	—	—	7
	$26,952	$ 23,777	$ 20,571	$ 9,187	$ 19,283	$99,770

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	April 1, 2017					
	Consumer Loans Held for Investment					
	Securitized 2005	Securitized 2007	Unsecuritized	Construction Advances	Consumer Loans Held For Sale	Total
Asset Class						
Credit Quality Indicator (FICO® score)						
Chattel loans						
0-619	$705	$ 411	$ 393	$ —	$ —	$1,509
620-719	11,681	8,072	5,406	—	697	25,856
720+	12,748	7,800	5,081	—	3,097	28,726
Other	51	—	433	—	—	484
Subtotal	25,185	16,283	11,313	—	3,794	56,575
Conforming mortgages						
0-619	—	—	161	261	99	521
620-719	—	—	1,792	4,231	10,553	16,576
720+	—	—	247	2,465	4,124	6,836
Subtotal	—	—	2,200	6,957	14,776	23,933
Non-conforming mortgages						
0-619	86	435	1,327	—	—	1,848
620-719	1,242	4,947	3,372	—	—	9,561
720+	1,527	2,909	484	—	—	4,920
Other	—	—	299	—	—	299
Subtotal	2,855	8,291	5,482	—	—	16,628
Other loans						
Subtotal	—	—	12	—	—	12
	$28,040	$ 24,574	$ 19,007	$ 6,957	$ 18,570	$97,148

Loan contracts secured by collateral that is geographically concentrated could experience higher rates of delinquencies, default and foreclosure losses than loan contracts secured by collateral that is more geographically dispersed. Forty-seven percent of the outstanding principal balance of consumer loans receivable portfolio is concentrated in Texas and 11% is concentrated in Florida. Other than Texas and Florida, no other state had concentrations in excess of 10% of the principal balance of the consumer loans receivable as of July 1, 2017. Collateral for repossessed loans is acquired through foreclosure or similar proceedings and is recorded at the estimated fair value of the home, less the costs to sell. At repossession, the fair value of the collateral is computed based on the historical recovery rates of previously charged-off loans; the loan is charged off and the loss is charged to the allowance for loan losses. On a monthly basis, the fair value of the collateral is adjusted to the lower of the amount recorded at repossession or the estimated sales price less estimated costs to sell, based on current information. Repossessed homes totaled approximately $1.8 million and $1.2 million as of July 1, 2017 and April 1, 2017, respectively, and are included in prepaid and other assets in the consolidated balance sheet. Foreclosure or similar proceedings in progress totaled approximately $934,000 and $694,000 as of July 1, 2017 and April 1, 2017, respectively.

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6. Commercial Loans Receivable and Allowance for Loan Loss

The Company's commercial loans receivable balance consists of two classes: (i) direct financing arrangements for the home product needs of our independent retailers, communities and developers; and (ii) amounts loaned by the Company under participation financing programs.

Under the terms of the direct programs, the Company provides funds for the independent retailers, communities and developers' financed home purchases. The notes are secured by the homes as collateral and, in some instances, other security depending on the circumstances. The other terms of direct arrangements vary depending on the needs of the borrower and the opportunity for the Company.

Under the terms of the participation programs, the Company provides loans to independent floor plan lenders, representing a significant portion of the funds that such financiers then lend to retailers to finance their inventory purchases. The participation commercial loan receivables are unsecured general obligations of the independent floor plan lenders.

Commercial loans receivables, net, consist of the following by class of financing notes receivable (in thousands):

	July 1, 2017	April 1, 2017
Direct loans receivable	$25,352	$24,959
Participation loans receivable	1,160	1,084
Allowance for loan loss	(222)	(210)
	$26,290	$25,833

The commercial loans receivable balance has the following characteristics:

	July 1, 2017	April 1, 2017
Weighted average contractual interest rate	6.1 %	5.6 %
Weighted average months to maturity	6	6

The Company evaluates the potential for loss from its participation loan programs based on each independent lender's overall financial stability, as well as historical experience, and has determined that an applicable allowance for loan loss was not needed at either July 1, 2017 or April 1, 2017.

With respect to direct programs with communities and developers, borrower activity is monitored on a regular basis and contractual arrangements are in place to provide adequate loss mitigation in the event of a default. For direct programs with independent retailers, the risk of loss is spread over numerous borrowers. Borrower activity is monitored in conjunction with third-party service providers, where applicable, to estimate the potential for loss on the related notes receivable, considering potential exposures, including repossession costs, remarketing expenses, impairment of value and the risk of collateral loss. The Company has historically been able to resell repossessed unused homes, thereby mitigating loss experience. If a default occurs and collateral is lost, the Company is exposed to loss of the full value of the home loan. If the Company determines that it is probable that a borrower will default, a specific reserve is determined and recorded within the estimated allowance for loan loss. The Company recorded an allowance for loan loss of $222,000 and $135,000 at July 1, 2017 and July 2, 2016, respectively.

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The following table represents changes in the estimated allowance for loan losses, including related additions and deductions to the allowance for loan loss applicable to the direct programs (in thousands):

	Three Months Ended	
	July 1, 2017	July 2, 2016
Balance at beginning of period	$210	$ 128
Provision for inventory finance credit losses	12	7
Loans charged off, net of recoveries	—	—
Balance at end of period	$222	$ 135

The following table disaggregates commercial loans receivable and the estimated allowance for loan loss for each class of financing receivable by evaluation methodology (in thousands):

	Direct Commercial Loans		Participation Commercial Loans	
	July 1, 2017	April 1, 2017	July 1, 2017	April 1, 2017
Inventory finance notes receivable:				
Collectively evaluated for impairment	$14,901	$13,688	$ —	$ —
Individually evaluated for impairment	10,451	11,271	1,160	1,084
	$25,352	$24,959	$ 1,160	$ 1,084
Allowance for loan loss:				
Collectively evaluated for impairment	$(150)	$(137)	$ —	$ —
Individually evaluated for impairment	(72)	(73)	—	—
	$(222)	$(210)	$ —	$ —

Loans are subject to regular review and are given management's attention whenever a problem situation appears to be developing. Loans with indicators of potential performance problems are placed on watch list status and are subject to additional monitoring and scrutiny. Nonperforming status includes loans accounted for on a non-accrual basis and accruing loans with principal payments past due 90 days or more. The Company's policy is to place loans on nonaccrual status when interest is past due and remains unpaid 90 days or more or when there is a clear indication that the borrower has the inability or unwillingness to meet payments as they become due. The Company will resume accrual of interest once these factors have been remedied. At July 1, 2017, there are no commercial loans that are 90 days or more past due that are still accruing interest. Payments received on nonaccrual loans are recorded on a cash basis, first to interest and then to principal. At July 1, 2017, the Company was not aware of any potential problem loans that would have a material effect on the commercial receivables balance. Charge-offs occur when it becomes probable that outstanding amounts will not be recovered.

The following table disaggregates the Company's inventory finance receivables by class and credit quality indicator (in thousands):

	Direct Commercial Loans		Participation Commercial Loans	
	July 1, 2017	April 1, 2017	July 1, 2017	April 1, 2017
Risk profile based on payment activity:				
Performing	$25,279	$24,886	$ 1,160	$ 1,084
Watch list	—	—	—	—
Nonperforming	73	73	—	—
	$25,352	$24,959	$ 1,160	$ 1,084

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The Company has concentrations of commercial loans receivable related to factory-built homes located in the following states, measured as a percentage of commercial loans receivables principal balance outstanding:

	July 1, 2017	April 1, 2017
Arizona	17.8%	21.3 %
California	15.1%	11.0 %
Oregon	13.2%	15.7 %
Texas	12.5%	11.0 %
Indiana	10.3%	10.7 %

The risks created by these concentrations have been considered in the determination of the adequacy of the allowance for loan losses. The Company did not have concentrations in excess of 10% of the principal balance of the commercial loans receivables in any other states as of July 1, 2017 or April 1, 2017, respectively.

As of July 1, 2017, the Company had concentrations with one independent third-party that equaled 20% of the principal balance outstanding, all of which was secured. As of April 1, 2017, the Company had concentrations with one independent third-party that equaled 23% of the principal balance outstanding, all of which was secured.

7. Property, Plant and Equipment

Property, plant and equipment are carried at cost. Depreciation is calculated using the straight-line method over the estimated useful lives of each asset. Estimated useful lives for significant classes of assets are as follows: (i) buildings and improvements, 10 to 39 years, and (ii) machinery and equipment, 3 to 25 years. Repairs and maintenance charges are expensed as incurred. Property, plant and equipment consist of the following (in thousands):

	July 1, 2017	April 1, 2017
Property, plant and equipment, at cost:		
Land	$22,577	$22,897
Buildings and improvements	35,616	34,180
Machinery and equipment	21,846	21,618
	80,039	78,695
Accumulated depreciation	(22,452)	(21,731)
Property, plant and equipment, net	$57,587	$56,964

Included in the amounts above are certain assets under a capital lease. See Note 8 for additional information.

8. Capital Lease

On April 3, 2017, in connection with the purchase of Lexington Homes, the Company recorded capital leases covering the manufacturing facilities and land in Lexington, Mississippi. The following amounts were recorded for the leased assets as of July 1, 2017:

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	July 1, 2017
Land	$419
Buildings and improvements	706
	1,125
Accumulated amortization	(9)
Leased assets, net	$1,116

The future minimum payments under the leases as of July 1, 2017 are as follows (in thousands):

FY 2018	$701
FY 2019	73
FY 2020	459
FY 2021	—
FY 2022	—
Thereafter	—
Total remaining lease payments	1,233
Less: Amount representing interest	(71)
Present value of future minimum lease payments	$1,162

9. Goodwill and Other Intangibles

Intangible assets principally consist of goodwill, trademarks and trade names, state insurance licenses, customer relationships, and other, which includes technology, insurance policies and renewal rights and other. Goodwill, trademarks and trade names and state insurance licenses are indefinite-lived intangible assets and are evaluated for impairment annually and whenever events or circumstances indicate that more likely than not impairment has occurred. During the three months ended July 1, 2017 and July 2, 2016, no impairment expense was recorded. Finite-lived intangibles are amortized over their estimated useful lives on a straight-line basis and are reviewed for possible impairment whenever events or changes in circumstances indicate that carrying amounts may not be recoverable. The value of customer relationships is amortized over 4 to 15 years and other intangibles over 7 to 15 years.

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Goodwill and other intangibles consist of the following (in thousands):

	July 1, 2017			April 1, 2017		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Indefinite lived:						
Goodwill	$69,753	$ —	$69,753	$69,753	$ —	$69,753
Trademarks and trade names	7,200	—	7,200	7,000	—	7,000
State insurance licenses	1,100	—	1,100	1,100	—	1,100
Total indefinite-lived intangible assets	78,053	—	78,053	77,853	—	77,853
Finite lived:						
Customer relationships	7,100	(5,596)	1,504	7,100	(5,543)	1,557
Other	1,384	(812)	572	1,384	(773)	611
Total goodwill and other intangible assets	$86,537	$ (6,408)	$80,129	$86,337	$ (6,316)	$80,021

Amortization expense recognized on intangible assets was $92,000 in each of the three months ended July 1, 2017 and July 2, 2016.

10. Accrued Liabilities

Accrued liabilities consist of the following (in thousands):

	July 1, 2017	April 1, 2017
Salaries, wages and benefits	$17,633	$22,029
Unearned insurance premiums	17,476	17,488
Customer deposits	17,233	15,986
Estimated warranties	16,316	15,479
Accrued volume rebates	6,753	5,686
Company repurchase option on certain loans sold	5,470	5,858
Insurance loss reserves	4,913	5,239
Accrued insurance	4,056	4,113
Deferred margin	3,192	2,906
Accrued taxes	2,092	1,682
Reserve for repurchase commitments	1,779	1,749
Capital lease obligation	1,162	—
Other	13,151	11,574
	$111,226	$109,789

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11. Warranties

Homes are generally warranted against manufacturing defects for a period of one year commencing at the time of sale to the retail customer. Estimated costs relating to home warranties are recorded at the date of sale. The Company has recorded a liability for estimated future warranty costs relating to homes sold based upon management's assessment of historical experience factors, an estimate of the amount of homes in the distribution channel and current industry trends. Activity in the liability for estimated warranties was as follows (in thousands):

	Three Months Ended	
	July 1, 2017	July 2, 2016
Balance at beginning of period	$15,479	$13,371
Purchase accounting additions	838	—
Charged to costs and expenses	5,223	6,136
Payments and deductions	(5,224)	(5,789)
Balance at end of period	$16,316	$13,718

12. Debt Obligations

Debt obligations consist of amounts related to loans sold that did not qualify for loan sale accounting treatment. The following table summarizes debt obligations (in thousands):

	July 1, 2017	April 1, 2017
Acquired securitized financings (acquired as part of the Palm Harbor transaction)		
Securitized financing 2005-1	$ 22,816	$ 23,756
Securitized financing 2007-1	24,933	25,728
Other secured financings	4,913	4,987
Secured Term Loan	4,927	3,520
Total securitized financings and other, net	$ 57,589	$ 57,991

The Company acquired CountryPlace's securitized financings during the first quarter of fiscal year 2012 as a part of the Palm Harbor acquisition. Acquired securitized financings were recorded at fair value at the time of acquisition, which resulted in a discount, and subsequently are accounted for in a manner similar to ASC 310-30 to accrete the discount.

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The Company considers expected prepayments and estimates the amount and timing of undiscounted expected principal, interest and other cash flows for securitized consumer loans receivable held for investment to determine the expected cash flows on securitized financings and the contractual payments. The amount of contractual principal and contractual interest payments due on the securitized financings in excess of all cash flows expected as of the date of the Palm Harbor acquisition include interest that cannot be accreted into interest expense (the non-accretable difference). The remaining amount is accreted into interest expense over the remaining life of the obligation (referred to as accretable yield). The following table summarizes acquired securitized financings (in thousands):

	July 1, 2017	April 1, 2017
Securitized financings – contractual amount	$54,415	$57,120
Purchase discount		
Accretable	(6,666)	(7,636)
Non-accretable (1)	—	—
Total acquired securitized financings, net	$47,749	$49,484

(1) There is no non-accretable difference, as the contractual payments on acquired securitized financing are determined by the cash collections from the underlying loans.

Over the life of the loans, the Company continues to estimate cash flows expected to be paid on securitized financings. The Company evaluates at the balance sheet date whether the present value of its securitized financings, determined using the effective interest rate, has increased or decreased. The present value of any subsequent change in cash flows expected to be paid adjusts the amount of accretable yield recognized on a prospective basis over the securitized financing's remaining life.

The changes in accretable yield on securitized financings were as follows (in thousands):

	Three Months Ended	
	July 1, 2017	July 2, 2016
Balance at the beginning of the period	$7,636	$12,333
Accretion	(871)	(968)
Adjustment to cash flows	(99)	94
Balance at the end of the period	$6,666	$11,459

On July 12, 2005, prior to the Company's acquisition of Palm Harbor and CountryPlace, CountryPlace completed its initial securitization (2005-1) for approximately $141.0 million of loans, which was funded by issuing bonds totaling approximately $118.4 million. The bonds were issued in four different classes: Class A-1 totaling $36.3 million with a coupon rate of 4.23%; Class A-2 totaling $27.4 million with a coupon rate of 4.42%; Class A-3 totaling $27.3 million with a coupon rate of 4.80%; and Class A-4 totaling $27.4 million with a coupon rate of 5.20%. The bonds mature at varying dates and at issuance had an expected weighted average maturity of 4.66 years. For accounting purposes, this transaction was structured as a securitized borrowing. As of July 1, 2017, the Class A-1, Class A-2, and Class A-3 bonds have been retired.

On March 22, 2007, prior to the Company's acquisition of Palm Harbor and CountryPlace, CountryPlace completed its second securitization (2007-1) for approximately $116.5 million of loans, which was funded by issuing bonds totaling approximately $101.9 million. The bonds were issued in four classes: Class A-1 totaling $28.9 million with a coupon rate of 5.484%; Class A-2 totaling $23.4 million with a coupon rate of 5.232%; Class A-3 totaling $24.5 million with a coupon rate of 5.593%; and Class A-4 totaling $25.1 million with a coupon rate of 5.846%. The bonds mature at varying dates and at issuance had an expected weighted average maturity of 4.86 years. For accounting purposes, this transaction was also structured as a securitized borrowing. As of July 1, 2017, the Class A-1, Class A-2 and Class A-3 bonds have been retired.

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CountryPlace's securitized debt is subject to provisions that require certain levels of overcollateralization. Overcollateralization is equal to CountryPlace's equity in the bonds. Failure to satisfy these provisions could cause cash, which would normally be distributed to CountryPlace, to be used for repayment of the principal of the related Class A bonds until the required overcollateralization level is reached. During periods when the overcollateralization is below the specified level, cash collections from the securitized loans in excess of servicing fees payable to CountryPlace and amounts owed to the Class A bondholders, trustee and surety, are applied to reduce the Class A debt until such time the overcollateralization level reaches the specified level. Therefore, failure to meet the overcollateralization requirement could adversely affect the timing of cash flows received by CountryPlace. However, principal payments of the securitized debt, including accelerated amounts, is payable only from cash collections from the securitized loans and no additional sources of repayment are required or permitted. As of July 1, 2017, the 2005-1 and 2007-1 securitized portfolios were within the required overcollateralization level.

The Company has entered into agreements with independent third party banks for a total of $15.0 million secured credit facilities with one year drawn periods and maturity dates of ten years. The proceeds are used by the Company to originate and hold consumer chattel loans secured by manufactured homes, which are pledged as collateral to the facility. The maximum advance for loans under these programs is 80% of the outstanding collateral principal balance, with the Company providing the remaining funds. One of the facilities has a floating interest rate during a one year warehouse period in which the Company has the option to convert all or a portion of the loan to a fixed rate. During the warehouse period, the facility bears interest at an annual rate of the average one month LIBOR rates plus 3.50%. Upon conversion, converted balances bear interest at an annual rate of 10 year US Treasury bonds plus 2.75%. Payments are based on a 20 year amortization schedule with a balloon payment due upon maturity. The other facility has a fixed interest rate of 4.75% and a balloon payment due upon maturity.

13. Reinsurance

Standard Casualty is primarily a specialty writer of manufactured home physical damage insurance. Certain of Standard Casualty's premiums and benefits are assumed from and ceded to other insurance companies under various reinsurance agreements. The ceded reinsurance agreements provide Standard Casualty with increased capacity to write larger risks and maintain its exposure to loss within its capital resources. Standard Casualty remains obligated for amounts ceded in the event that the reinsurers do not meet their obligations. Substantially all of Standard Casualty's assumed reinsurance is with one entity.

The effects of reinsurance on premiums written and earned are as follows (in thousands):

	Three Months Ended			
	July 1, 2017		July 2, 2016	
	Written	Earned	Written	Earned
Direct premiums	$4,366	$4,150	$4,386	$3,926
Assumed premiums—nonaffiliate	6,260	6,267	6,947	5,632
Ceded premiums—nonaffiliate	(2,948)	(2,948)	(3,220)	(3,220)
Net premiums	$7,678	$7,469	$8,113	$6,338

Typical insurance policies written or assumed by Standard Casualty have a maximum coverage of $300,000 per claim, of which Standard cedes $200,000 of the risk of loss per reinsurance. Therefore, Standard Casualty maintains risk of loss limited to $100,000 per claim on typical policies. After this limit, amounts are recoverable by Standard Casualty through reinsurance for catastrophic losses in excess of $1.5 million per occurrence up to a maximum of $43.5 million in the aggregate.

Purchasing reinsurance contracts protects Standard Casualty from frequency and/or severity of losses incurred on insurance policies issued, such as in the case of a catastrophe that generates a large number of serious claims on multiple policies at the same time.

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14. Income Taxes

The Company's deferred tax assets primarily result from financial statement accruals not currently deductible for tax purposes and differences in the acquired basis of certain assets, and its deferred tax liabilities primarily result from tax amortization of goodwill and other intangible assets.

The Company complies with the provisions of ASC 740, Income Taxes ("ASC 740"), which clarifies the accounting for income taxes by prescribing a minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. ASC 740 also provides guidance on derecognizing, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition. The amount of unrecognized tax benefits recorded by the Company is insignificant and the impact on the effective tax rate if all unrecognized tax benefits were recognized would be insignificant. The Company classifies interest and penalties related to unrecognized tax benefits in tax expense.

Income tax returns are filed in the U.S. federal jurisdiction and in several state jurisdictions. The Company is no longer subject to examination by the IRS for years before fiscal year 2013. In general, the Company is no longer subject to state and local income tax examinations by tax authorities for years before fiscal year 2012. The Company believes that its income tax filing positions and deductions will be sustained on audit and does not anticipate any adjustments that will result in a material change to the Company's financial position. The total amount of unrecognized tax benefit related to any particular tax position is not anticipated to change significantly within the next 12 months. The provision for income taxes generally represents income taxes paid or payable for the current year plus the change in deferred taxes during the year.

15. Commitments and Contingencies

Repurchase Contingencies. The Company is contingently liable under terms of repurchase agreements with financial institutions providing inventory financing for independent retailers of its products. These arrangements, which are customary in the industry, provide for the repurchase of products sold to retailers in the event of default by the retailer. The risk of loss under these agreements is spread over numerous retailers. The price the Company is obligated to pay generally declines over the period of the agreement (generally 18 to 36 months, calculated from the date of sale to the retailer) and the risk of loss is further reduced by the resale value of the repurchased homes. The maximum amount for which the Company was contingently liable under such agreements approximated $48.2 million at July 1, 2017, without reduction for the resale value of the homes. The Company applies ASC 460, Guarantees ("ASC 460"), and ASC 450-20, Loss Contingencies ("ASC 450-20"), to account for its liability for repurchase commitments. Under the provisions of ASC 460, the Company records the greater of the estimated value of the non-contingent obligation or a contingent liability for each repurchase arrangement under the provisions of ASC 450-20. The Company recorded an estimated liability of $1.8 million and $1.7 million at July 1, 2017 and April 1, 2017, respectively, related to the commitments pertaining to these agreements.

Letters of Credit. To secure certain reinsurance contracts, Standard Casualty maintains an irrevocable letter of credit of $7.0 million to provide assurance that Standard Casualty will fulfill its reinsurance obligations. This letter of credit is secured by certain of the Company's investments.

Construction-Period Mortgages. CountryPlace funds construction-period mortgages through periodic advances during the period of home construction. At the time of initial funding, CountryPlace commits to fully fund the loan contract in accordance with a predetermined schedule. Subsequent advances are contingent upon the performance of contractual obligations by the seller of the home and the borrower. Cumulative advances on construction-period mortgages are carried in the consolidated balance sheet at the amount advanced less a valuation allowance, which are included in consumer loans receivable. The total loan contract amount, less cumulative advances, represents an off-balance sheet contingent commitment of CountryPlace to fund future advances.

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Loan contracts with off-balance sheet commitments are summarized below (in thousands):

	July 1, 2017	April 1, 2017
Construction loan contract amount	$24,546	$18,031
Cumulative advances	(9,187)	(6,957)
Remaining construction contingent commitment	$15,359	$11,074

Representations and Warranties of Mortgages Sold. CountryPlace sells loans to GSEs and whole-loan purchasers and finances certain loans with long-term credit facilities secured by the respective loans. In connection with these activities, CountryPlace provides to the GSEs, whole-loan purchasers and lenders, representations and warranties related to the loans sold or financed. These representations and warranties generally relate to the ownership of the loan, the validity of the lien securing the loan, the loan's compliance with the criteria for inclusion in the sale transactions, including compliance with underwriting standards or loan criteria established by the buyer, and CountryPlace's ability to deliver documentation in compliance with applicable laws. Generally, representations and warranties may be enforced at any time over the life of the loan. Upon a breach of a representation, CountryPlace may be required to repurchase the loan or to indemnify a party for incurred losses. Repurchase demands and claims for indemnification payments are reviewed on a loan-by-loan basis to validate if there has been a breach requiring repurchase. CountryPlace manages the risk of repurchase through underwriting and quality assurance practices and by servicing the mortgage loans to investor standards. CountryPlace maintains a reserve for these contingent repurchase and indemnification obligations. This reserve of $897,000 and $885,000 as of July 1, 2017 and April 1, 2017, respectively, included in accrued liabilities, reflects management's estimate of probable loss. CountryPlace considers a variety of assumptions, including borrower performance (both actual and estimated future defaults), historical repurchase demands and loan defect rates to estimate the liability for loan repurchases and indemnifications.

Interest Rate Lock Commitments. In originating loans for sale, CountryPlace issues interest rate lock commitments ("IRLCs") to prospective borrowers and third-party originators. These IRLCs represent an agreement to extend credit to a loan applicant, or an agreement to purchase a loan from a third-party originator, whereby the interest rate on the loan is set prior to loan closing or sale. These IRLCs bind CountryPlace to fund the approved loan at the specified rate regardless of whether interest rates or market prices for similar loans have changed between the commitment date and the closing date. As such, outstanding IRLCs are subject to interest rate risk and related loan sale price risk during the period from the date of the IRLC through the earlier of the loan sale date or IRLC expiration date. The loan commitments generally range between 30 and 180 days; however, borrowers are not obligated to close the related loans. As a result, CountryPlace is subject to fallout risk related to IRLCs, which is realized if approved borrowers choose not to close on the loans within the terms of the IRLCs unless the commitment is successfully paired with another loan that may mitigate losses from fallout.

As of July 1, 2017, CountryPlace had outstanding IRLCs with a notional amount of $14.7 million and are recorded at fair value in accordance with ASC 815, Derivatives and Hedging ("ASC 815"). ASC 815 clarifies that the expected net future cash flows related to the associated servicing of a loan should be included in the measurement of all written loan commitments that are accounted for at fair value through earnings. The estimated fair values of IRLCs are recorded in other assets in the consolidated balance sheets. The fair value of IRLCs is based on the value of the underlying mortgage loan adjusted for: (i) estimated cost to complete and originate the loan and (ii) the estimated percentage of IRLCs that will result in closed mortgage loans. The initial and subsequent changes in the value of IRLCs are a component of gain (loss) on mortgage loans held for sale. During the three months ended July 1, 2017 and July 2, 2016, CountryPlace recognized losses of $25,000 and gains of $28,000 on the outstanding IRLCs, respectively.

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Forward Sales Commitments. CountryPlace manages the risk profiles of a portion of its outstanding IRLCs and mortgage loans held for sale by entering into forward sales of mortgage-backed securities ("MBS") and whole loan sale commitments. As of July 1, 2017, CountryPlace had $36.5 million in outstanding notional forward sales of MBSs and forward sales commitments. Commitments to forward sales of whole loans are typically in an amount proportionate with the amount of IRLCs expected to close in particular time frames, assuming no change in mortgage interest rates, for the respective loan products intended for whole loan sale.

The estimated fair values of forward sales of MBS and forward sale commitments are based on quoted market values and are recorded within other current assets in the consolidated balance sheets. During the three months ended July 1, 2017 and July 2, 2016, CountryPlace recognized gains of $155,000 and losses of $44,000 on forward sales and whole loan sale commitments, respectively.

Legal Matters. The Company is party to certain legal proceedings that arise in the ordinary course and are incidental to its business. Certain of the claims pending against the Company in these proceedings allege, among other things, breach of contract and warranty, product liability and personal injury. Although litigation is inherently uncertain, based on past experience and the information currently available, management does not believe that the currently pending and threatened litigation or claims will have a material adverse effect on the Company's consolidated financial position, liquidity or results of operations. However, future events or circumstances currently unknown to management will determine whether the resolution of pending or threatened litigation or claims will ultimately have a material effect on the Company's consolidated financial position, liquidity or results of operations in any future reporting periods.

16. Stockholders' Equity

The following table represents changes in stockholders' equity for the three months ended July 1, 2017 (dollars in thousands):

	Common Stock		Additional paid-in capital	Retained earnings	Accumulated other comprehensive income	Total
	Shares	Amount				
Balance, April 1, 2017	8,994,968	$ 90	$244,791	$148,141	$ 1,386	$394,408
Cumulative effect of implementing ASU 2016-09	—	—	—	69	—	69
Stock option exercises, including incremental tax benefits	23,852	—	(1,780)		—	(1,780)
Share-based compensation	—	—	513	—	—	513
Net income	—	—	—	11,753	—	11,753
Unrealized loss on available-for-sale securities	—	—	—	—	(555)	(555)
Balance, July 1, 2017	9,018,820	$ 90	$243,524	$159,963	$ 831	$404,408

Other comprehensive income is comprised of unrealized gains and losses on available-for-sale investments.

(1) Unrealized losses before tax effect on available-for-sale securities were $909,000 for the three months ended July 1, 2017.

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17. Stock-Based Compensation

The Company maintains stock incentive plans whereby stock option grants or awards of restricted stock may be made to certain officers, directors and key employees. As of July 1, 2017, the plans, which are shareholder approved, permit the award of up to 1,650,000 shares of the Company's common stock, of which 374,850 shares were still available for grant. When options are exercised, new shares of the Company's common stock are issued. Stock options may not be granted below 100% of the fair market value of the Company's common stock at the date of grant and generally expire seven years from the date of grant. Stock options and awards of restricted stock typically vest over a one to five year period as determined by the plan administrator (the Compensation Committee of the Board of Directors, which consists of independent directors). The stock incentive plans provide for accelerated vesting of stock options upon a change in control (as defined in the plans).

Stock-based compensation cost charged against income for the three months ended July 1, 2017 and July 2, 2016 was $513,000 and $370,000, respectively.

As of July 1, 2017, total unrecognized compensation cost related to stock options was approximately $3.6 million and the related weighted-average period over which it is expected to be recognized is approximately 3.31 years.

The following table summarizes the option activity within the Company's stock-based compensation plans for the three months ended July 1, 2017:

	Number of Shares
Outstanding at April 1, 2017	464,930
Granted	4,000
Exercised	(56,500)
Canceled or expired	—
Outstanding at July 1, 2017	412,430
Exercisable at July 1, 2017	189,525

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18. Earnings Per Share

Basic earnings per common share is computed based on the weighted-average number of common shares outstanding during the reporting period. Diluted earnings per common share is computed based on the combination of dilutive common share equivalents, comprised of shares issuable under the Company's stock-based compensation plans and the weighted-average number of common shares outstanding during the reporting period. Dilutive common share equivalents include the dilutive effect of in-the-money options to purchase shares, which is calculated based on the average share price for each period using the treasury stock method. The following table sets forth the computation of basic and diluted earnings per share (dollars in thousands, except per share amounts):

	Three Months Ended	
	July 1, 2017	July 2, 2016
Net income	$11,753	$ 5,443
Weighted average shares outstanding:		
Basic	9,006,999	8,937,265
Common stock equivalents—treasury stock method	155,492	147,777
Diluted	9,162,491	9,085,042
Net income per share:		
Basic	$1.30	$ 0.61
Diluted	$1.28	$ 0.60

There were 10,973 and 2,147 anti-dilutive common stock equivalents excluded for the three months ended July 1, 2017 and July 2, 2016, respectively.

19. Fair Value Measurements

The book value and estimated fair value of the Company's financial instruments are as follows (in thousands):

	July 1, 2017		April 1, 2017	
	Book Value	Estimated Fair Value	Book Value	Estimated Fair Value
Available-for-sale securities (1)	$24,934	$24,934	$24,162	$24,162
Non-marketable equity investments (2)	17,892	17,892	17,383	17,383
Consumer loans receivable (3)	98,379	126,456	95,801	121,021
Interest rate lock commitment derivatives (4)	10	10	35	35
Forward loan sale commitment derivatives (4)	(69)	(69)	(86)	(86)
Commercial loans receivable (5)	26,290	26,388	25,833	25,841
Securitized financings and other (6)	(57,589)	(62,561)	(57,991)	(61,270)
Mortgage servicing rights (7)	1,285	1,285	1,110	1,110

(1) For Level 1 classified securities, the fair value is based on quoted market prices. The fair value of Level 2 securities is based on other inputs, as further described below.

(2) The fair value approximates book value based on the non-marketable nature of the investments.

Includes consumer loans receivable held for investment, held for sale and construction advances. The fair value of the loans held for investment is based on the discounted value of the remaining principal and interest cash flows.

(3) The fair value of the loans held for sale are estimated based on recent GSE mortgage-backed bond prices. The fair value of the construction advances approximates book value and the sales price of these loans is estimated based on construction completed.

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(4) The fair values are based on changes in GSE mortgage-backed bond prices and, additionally for IRLCs, pull through rates.
(5) The fair value is estimated using market interest rates of comparable loans.
(6) The fair value is estimated using recent public transactions of similar asset-backed securities.
(7) The fair value of the mortgage servicing rights is based on the present value of expected net cash flows related to servicing these loans.

In accordance with ASC 820, Fair Value Measurements and Disclosures ("ASC 820"), fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. ASC 820 also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

Level 1 – Quoted prices in active markets for identical assets or liabilities.

Level 2 – Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

The Company utilizes the market approach to measure fair value for its financial assets and liabilities. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities.

When the Company uses observable market prices for identical securities that are traded in less active markets, it classifies such securities as Level 2. When observable market prices for identical securities are not available, the Company prices its marketable debt instruments using non-binding market consensus prices that are corroborated with observable market data; quoted market prices for similar instruments; or pricing models, such as a discounted cash flow model, with all significant inputs derived from or corroborated with observable market data. Non-binding market consensus prices are based on the proprietary valuation models of pricing providers or brokers. These valuation models incorporate a number of inputs, including non-binding and binding broker quotes; observable market prices for identical or similar securities; and the internal assumptions of pricing providers or brokers that use observable market inputs and, to a lesser degree, unobservable market inputs.

Financial instruments measured at fair value on a recurring basis are summarized below (in thousands):

	July 1, 2017			
	Total	Level 1	Level 2	Level 3
Securities issued by the U.S Treasury and Government (1)	$349	$ —	$349	$ —
Mortgage-backed securities (1)	5,751	—	5,751	—
Securities issued by states and political subdivisions (1)	6,971	—	6,971	—
Corporate debt securities (1)	1,692	—	1,692	—
Marketable equity securities (1)	7,409	7,409	—	—
Interest rate lock commitment derivatives (2)	10	—	—	10
Forward loan sale commitment derivatives (2)	(69)	—	—	(69)
Mortgage servicing rights (3)	1,285	—	—	1,285

(1) Unrealized gains or losses on investments are recorded in accumulated other comprehensive income (loss) at each measurement date.

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(2) Gains or losses on derivatives are recognized in current period earnings through cost of sales.

(3) Changes in the fair value of mortgage servicing rights are recognized in the current period earnings through net revenue.

No transfers between Level 1, Level 2 or Level 3 occurred during the three months ended July 1, 2017. The Company's policy regarding the recording of transfers between levels is to record any such transfers at the end of the reporting period.

Financial instruments for which fair value is disclosed but not required to be recognized in the balance sheet on a recurring basis are summarized below (in thousands):

	July 1, 2017			
	Total	Level 1	Level 2	Level 3
Loans held for investment	$97,231	$ —	$ —	$97,231
Loans held for sale	20,038	—	—	20,038
Loans held—construction advances	9,187	—	—	9,187
Commercial loans receivable	26,388	—	—	26,388
Securitized financings and other	(62,561)	—	(62,561)	—
Non-marketable equity investments	17,892	—	—	17,892

No recent sales have been executed in an orderly market of manufactured home loan portfolios with comparable product features, credit characteristics or performance. Therefore, loans held for investment are measured using Level 3 inputs that are calculated using estimated discounted future cash flows from the evaluation of loan credit quality and performance history to determine expected prepayments and defaults on the portfolio, discounted with rates considered to reflect current market conditions. Loans held for sale are measured at the lower of cost or fair value using inputs that consist quoted market prices for mortgage-backed securities or investor purchase commitments for similar types of loan commitments on hand from investors. These loans are held for relatively short periods, typically no more than 45 days. As a result, changes in loan-specific credit risk are not a significant component of the change in fair value and changes are largely driven by changes in interest rates or investor yield requirements. The cost of loans held for sale is lower than the fair value as of July 1, 2017. As noted above, activity in the manufactured housing asset-backed securities market is infrequent with no reliable market price information. As such, to determine the fair value of securitized financings, management evaluates the credit quality and performance history of the underlying loan assets to estimate the expected prepayment of the debt and credit spreads, based on market activity for similar rated bonds from other asset classes with similar durations.

ASC 825, Financial Instruments ("ASC 825"), requires disclosure of fair value information about financial instruments, whether or not recognized in the balance sheet, for which it is practicable to estimate fair value. Fair value estimates are made as of a specific point in time based on the characteristics of the financial instruments and the relevant market information. Where available, quoted market prices are used. In other cases, fair values are based on estimates using other valuation techniques. These techniques involve uncertainties and are significantly affected by the assumptions used and the judgments made regarding risk characteristics of various financial instruments, discount rates, estimates of future cash flows, future expected loss experience and other factors. Changes in assumptions could significantly affect these estimates and the resulting fair values. Derived fair value estimates cannot be substantiated by comparison to independent markets and, in many cases, could not be realized in an immediate sale of the instrument. Also, because of differences in methodologies and assumptions used to estimate fair values, the Company's fair values should not be compared to those of other companies.

Under ASC 825, fair value estimates are based on existing financial instruments without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. Accordingly, the aggregate fair value amounts presented do not represent the underlying market value of the Company.

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The Company records impairment losses on long-lived assets held for sale when the fair value of such long-lived assets is below their carrying values. The Company records impairment charges on long-lived assets used in operations when events and circumstances indicate that long-lived assets might be impaired and the undiscounted cash flows estimated to be generated by those assets are less than their carrying amounts. No impairment charges were recorded during the three months ended July 1, 2017.

Mortgage Servicing. Mortgage Servicing Rights ("MSRs") are the rights to receive a portion of the interest coupon and fees collected from the mortgagors for performing specified mortgage servicing activities, which consist of collecting loan payments, remitting principal and interest payments to investors, managing escrow accounts, performing loss mitigation activities on behalf of investors and otherwise administering the loan servicing portfolio. MSRs are initially recorded at fair value. Changes in fair value subsequent to the initial capitalization are recorded in the Company's results of operations. The Company recognizes MSRs on all loans sold to investors that meet the requirements for sale accounting and for which servicing rights are retained.

The Company applies fair value accounting to MSRs, with all changes in fair value recorded to net revenue in accordance with ASC 860-50, Servicing Assets and Liabilities. The fair value of MSRs is based on the present value of the expected future cash flows related to servicing these loans. The revenue components of the cash flows are servicing fees, interest earned on custodial accounts and other ancillary income. The expense components include operating costs related to servicing the loans (including delinquency and foreclosure costs) and interest expenses on servicer advances that the Company believes are consistent with the assumptions major market participants use in valuing MSRs. The expected cash flows are primarily impacted by prepayment estimates, delinquencies and market discounts. Generally, the value of MSRs is expected to increase when interest rates rise and decrease when interest rates decline, due to the effect those changes in interest rates have on prepayment estimates. Other factors noted above as well as the overall market demand for MSRs may also affect the valuation.

	July 1, 2017		April 1, 2017	
Number of loans serviced with MSRs	4,110		4,041	
Weighted average servicing fee (basis points)	31.69		31.42	
Capitalized servicing multiple	83.91	%	74.79	%
Capitalized servicing rate (basis points)	26.59		23.5	
Serviced portfolio with MSRs (in thousands)	$483,153		$472,492	
Mortgage servicing rights (in thousands)	$1,285		$1,110	

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20. Business Segment Information

The Company operates principally in two segments: (1) factory-built housing, which includes wholesale and retail systems-built housing operations and (2) financial services, which includes manufactured housing consumer finance and insurance. The following table details net revenue and income before income taxes by segment (in thousands):

	Three Months Ended	
	July 1, 2017	July 2, 2016
Net revenue:		
Factory-built housing	$192,882	$172,486
Financial services	13,934	12,655
	$206,816	$185,141
Income before income taxes:		
Factory-built housing	$13,170	$10,738
Financial services	2,481	(2,308)
	$15,651	$8,430

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Introduction

The following should be read in conjunction with Cavco Industries, Inc. and its subsidiaries' (collectively, the "Company" or "Cavco") Consolidated Financial Statements and the related Notes that appear in Item 1 of this Report. References to "Note" or "Notes" pertain to the Notes to the Company's Consolidated Financial Statements.

Overview

Headquartered in Phoenix, Arizona, the Company designs and produces factory-built homes primarily distributed through a network of independent and Company-owned retailers. We are the second largest producer of manufactured homes in the United States, based on reported wholesale shipments, marketed under a variety of brand names, including Cavco Homes, Fleetwood Homes, Palm Harbor Homes, Fairmont Homes, Friendship Homes, Chariot Eagle and Lexington Homes. The Company is also a leading builder of park model RVs, vacation cabins and systems-built commercial structures, as well as modular homes built primarily under the Nationwide Homes brand. Cavco's mortgage subsidiary, CountryPlace Acceptance Corp. ("CountryPlace"), is an approved Federal National Mortgage Association ("FNMA" or "Fannie Mae") and Federal Home Loan Mortgage Corporation ("FHLMC" or "Freddie Mac") seller/servicer, and a Government National Mortgage Association ("GNMA" or "Ginnie Mae") mortgage-backed securities issuer that offers conforming mortgages, non-conforming mortgages and chattel loans to purchasers of factory-built and site-built homes. Our insurance subsidiary, Standard Casualty Co. ("Standard Casualty"), provides property and casualty insurance primarily to owners of manufactured homes.

Company Growth

From its inception in 1965, Cavco traditionally served affordable housing markets in the southwestern United States principally through manufactured home production. During the period from 1997 to 2000, Cavco was purchased by and became a wholly-owned subsidiary of Centex Corporation, which operated the Company until 2003, when Cavco became a stand-alone publicly-held Company traded on the NASDAQ Global Select Market under the ticker symbol CVCO.

Beginning in 2007, the overall housing industry experienced a multi-year decline, which included the manufactured housing industry. Since this downturn, Cavco strategically expanded its factory operations and related business initiatives primarily through the acquisition of industry competitor operations. This development has enabled the Company to effectively participate in the ensuing housing industry recovery.

In 2009, the Company acquired certain manufactured housing assets and liabilities of Fleetwood Enterprises, Inc. ("Fleetwood"). The assets purchased included seven operating production facilities as well as idle factories. During fiscal year 2011, the Company acquired certain manufactured housing assets and liabilities of Palm Harbor Homes, Inc., a Florida corporation. The assets purchased included five operating production facilities as well as idle factories, 49 operating retail locations, a manufactured housing finance company and a homeowners insurance company. These acquisitions expanded the Company’s presence across the United States.

On March 30, 2015, the Company purchased the business and operating assets of Chariot Eagle, a Florida-based manufacturer of park model RVs and manufactured homes. This transaction has grown the Company's offering of park model RV product lines and further strengthened our market position in the Southeastern United States.

On May 1, 2015, Cavco acquired certain assets and liabilities of Fairmont Homes. Fairmont Homes is a builder of manufactured and modular homes and park model RVs, with manufacturing plants in Indiana and Minnesota selling under the Fairmont Homes and Friendship Homes brands. This transaction provides additional home production capabilities and increased distribution into new markets in the Midwest, the western Great Plains states and several provinces in Canada.

On April 3, 2017, the Company purchased Lexington Homes, which operates one manufacturing facility in Lexington, Mississippi. This transaction was accounted for as a business combination and provides additional home production capabilities and increased distribution into new markets in the Southeast.

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The Company operates 20 homebuilding facilities located in Millersburg and Woodburn, Oregon; Nampa, Idaho; Riverside, California; Phoenix and Goodyear, Arizona; Austin, Fort Worth, Seguin and Waco, Texas; Montevideo, Minnesota; Nappanee, Indiana; Lafayette, Tennessee; Lexington, Mississippi; Martinsville and Rocky Mount, Virginia; Douglas, Georgia; and Ocala and Plant City, Florida. The majority of the homes produced are sold to and distributed by independently owned retailers located primarily throughout the United States and Canada. In addition, our homes are sold through 42 Company-owned U.S. retail locations.

We continually review our product offerings throughout the combined organization and strive to improve product designs, production methods and marketing strategies. The supportive market response to the past and recent acquisitions has been encouraging and we believe that these expansions provide positive long-term strategic benefits for the Company. We plan to focus on developing synergies among all operations, which continue to have significant organic growth potential.

Industry and Company Outlook

According to data reported by the Manufactured Housing Institute ("MHI"), industry home shipments continue to improve, increasing 18.2% for the first 5 months of calendar 2017 compared to the same period in the prior year. During calendar year 2016 our industry shipped approximately 81,000 HUD code manufactured homes, an increase of 14.1% over the approximately 71,000 homes shipped in 2015. Shipments were 64,000 in 2014, 60,000 in 2013 and 55,000 in calendar year 2012, among the lowest levels since industry shipment statistics began to be recorded in 1959. Annual home shipments from 2009 to 2016 were less than the annual home shipments for each of the 40 years from 1969 to 2008. While industry HUD code manufactured home shipments improved modestly these recent years, the manufactured housing industry continues to operate at relatively low levels compared to historical shipment statistics. We believe that employment rates and underemployment among potential home buyers who favor affordable housing as well as low consumer confidence levels are improving from low levels reported in recent years. "First-time" and "move-up" buyers of affordable homes are historically among the largest segments of new manufactured home purchasers. Included in this group are lower-income households that were particularly affected by an extended period of persistently low employment rates and underemployment. The process of repairing damaged credit among consumers and efforts to save for a home loan down-payment often require substantial time. Improving consumer confidence in the U.S. economy is evident among manufactured home buyers interested in our products for seasonal or retirement living that have been concerned about financial stability, and appear to be less hesitant to commit to a new home purchase. We believe sales of our products may continue to increase as employment and consumer confidence levels continue to recover.

The two largest manufactured housing consumer demographics, young adults and those who are 55+ years old, are both growing. The U.S. adult population is estimated to expand by approximately 11.7 million between 2017 and 2022. Young adults born from 1976 to 1995, sometimes referred to as Gen Y, represent a large segment of the population. Late-stage Gen Y is approximately 2 million people larger than the next age category born from 1966 to 1975, Gen X, and is considered to be in the peak home-buying years. Gen Y represents prime first-time home buyers who may be attracted by the affordability, diversity of style choices and location flexibility of factory-built homes. The age 55 and older category is reported to be the fastest growing segment of the U.S. population. This group is similarly interested in the value proposition; however, they are also motivated by the energy efficiency and low maintenance requirements of systems-built homes, and by the lifestyle offered by planned communities that are specifically designed for homeowners that fall into this age group.

The housing industry is subject to seasonal fluctuations based on new home buyer purchasing patterns. Further, Cavco’s Company-owned retail stores experience decreased home buyer traffic during holidays and popular vacation periods. Still, diversification among Cavco’s product lines and operations have served to partially offset the extent of seasonal fluctuations. Demand for our core single-family new home products typically peaks each spring and summer before declining in the winter, consistent with the overall housing industry. Demand patterns for park model and cabin RVs and homes used primarily for retirement seasonal living partially offset the general housing seasonality.

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Cavco's mortgage subsidiary experiences minimal seasonal fluctuation in its mortgage origination activities as a result of the time needed for loan application approval processes and subsequent home loan closing activities. The mortgage subsidiary realizes no seasonal impacts from its mortgage servicing operations. Revenue for the home insurance subsidiary is not substantially impacted by seasonality as it recognizes revenue from policy sales ratably over each policy's term year. However, the insurance subsidiary is subject to adverse effects from excessive policy claims that may occur during periods of inclement weather, including seasonal spring storms in Texas where most of its policies are underwritten.

Consumer financing for the retail purchase of manufactured homes needs to become generally more available before marked emergence from continued low home shipment levels can occur. Restrictive underwriting guidelines, irregular appraisal processes, higher interest rates compared to site-built homes, regulatory burdens, a limited number of institutions lending to manufactured home buyers and limited secondary market availability for manufactured home loans are significant constraints to industry growth. We are working directly with other industry participants to develop manufactured home consumer financing models to attract industry financiers interested in furthering or expanding lending opportunities in the industry. We continue to invest in community-based lending initiatives that provide home-only financing to new residents of certain manufactured home communities. CountryPlace has invested in and developed chattel lending programs to grow sales of homes through traditional distribution point as well. We believe that growing our participation in chattel lending may provide additional sales growth opportunities for our factory-built housing operation.

We are also working through industry trade associations to encourage favorable legislative and GSE action to address the mortgage financing needs of potential buyers of affordable homes. Federal law requires the GSEs to issue a regulation to implement the "Duty to Serve" requirements specified in the Federal Housing Enterprises Financial Safety and Soundness Act of 1992, as amended by the Housing and Economic Recovery Act of 2008. On May 8, 2017, FNMA and FHLMC released their Underserved Markets Plan that describes, with specificity, the actions they will take over a three-year period to fulfill the "Duty to Serve" obligation. The focus of each of the three-year plans is to establish steps to ensure chattel loans can be purchased in bulk prior to proceeding with a chattel loan pilot. Expansion of the secondary market for chattel lending through the GSEs could provide further demand for housing, as lending options would likely become more available to home buyers. Although some limited progress has been made in the area, meaningful positive impact in the form of increased home orders has yet to be realized. See "Regulatory Developments" below.

While sales activity of existing homes has improved, the current lending environment that favors site-built housing and more affluent home buyers has not provided improved capabilities for affordable-home buyers to facilitate a new home purchase.

Based on the relatively low cost associated with manufactured home ownership, our products have traditionally competed with rental housing's monthly payment affordability. Rental housing activity is reported to have continued to increase in recent years. As a result, tenant housing vacancy rates appear to have declined, causing a corresponding rise in associated rental rates. These rental market factors may cause some renters to become interested buyers of affordable housing alternatives including manufactured homes.

Further, with respect to the general rise in demand for rental housing, we have realized a larger proportion of orders from developers and community owners for new manufactured homes intended for use as rental housing. The Company is responsive to the unique product and related requirements of these home buyers and values the opportunity to provide homes that are well suited for these purposes.

The backlog of sales orders at July 1, 2017 varied among our 20 factories and in total was approximately $137 million compared to $55 million at July 2, 2016. Retailers may cancel orders prior to production without penalty. Accordingly, until the production of a particular home has commenced, we do not consider our backlog to be firm orders.

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The Company participates in certain commercial loan programs with members of the Company's independent wholesale distribution chain. Under these programs, the Company provides a significant amount of the funds that independent financiers then lend to distributors to finance retail inventories of our products. In addition, the Company has entered into direct commercial loan arrangements with distributors, communities and developers under which the Company provides funds for financing homes (see Note 6 to the Consolidated Financial Statements). The Company's involvement in commercial loans has increased the availability of manufactured home financing to distributors and users of our products. We believe that our participation in wholesale financing is helpful to retailers, communities and developers and allows our homes additional opportunities for exposure to potential home buyers. These initiatives support the Company's ongoing efforts to expand our distribution base in all of our markets with existing and new customers. However, the initiatives expose the Company to risks associated with the creditworthiness of certain customers and business partners, including independent retailers, developers, communities and inventory financing partners.

With manufacturing facilities strategically positioned across the United States, we utilize local market research to design homes to meet the demands of our customers. We have the ability to customize floor plans and designs to fulfill specific needs and interests. By offering a full range of homes from entry-level models to large custom homes with the ability to engineer designs in-house, we can accommodate virtually any customer request. In addition to homes built to the federal HUD code, we construct modular homes that conform to state and local codes, park models and cabins and light commercial buildings at many of our manufacturing facilities.

We employ a concerted effort to identify niche market opportunities where our diverse product lines and custom building capabilities provide us with a competitive advantage. Our green building initiatives involve the creation of an energy efficient envelope and higher utilization of renewable materials. These homes provide environmentally-friendly maintenance requirements, typically lower utility costs, specially designed ventilation systems and sustainability. Cavco also builds homes designed to use alternative energy sources, such as solar and wind. Building green may significantly reduce greenhouse gas emissions without sacrificing features, style or comfort. From bamboo flooring and tankless water heaters to solar-powered homes, our products are diverse and tailored to a wide range of consumer interests. Innovation in housing design is a forte of the Company and we continue to introduce new models at competitive price points with expressive interiors and exteriors that complement home styles in the areas in which they are located.

We maintain a conservative cost structure in an effort to build added value into our homes. We have placed a consistent focus on developing synergies among all operations. In addition, the Company has worked diligently to maintain a solid financial position. Our balance sheet strength and position in cash and cash equivalents should help avoid liquidity problems and enable us to act effectively as market opportunities present themselves.

In 2008, we announced a stock repurchase program, under which a total of $10.0 million may be used to repurchase our outstanding common stock. The repurchases may be made in the open market or in privately negotiated transactions in compliance with applicable state and federal securities laws and other legal requirements. The level of repurchase activity is subject to market conditions and other investment opportunities. The plan does not obligate us to acquire any particular amount of common stock and may be suspended or discontinued at any time. The repurchase program will be funded using our available cash. No repurchases have been made under this program to date.

Regulatory Developments

In 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act" or the "Act") was passed into law. The Dodd-Frank Act is a sweeping piece of legislation and the financial services industry continues to assess its implications and implement necessary changes in procedures and business practices. The Act established the Consumer Financial Protection Bureau ("CFPB") to regulate consumer financial products and services. Although many rules have been implemented, the full impact will not be known for years as revisions and the development of additional rules continue, and Congress and the new President consider amending part of the Act. Enforcement actions are in the early stages and the effects of possible litigation related to the regulations remains unknown.

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In 2014, certain CFPB mortgage finance rules required under the Dodd-Frank Act became effective. The rules apply to consumer credit transactions secured by a dwelling, which include real property mortgages and chattel loans (financed without land) secured by manufactured homes. The rules defined standards for origination of "Qualified Mortgages," established specific requirements for lenders to prove borrowers' ability to repay loans, and outlined the conditions under which Qualified Mortgages are subject to safe harbor limitations on liability to borrowers. The rules also established interest rates and other cost parameters for determining which Qualified Mortgages fall under safe harbor protection. Among other issues, Qualified Mortgages with interest rates and other costs outside the limits are deemed "rebuttable" by borrowers and expose the lender and its assignees (including investors in loans, pools of loans and instruments secured by loans or loan pools) to possible litigation and penalties.

While many manufactured homes are currently financed with agency-conforming mortgages in which the ability to repay is verified, and interest rates and other costs are within the safe harbor limits established under the CFPB, mortgage finance rules, certain loans to finance the purchase of manufactured homes, especially chattel loans and non-conforming land-home loans, may fall outside the safe harbor limits. The rules have caused some lenders to curtail underwriting such loans, and some investors are reluctant to own or participate in owning such loans because of the uncertainty of potential litigation and other costs. As a result, some prospective buyers of manufactured homes may be unable to secure the financing necessary to complete purchases. In addition, compliance with the law and ongoing rule implementation has caused lenders to incur additional costs to implement new processes, procedures, controls and infrastructure required to comply with the regulations. Compliance may constrain lenders' ability to profitably price certain loans. Failure to comply with these regulations, changes in these or other regulations, or the imposition of additional regulations, could affect our earnings, limit our access to capital and have a material adverse effect on our business and results of operations.

The CFPB rules amending the Truth in Lending Act ("TILA") and the Real Estate Settlement Procedures Act ("RESPA") expand the types of mortgage loans that are subject to the protections of the Home Ownership and Equity Protections Act of 1994 ("HOEPA"), revise and expand the tests for coverage under HOEPA, and impose additional restrictions on mortgages that are covered by HOEPA. As a result, certain manufactured home loans are now subject to HOEPA limits on interest rates and fees. Loans with rates or fees in excess of the limits are deemed High Cost Mortgages and provide additional protections for borrowers, including with respect to determining the value of the home. Most loans for the purchase of manufactured homes have been written at rates and fees that would not appear to be considered High Cost Mortgages under the new rule. Although some lenders may continue to offer loans that are now deemed High Cost Mortgages, the rate and fee limits appear to have deterred some lenders from offering loans to certain borrowers and may continue to make them reluctant to enter into loans subject to the provisions of HOEPA. As a result, some prospective buyers of manufactured homes may be unable to secure financing necessary to complete manufactured home purchases.

The Dodd-Frank Act amended provisions of TILA to require rules for appraisals on principal residences securing higher-priced mortgage loans ("HPML"). Certain loans secured by manufactured homes, primarily chattel loans, could be considered HPMLs. Among other things, the rule requires creditors to provide copies of appraisal reports to borrowers prior to loan closing. To implement these amendments, the CFPB adopted the HPML Appraisal Rule effective December 30, 2014 and loans secured by new manufactured homes were exempt from the rule until July 18, 2015. While effects of these requirements are not fully known, some prospective home buyers may be deterred from completing a manufactured home purchase as a result of appraised values.

The Dodd-Frank Act also required integrating disclosures provided by lenders to borrowers under TILA and RESPA. The final rule became effective October 3, 2015. The TILA-RESPA Integrated Disclosure ("TRID") mandated extensive changes to the mortgage loan closing process and necessitated significant changes to mortgage origination systems. Since its implementation, technical ambiguities in the rule have resulted in lender and investor uncertainty regarding acceptable cures and tolerances for disclosure and estimate errors. It is not yet fully known how the GSEs and HUD will view TRID compliance, how they will apply their own interpretations of TRID to their repurchase and claims review processes, or how the market for private-label securitizations may be impacted.

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Regulation C of the Home Mortgage Disclosure Act ("HMDA") enacted in 1975 requires certain financial institutions, including non-depository institutions, to collect, record, report and disclose information about their mortgage lending activity. The data-related requirements in the HMDA and Regulation C are used to identify potential discriminatory lending patterns and enforce anti-discrimination statutes. The Dodd-Frank Act transferred rulemaking authority for HMDA to the CFPB, effective in 2011. It also amended the HMDA to require financial institutions to report additional data points and to collect, record and report additional information. The CFPB issued a final rule amending Regulation C, which becomes effective on January 1, 2018. Regulation C generally applies to consumer-purpose, closed-end loans and open-end lines of credit that are secured by a dwelling. Non-depository financial institutions are subject to Regulation C if they originate at least 25 covered closed-end mortgage loans or at least 100 covered open-end lines of credit in each of the two preceding calendar years. Violations of Regulation C, including incomplete, inaccurate, or omitted data are subject to administrative sanctions, including civil money penalties and compliance can be enforced by the Federal Reserve Board, Federal Deposit Insurance Corporation, the Office of the Comptroller of Currency, the National Credit Union Administration, HUD, or the CFPB.

New Federal Housing Administration ("FHA") Title I program guidelines became effective on June 1, 2010 and provide Ginnie Mae the ability to securitize manufactured home FHA Title I loans. These guidelines were intended to allow lenders to obtain new capital, which can then be used to fund new loans for our customers. Chattel loans have languished for several years and these changes were meant to broaden chattel financing availability for prospective homeowners. However, we are aware of only a small number of loans currently being securitized under the Ginnie Mae program.

The Secure and Fair Enforcement for Mortgage Licensing Act of 2008 ("SAFE Act") established requirements for the licensing and registration of all individuals that are Mortgage Loan Originators ("MLOs"). MLOs must be registered or licensed by the states. Traditionally, manufactured housing retailers have assisted home buyers with securing financing for the purchase of homes. This assistance may have included assisting with loan applications and presenting terms of loans. Under the SAFE Act, these activities are prohibited unless performed by a registered or licensed MLO. Although the definition of an MLO contains exemptions for administrative and other specific functions and industries, manufactured housing retailers are no longer able to negotiate rates and terms for loans unless they are licensed as MLOs. Compliance may require manufactured housing retailers to become licensed lenders and employ MLOs, or alter business practices related to assisting home buyers in securing financing. This may result in increased costs for retailers who elect to employ MLOs, penalties assessed against or litigation costs incurred by retailers found to be in violation, reduced home sales from home buyers' inability to secure financing without retailer assistance, or increased costs to home buyers or reduced transaction profitability for retailers as a result of the additional cost of mandatory MLO involvement.

The Housing and Economic Recovery Act of 2008 requires the GSEs to facilitate a secondary market for mortgages on housing for very low, low and moderate-income families in under-served markets, including manufactured housing. On January 30, 2017, the Federal Housing Finance Agency issued a final rule specifying the scope of GSE activities that are eligible to receive credit for compliance with the "Duty to Serve" rule after January 2018. On May 8, 2017, both GSEs released their Underserved Markets Plan, which included steps to ensure chattel loans can be purchased in bulk prior to proceeding with a chattel loan pilot. Both GSEs have expressed interest in pursuing such pilot programs for manufactured housing, however, it is uncertain whether either GSE will conduct a pilot program or launch a chattel loan program.

If passed by Congress and signed into law, the proposed Preserving Access to Manufactured Housing Act of 2017 (House of Representatives Bill 1699) would amend some Dodd-Frank Act provisions that affect manufactured housing financing. In addition to standalone legislation, on July 13, 2017, the House Appropriations Committee passed the language of the bill as a part of its Fiscal Year 2018 Financial Services Appropriations bill. Additionally, on June 8, 2017, the U.S. House of Representatives passed the Financial CHOICE Act (House of Representatives Bill 10), which included the legislative language of House of Representatives Bill 1699. On August 3, 2017, the U.S. Senate introduced Senate Bill 1751, companion legislation to House of Representatives Bill 1699. These bills would revise the triggers by which small-sized manufactured home loans are considered “High-Cost” under HOEPA and clarify the MLO licensing requirements for manufactured home retailers and their employees.

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Our sale of insurance products is subject to various state insurance laws and regulations which govern allowable charges and other insurance practices. Standard Casualty's insurance operations are regulated by the state insurance boards where it underwrites its policies. Underwriting, premiums, investments and capital reserves (including dividend payments to stockholders) are subject to the rules and regulations of these state agencies.

In 2010, the Patient Protection and Affordable Care Act, as amended by the Health Care and Education Reconciliation Act ("Health Reform Law"), was passed into law. As enacted, the Health Reform Law reforms, among other things, certain aspects of health insurance. The Health Reform Law could continue to increase our healthcare costs, adversely impacting the Company's earnings. On March 6, 2017, the American Health Care Act of 2017 (House of Representatives Bill 1628) passed the vote of the House of Representatives, which would repeal and replace the Health Reform Law. However, that bill and subsequent reform bills have not passed the Senate. It is uncertain how future legislation would impact our operations.

Governmental authorities have the power to enforce compliance with their regulations, and violations may result in the payment of fines, the entry of injunctions or both. Although we believe that our operations are in substantial compliance with the requirements of all applicable laws and regulations, these requirements have generally become more strict in recent years. Accordingly, we are unable to predict the ultimate cost of compliance with all applicable laws and enforcement policies.

Results of Operations

Three Months Ended July 1, 2017 compared to July 2, 2016

Net Revenue. The following tables summarize net revenue for the three months ended July 1, 2017 and July 2, 2016.

	Three Months Ended			
	July 1, 2017	July 2, 2016	$ Change	% Change
	(Dollars in thousands)			
Net revenue:				
Factory-built housing	$192,882	$172,486	$20,396	11.8 %
Financial services	13,934	12,655	1,279	10.1 %
	$206,816	$185,141	$21,675	11.7 %
Total homes sold	3,475	3,395	80	2.4 %
Net factory-built housing revenue per home sold	$55,506	$50,806	$4,700	9.3 %

The increase in net revenue from the factory-built housing segment for the three months ended July 1, 2017 compared to the same periods last year was driven primarily by improved home sales volume and a larger proportion of higher priced homes sold.

Net factory-built housing revenue per home sold is a volatile metric dependent upon several factors. A primary factor is the price disparity between sales of homes to independent retailers, builders, communities and developers ("Wholesale") and sales of homes to consumers by Company-owned retail centers ("Retail"). Wholesale sales prices are primarily comprised of the home and the cost to ship the home from a homebuilding facility to the home-site. Retail home prices include these items and retail markup, as well as items that are largely subject to home buyer discretion, including, but not limited to, installation, utilities, site improvements, landscaping and additional services. Changes to the proportion of home sales among these distribution channels between reporting periods impacts the overall net revenue per home sold. For the three months ended July 1, 2017, the Company sold 2,860 homes Wholesale and 615 Retail versus 2,761 homes Wholesale and 634 homes Retail in the comparable prior year period. Further, fluctuations in net factory-built housing revenue per home sold are the result of changes in product mix, which results from home buyer tastes and preferences as they select home types/models, as well as optional home upgrades when purchasing the home. These selections vary regularly based on consumer interests,

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local housing preferences and economic circumstances. Our product prices are also periodically adjusted for the cost and availability of raw materials included in and labor used to produce each home. For these reasons, we have experienced, and expect to continue to experience, volatility in overall net factory-built housing revenue per home sold.

Financial services segment revenue increased, resulting from 2.9% more insurance policies in force in the current year compared to the prior year as well as an increase of 13.4% in home loan sales volume year over year. Financial services segment revenue is partially offset by lower interest income earned on securitized loan portfolios that continue to amortize.

Gross Profit. The following tables summarize gross profit for the three months ended July 1, 2017 and July 2, 2016.

	Three months ended			
	July 1, 2017	July 2, 2016	$ Change	% Change
	(Dollars in thousands)			
Gross profit:				
Factory-built housing	$34,500	$30,659	$ 3,841	12.5 %
Financial services	7,466	2,593	4,873	187.9 %
	$41,966	$33,252	$ 8,714	26.2 %
Gross profit as % of Net revenue:	20.3 %	18.0 %	N/A	2.3 %

Factory-built housing gross profit for the three months ended July 1, 2017 was up consistent with improved home sales revenue.

Financial services gross profit for the three months ended July 1, 2017 increased as a result of fewer weather-related insurance claims and higher home loan sales volume, offset by lower interest income earned on securitized loan portfolios that continue to amortize. While claims activity typically spikes in April and May each year, a prime season for storm activity in our largest policy state of Texas, the severity of hail, wind and flood damage to insured homes was considerably greater in the first quarter of fiscal year 2017 than during the current period. Those losses from these events were somewhat mitigated by reinsurance contracts.

As a percentage of net revenue, gross profits increased modestly from overall increased construction leverage.

Selling, General and Administrative Expenses. The following tables summarize selling, general and administrative expenses for the three months ended July 1, 2017 and July 2, 2016.

	Three months ended			
	July 1, 2017	July 2, 2016	$ Change	% Change
	(Dollars in thousands)			
Selling, general and administrative expenses:				
Factory-built housing	$22,297	$20,875	$ 1,422	6.8 %
Financial services	4,008	3,812	196	5.1 %
	$26,305	$24,687	$ 1,618	6.6 %
Selling, general and administrative expenses as % of Net revenue:	12.7 %	13.3 %	N/A	(0.6)%

Selling, general and administrative expenses related to factory-built housing increased for the three months ended July 1, 2017 primarily from higher salary and incentive compensation expense from larger home sales and earnings overall.

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Selling, general and administrative expenses for financial services increased primarily from higher compensation expense.

As a percentage of net revenue, selling, general and administrative expenses decreased modestly from fixed cost efficiencies gained from higher revenue.

Interest Expense. The following tables summarize interest expense for the three months ended July 1, 2017 and July 2, 2016.

	Three months ended July 1, 2017	July 2, 2016	$ Change	% Change
	(Dollars in thousands)			
Interest expense	$1,048	$1,161	$(113)	(9.7)%

Interest expense consists primarily of debt service on the CountyPlace securitized financings of manufactured home loans and interest related to the capital lease treatment for leases of manufacturing facilities and land entered into as part of the Lexington and Fairmont acquisitions. On September 20, 2016, the Company purchased the assets under the capital lease for Fairmont, terminating the lease agreement; however, it was still in place in the first quarter of fiscal year 2017. The decrease for the three months ended July 1, 2017 compared to the same period in the prior year is attributable to lower interest expense on securitized portfolios that continue to amortize.

Other Income, net. The following tables summarize other income, net for the three months ended July 1, 2017 and July 2, 2016.

	Three Months Ended July 1, 2017	July 2, 2016	$ Change	% Change
	(Dollars in thousands)			
Other income, net	$1,038	$1,026	$ 12	1.2 %

Other income, net, is attributable to interest income earned on commercial loans receivable in the factory-built housing segment and also represents gains and losses on corporate investments and property, plant and equipment.

Income Before Income Taxes. The following tables summarize income before income taxes for the three months ended July 1, 2017 and July 2, 2016.

	Three Months Ended July 1, 2017	July 2, 2016	$ Change	% Change
	(Dollars in thousands)			
Income before income taxes:				
Factory-built housing	$13,170	$10,738	$2,432	22.6 %
Financial services	2,481	(2,308)	4,789	(207.5)%
	$15,651	$8,430	$7,221	85.7 %

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Income taxes. The following tables summarize Income taxes for the three months ended July 1, 2017 and July 2, 2016.

	Three Months Ended July 1, 2017	July 2, 2016	$ Change	% Change
	(Dollars in thousands)			
Income taxes	$3,898	$2,987	$ 911	30.5 %

The effective income tax rate for the first fiscal quarter was 24.9% compared to an effective tax rate of 35.4% for the same period last year. The current quarter contains a benefit of $1.4 million related to the Company's required implementation of Accounting Standards Update No. 2016-09, Compensation-Stock Compensation (Topic 718): Improvement to Employee Share-based Payment Accounting, which, among other items, requires us to record excess tax benefits on exercises of stock options as a reduction of income tax expense in the consolidated statement of comprehensive income, whereas they were previously recognized in equity.

Liquidity and Capital Resources

We believe that cash and cash equivalents at July 1, 2017, together with cash flow from operations, will be sufficient to fund our operations and provide for growth for the next 12 months and into the foreseeable future. We maintain cash in various deposit accounts, the balances of which are in excess of federally insured limits. We expect to continue to evaluate potential acquisitions of, or strategic investments in, businesses that are complementary to our Company. Such transactions may require the use of cash and have other impacts on the Company's liquidity and capital resources in the event of such a transaction. Because of the Company’s sufficient cash position, the Company has not sought external sources of liquidity, with the exception of certain credit facilities for our chattel lending programs. However, depending on our operating results and strategic opportunities, we may need to seek additional or alternative sources of financing. There can be no assurance that such financing would be available on satisfactory terms, if at all. If this financing were not available, it could be necessary for us to reevaluate our long-term operating plans to make more efficient use of our existing capital resources. The exact nature of any changes to our plans that would be considered depends on various factors, such as conditions in the factory-built housing industry and general economic conditions outside of our control.

Projected cash provided by operations in the coming year is largely dependent on sales volume and other activities. Operating activities used $47,000 of cash during the three months ended July 1, 2017, compared to providing cash of $8.2 million during the same period last year. Cash used in operating activities during the current period was primarily from loan origination activity in excess of proceeds from the sale of loans and expansion of chattel lending programs, along with increased accounts receivable resulting from higher home sales, greater inventory levels and lower accrued liabilities, including salaries and benefit accruals. This was offset by cash generated by net income before non-cash charges and principal payments received on consumer loans receivable in the ordinary course of business. Cash provided by operating activities during the prior period was primarily the result of cash generated by net income before non-cash charges along with higher accounts payable and accrued liabilities, including insurance loss reserves and customer deposits.

Consumer loans receivable originated increased to $34.4 million from $25.6 million for the three months ended July 1, 2017 and July 2, 2016, respectively. Proceeds from sales of consumer loans provided $29.3 million in cash, compared to $25.8 million in the previous year, a net increase of $3.5 million, which relates to the timing of loan sales.

With respect to consumer lending for the purchase of manufactured housing, states may classify manufactured homes for both legal and tax purposes as personal property rather than real estate. As a result, financing for the purchase of manufactured homes is characterized by shorter loan maturities and higher interest rates. Unfavorable changes in these factors and the current adverse trend in the availability and terms of financing in the industry may have material negative effects on our results of operations and financial condition. See Item IA, "Risk Factors."

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Cavco has entered into programs to provide some of the capital used by inventory lenders to finance wholesale home purchases by retailers. The Company has also entered into direct commercial loan arrangements with distributors, communities and developers under which the Company provides funds for financing homes and has invested in community-based lending initiatives that provide home-only financing to new residents of certain manufactured home communities (see Note 6 to the Consolidated Financial Statements). In addition, the Company has invested in and developed chattel lending programs to grow sales of homes through traditional distribution point as well.

Investing activities used $0.6 million of cash during the three months ended July 1, 2017, compared to $1.2 million during the same period last year. In the current year, cash was used for the purchase of Lexington Homes and other property, plant and equipment as well as investments, offset by investment sales. In the prior period, cash was used for the purchases of property, plant and equipment as well as investments by our insurance subsidiary for its investment portfolio, offset by that subsidiary's investment sales.

Financing activities used $2.4 million in cash during the three months ended July 1, 2017 primarily from payment on securitized financings and payments on stock option exercises, offset by loans accounted for as other secured financings. Financing activities used $2.3 million in cash during the three months ended July 2, 2016, largely from cash used to repay securitized financings, offset by loan sales accounted for as other secured financings and cash from stock option exercises.

CountryPlace's securitized debt is subject to provisions that require certain levels of overcollateralization. Overcollateralization is equal to CountryPlace's equity in the bonds. Failure to satisfy these provisions could cause cash, which would normally be distributed to CountryPlace, to be used for repayment of the principal of the related Class A bonds until the required overcollateralization level is reached. During periods when the overcollateralization is below the specified level, cash collections from the securitized loans in excess of servicing fees payable to CountryPlace and amounts owed to the Class A bondholders, trustee and surety, are applied to reduce the Class A debt until such time the overcollateralization level reaches the specified level. Therefore, failure to meet the overcollateralization requirement could adversely affect the timing of cash flows received by CountryPlace. However, principal payments of the securitized debt, including accelerated amounts, is payable only from cash collections from the securitized loans and no additional sources of repayment are required or permitted. As of July 1, 2017, the 2005-1 and 2007-1 securitized portfolios were within the required overcollateralization level.

Critical Accounting Policies

In Part II, Item 7 of our Form 10-K, under the heading "Critical Accounting Policies," we have provided a discussion of the critical accounting policies that management believes affect its more significant judgments and estimates used in the preparation of our Consolidated Financial Statements.

Recent Accounting Pronouncements

In November 2015, the FASB issued ASU 2015-17, Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes ("ASU 2015-17"). ASU 2015-17 became effective in fiscal year 2018. Therefore, we presented all deferred tax liabilities and assets as noncurrent on the balance sheet instead of separating deferred taxes into current and noncurrent amounts. Prior period was not retrospectively adjusted. In addition, in March 2016, the FASB issued ASU 2016-09, Compensation- Stock Compensation (Topic 718) ("ASU 2016-09"), which also became effective in fiscal year 2018. As a result of this required implementation, excess tax benefits are recorded on exercises of stock options as a reduction of income tax expense in the consolidated statement of comprehensive income, whereas they were previously recognized in equity.

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In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers (Topic 606) ("ASU 2014-09"), which outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The standard requires entities to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The new guidance also includes a cohesive set of disclosure requirements intended to provide users of financial statements with comprehensive information about the nature, amount, timing and uncertainty of revenue and cash flows arising from a company's contracts with customers. In August 2015, the FASB issued ASU 2015-14, Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date, which deferred the effective date of the new revenue standard. Accordingly, the updated standard is effective for us beginning with the first quarter of the Company's fiscal year 2019, with early application permitted in fiscal year 2018. The standard allows for either "full retrospective" adoption, meaning the standard is applied to all of the periods presented, or "modified retrospective" adoption, meaning the standard is applied only to the most current period presented in the financial statements. The Company is currently evaluating the effect ASU 2014-09 will have on the Company's Consolidated Financial Statements and disclosures.

In January 2016, the FASB issued ASU 2016-01, Financial Instruments (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities ("ASU 2016-01"). ASU 2016-01 will be effective beginning with the first quarter of the Company's fiscal year 2019. The amendments require certain equity investments to be measured at fair value with changes in the fair value recognized through net income. The Company is currently evaluating the effect ASU 2016-01 will have on the Company's Consolidated Financial Statements and disclosures.

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842) ("ASU 2016-02"). ASU 2016-02 will be effective beginning with the first quarter of the Company's fiscal year 2020, with early adoption permitted. The amendments require the recognition of lease assets and lease liabilities on the balance sheet for most leases, but recognize expenses in the income statement in a manner similar to current accounting treatment. In addition, disclosures of key information about leasing arrangements are required. Upon adoption, leases will be recognized and measured at the beginning of the earliest period presented using a modified retrospective approach. The Company is currently evaluating the effect ASU 2016-02 will have on the Company's Consolidated Financial Statements and disclosures.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments ("ASU 2016-13"). ASU 2016-13 changes the impairment model for most financial assets and certain other instruments, which sets forth a new forward-looking impairment model based on expected losses rather than incurred losses. The guidance also requires increased disclosures. ASU 2016-01 will be effective beginning with the first quarter of the Company's fiscal year 2021. The Company is currently evaluating the effect ASU 2016-13 will have on the Company's Consolidated Financial Statements and disclosures.

In November 2016, the FASB issued ASU 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash (a consensus of the FASB Emerging Issues Task Force ("ASU 2016-18"), which provides guidance on the presentation of restricted cash or restricted cash equivalents in the statement of cash flows. ASU 2016-18 will be effective beginning with the first quarter of the Company's fiscal year 2019. The adoption of ASU 2016-18 is not expected to have a material impact on the consolidated financial statements and will only change the presentation of the Consolidated Statement of Cash Flows.

In March 2017, the FASB issued ASU 2017-08, Receivables — Nonrefundable Fees and Other Costs (Subtopic 310-20), Premium Amortization on Purchased Callable Debt Securities ("ASU 2017-08"), which requires the premium on callable debt securities to be amortized to the earliest call date as opposed to the contractual life of the security. ASU 2017-08 will be effective beginning with the first quarter of the Company's fiscal year 2020. The Company is currently evaluating the effect ASU 2017-08 will have on the Company's Consolidated Financial Statements and disclosures.

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From time to time, new accounting pronouncements are issued by the FASB and other regulatory bodies that are adopted by the Company as of the specified effective dates. Unless otherwise discussed, management believes that the impact of recently issued standards, which are not yet effective, will not have a material impact on the Company's Consolidated Financial Statements upon adoption.

Forward-looking Statements

Statements in this Report on Form 10-Q, including those set forth in this section, may be considered "forward looking statements" within the meaning of Section 21E of the Securities Act of 1934. These forward-looking statements are often identified by words such as "estimate," "predict," "hope," "may," "believe," "anticipate," "plan," "expect," "require," "intend," "assume," and similar words. Forward-looking statements contained in this Report on Form 10-Q speak only as of the date of this report or, in the case of any document incorporated by reference, the date of that document. We do not intend to publicly update or revise any forward-looking statement contained in this Report on Form 10-Q or in any document incorporated herein by reference to reflect changed assumptions, the occurrence of unanticipated events or changes to future operating results over time.

Forward-looking statements involve risks, uncertainties and other factors, which may cause our actual results, performance or achievements to be materially different from those expressed or implied by such forward-looking statements. In addition to the Risk Factors described in Part I, Item 1A. Risk Factors in our Form 10-K, factors that could affect our results and cause them to materially differ from those contained in the forward-looking statements include, but are not limited to:

- We operate in an industry that is currently experiencing a prolonged and significant downturn;
- We may not be able to successfully integrate past acquisitions, including the recent acquisition of Lexington Homes, or any future acquisitions to attain the anticipated benefits. Past acquisitions may adversely impact the Company's liquidity;
- Our involvement in vertically integrated lines of business, including manufactured housing consumer finance, commercial finance and insurance, exposes the Company to certain risks;
- Tightened credit standards, curtailed lending activity by home-only lenders and increased government lending regulations have contributed to a constrained consumer financing market;
- The availability of wholesale financing for industry retailers is limited due to a reduced number of floor plan lenders and reduced lending limits;
- Our participation in certain financing programs for the purchase of our products by industry distributors and consumers may expose us to additional risk of credit loss, which could adversely impact the Company's liquidity and results of operations;
- Our results of operations could be adversely affected by significant warranty and construction defect claims on factory-built housing;
- We have contingent repurchase obligations related to wholesale financing provided to industry retailers;
- Our operating results could be affected by market forces and declining housing demand;
- We have incurred net losses in certain prior periods and there can be no assurance that we will generate income in the future;
- A write-off of all or part of our goodwill could adversely affect our operating results and net worth;
- The cyclical and seasonal nature of the manufactured housing industry causes our revenues and operating results to fluctuate, and we expect this cyclicality and seasonality to continue in the future;
- Our liquidity and ability to raise capital may be limited;

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- The manufactured housing industry is highly competitive, and increased competition may result in lower revenue;
- If we are unable to establish or maintain relationships with independent distributors who sell our homes, our revenue could decline;
- Our business and operations are concentrated in certain geographic regions, which could be impacted by market declines;
- Our results of operations can be adversely affected by labor shortages and the pricing and availability of raw materials;
- If the manufactured housing industry is not able to secure favorable local zoning ordinances, our revenue could decline and our business could be adversely affected;
- The loss of any of our executive officers could reduce our ability to execute our business strategy and could have a material adverse effect on our business and results of operations;
- Certain provisions of our organizational documents could delay or make more difficult a change in control of our Company;
- Volatility of stock price;
- Deterioration in economic conditions and turmoil in financial markets could reduce our earnings and financial condition;
- The cost of operations could be adversely impacted by increased costs of healthcare benefits provided to employees;
- A prolonged delay by Congress and the President to approve budgets or continuing appropriation resolutions to facilitate the operations of the federal government could delay the completion of home sales and/or cause cancellations, and thereby negatively impact our deliveries and revenues;
- Information technology failures or data security breaches could harm our business; and
- We are subject to extensive regulation affecting the production and sale of manufactured housing, which could adversely affect our profitability.

We may make additional written or oral forward-looking statements from time to time in filings with the SEC or in public news releases or statements. Such additional statements may include, but are not limited to, projections of revenues, income or loss, capital expenditures, acquisitions, plans for future operations, financing needs or plans, the impact of inflation and plans relating to our products or services, as well as assumptions relating to the foregoing.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Market risk is the risk of loss arising from adverse changes in market prices and interest rates. We may from time to time be exposed to interest rate risk inherent in our financial instruments, but are not currently subject to foreign currency or commodity price risk. We manage our exposure to these market risks through our regular operating and financing activities.

Our operations are interest rate sensitive. As overall manufactured housing demand can be adversely affected by increases in interest rates, a significant increase in wholesale or mortgage interest rates may negatively affect the ability of retailers and home buyers to secure financing. Higher interest rates could unfavorably impact our revenues, gross margins and net earnings. Our business is also sensitive to the effects of inflation, particularly with respect to raw material and transportation costs. We may not be able to offset inflation through increased selling prices.

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CountryPlace is exposed to market risk related to the accessibility and terms of long-term financing of its loans. In the past, CountryPlace accessed the asset-backed securities market to provide term financing of its chattel and non-conforming mortgage originations. At present, independent asset-backed and mortgage-backed securitization markets are not readily accessible to CountryPlace and other manufactured housing lenders. Accordingly, CountryPlace has not continued to securitize its loan originations as a means to obtain long-term funding.

We are also exposed to market risks related to our fixed rate consumer and commercial loan notes receivables, as well as our securitized financings balances. For fixed rate instruments, changes in interest rates do not change future earnings and cash flows. However, changes in interest rates could affect the fair value of these instruments. Assuming the level of these instruments as of July 1, 2017, is held constant, a 1% unfavorable change in average interest rates would adversely impact the fair value of these instruments, as follows (in thousands):

	Change in Fair Value
Consumer loans receivable	$4,062
Commercial loans receivable	$169
Securitized financings	$971

In originating loans for sale, CountryPlace issues IRLCs to prospective borrowers and third-party originators. These IRLCs represent an agreement to extend credit to a loan applicant, or an agreement to purchase a loan from a third-party originator, whereby the interest rate on the loan is set prior to loan closing or sale. These IRLCs bind CountryPlace to fund the approved loan at the specified rate regardless of whether interest rates or market prices for similar loans have changed between the commitment date and the closing date. As such, outstanding IRLCs are subject to interest rate risk and related loan sale price risk during the period from the date of the IRLC through the earlier of the loan sale date or IRLC expiration date. The loan commitments generally range between 30 and 180 days; however, borrowers are not obligated to close the related loans. As a result, CountryPlace is subject to fallout risk related to IRLCs, which is realized if approved borrowers choose not to close on the loans within the terms of the IRLCs. As of July 1, 2017, CountryPlace had outstanding IRLCs with a notional amount of $14.7 million and are recorded at fair value in accordance with ASC 815. The estimated fair values of IRLCs are based on quoted market values and are recorded in other assets in the consolidated balance sheets. The fair value of IRLCs is based on the value of the underlying mortgage loan adjusted for: (i) estimated cost to complete and originate the loan and (ii) the estimated percentage for IRLCs that will result in closed mortgage loans. The initial and subsequent changes in the value of IRLCs are a component of current income. Assuming CountryPlace's level of IRLCs as of July 1, 2017 is held constant, a 1% increase in average interest rates would decrease the fair value of CountryPlace's obligations by approximately $281,000.

Item 4. Controls and Procedures

(a) Disclosure Controls and Procedures

We carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in the Exchange Act Rules 13a-15(e) and 15d-15(e)). Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered in this report, our disclosure controls and procedures were effective.

(b) Changes in Internal Control over Financial Reporting

There have been no changes in our internal controls over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) that occurred during the fiscal quarter ended July 1, 2017, which have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II. OTHER INFORMATION

Item 1. Legal Proceedings

Information regarding reportable legal proceedings is contained in Part I, Item 3, Legal Proceedings, in our Form 10-K. The following describes legal proceedings, if any, that became reportable during the period ended July 1, 2017, and, if applicable, amends and restates descriptions of previously reported legal proceedings in which there have been material developments during such quarter.

We are party to certain legal proceedings that arise in the ordinary course and are incidental to our business. Certain of the claims pending against us in these proceedings allege, among other things, breach of contract, breach of express and implied warranties, construction defect, deceptive trade practices, unfair insurance practices, product liability and personal injury. Although litigation is inherently uncertain, based on past experience and the information currently available, management does not believe that the currently pending and threatened litigation or claims will have a material adverse effect on the Company's consolidated financial position, liquidity or results of operations. However, future events or circumstances currently unknown to management will determine whether the resolution of pending or threatened litigation or claims will ultimately have a material effect on our consolidated financial position, liquidity or results of operations in any future reporting periods.

Item 1A. Risk Factors

In addition to the other information set forth in this Report, you should carefully consider the factors discussed in Part I, Item 1A, Risk Factors, in our Form 10-K, which could materially affect our business, financial condition or future results. The risks described in this Report and in our Form 10-K are not the only risks facing our Company. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results.

Item 6. Exhibits

See Exhibit Index.

All other items required under Part II are omitted because they are not applicable.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Cavco Industries, Inc.
Registrant

Signature	Title	Date
/s/ Joseph H. Stegmayer Joseph H. Stegmayer	Chairman, President and Chief Executive Officer (Principal Executive Officer)	August 8, 2017
/s/ Daniel L. Urness Daniel L. Urness	Executive Vice President, Treasurer and Chief Financial Officer (Principal Financial and Accounting Officer)	August 8, 2017

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EXHIBIT INDEX

Exhibit No.	Exhibit
31.1	Certification of the Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 - Rule 13a-14(a)/15d-14(a)
31.2	Certification of the Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 - Rule 13a-14(a)/15d-14(a)
32	Certification of the Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101	The following materials contained in this Quarterly Report on Form 10-Q for the period ended July 1, 2017 were formatted in XBRL (eXtensible Business Reporting Language): (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Comprehensive Income, (iii) Consolidated Statements of Cash Flows and (iv) Notes to Consolidated Financial Statements