Paragon Personal and Auto Finance (No. 1) PLC

UK-ABS

EXPECTED CLOSING DATE:
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This pre-sale report addresses the structure and characteristics of the proposed transaction based on the information provided to Moody's as of 6 June, 2001

Investors should be aware that certain issues concerning this transaction have yet to be finalised. *Upon conclusive review of all documents and legal information as well as any subsequent changes in information, Moody's will endeavour to assign **definitive** ratings to this transaction. The definitive ratings may differ from the **prospective** ratings set forth in this report. Moody's will disseminate the assignment of definitive ratings through its Client Service Desk.*

TRANSACTION IN BRIEF

Class	Rating	Amount	Coupon
A	(P)**Aaa**	£178,210,000	3 Month LIBOR + [•] bps
B	(P)**A2**	£51,450,000	3 Month LIBOR + [•] bps
C	N/R	£21,340,000	3 Month LIBOR + [•] bps

Structure Summary

Structure Type:	Senior/subordinate mixed receivable (personal loans, retail credit loans, car finance contracts and secured loans) backed Notes with credit enhancement.
Revolving Period:	4 years
Note Payment Dates:	15th day of March, June, September, and December, commencing on September 15th, 2001
The Issuer:	Paragon Personal and Auto Finance (No. 1) PLC
Originators/Sellers:	Paragon Personal Finance Limited (PPF) Paragon Car Finance Limited (PCF), Colonial Finance UK Limited (CFUK)
Transaction Bank Account:	The Royal Bank of Scotland Group Plc, "RBS" (**Aa2**, **Prime-1**)
Servicer:	Paragon Finance PLC (PFPLC), "Paragon"
Interest Rate Swap Provider:	RBS
Lead Manager:	RBS

Credit Support

Cash Reserve:	4.3% of the Notes
Over-Collateralisation:	4.87% of the Notes
Subordinated Tranches:	20.5% Class B, 8.5% Class C

Provisional Portfolio Summary as at 11 May 2001

Number of Contracts:	103,336
Current Balance:	£213,040,144
Contract Interest Types:	Fixed and floating interest rate

	Unsecured Loans (Retail and Personal)	Car Finance Contracts	Secured Loans
Weighted Average Interest Rate:	13.3%	12.6%	11.7%
Weighted Average Remaining Term:	3.1 years	4.1 years	11.5 years
Weighted Average Seasoning:	16 months	1.1 months	5.9 months
Weighted Average LTV:	N/A	N/A	86.2%
Average Current Balance Outstanding:	£3,771	£7,398	£14,034

RATING OPINION

Moody's has assigned the following prospective long-term ratings to the debt issuance of Paragon Personal and Auto Finance (No. 1) PLC:

(P)**Aaa** £178,210,000 Class A Floating Rate Notes due 2021;

(P)**A2** £54,450,000 Class B Floating Rate Notes due 2032; and

N/R £21,340,000 Class C Floating Rate Notes due 2048.

The prospective rating of the Class A is based upon:

Positive Features:

- Moody's assessment of the credit quality of the receivables pool;
- The credit enhancement provided by Excess Spread, Over-Collateralisation, and the First Loss Fund;
- The subordination of the Class B and C Notes;
- The Performing Asset Balance Test, which acts as an early amortisation trigger during the revolving period;
- The eligibility criteria selected for the four types of loan contracts;
- The benefit of an interest rate swap with RBS (**Aa2**, **Prime-1**), which hedges the interest rate risk between the fixed rate interest from the asset pool and the floating rate coupons on the Notes;
- Moody's assessment of Paragon's operations, controls, and procedures for both underwriting and subsequent servicing of the asset pool; and
- The sound transaction's legal structure and tax analysis.

Less Favourable Features:

- The limited amount of performance data available, due to the fact that the Secured Loan business has only been originating loans since July of 1999;
- The presence of delinquent and non-performing loans in the collateral pool (See *"Collateral"* below).

Moody's prospective rating of the Class B Notes is based on the same as that set out above for the A Notes, except for taking into account the subordinated positions in the transaction of each of the Class B and Class C Notes. The prospective ratings on the Notes reflect the timely payment of interest and the ultimate payment of principal on the Notes on or before the legal final maturity.

RATING SUMMARY

Structure

The Issuer is a special purpose vehicle incorporated under the laws of England and is a wholly owned subsidiary of the Paragon Group of Companies. The activities of the Issuer are restricted to ensure that it is bankruptcy remote. The Issuer will fund the purchase of the assets by issuing the Class A, Class B, and Class C Notes.

The Notes pay quarterly coupons at a fixed spread over LIBOR, with the first payment being made on September 15th 2001.

The Issuer's beneficial interest in the English receivables will be an equitable interest only. No notification of the assignment and transfer of the receivables shall be made to the receivables' debtors. The Trustee will therefore need, via the power of attorney granted by Paragon, to give notice to obligors of the transfer of the receivables. In the case of an insolvency of Paragon, the Note Trustee will still be able to give notice to the borrowers requiring them to make payments directly to the Receivables Trustee's account.

In relation to the Scottish auto and unsecured receivables (12.0% of the provisional total pool) the transfer of the receivables must be done using a legal perfection of assets, which could be subject to Stamp Duty — the risk being mitigated through an additional reserve provided specifically for this purpose. Paragon will apply for adjudication from Stamp Duty, seeking a Section 42 Finance Act 1930 intra group exemption. If this application is adjudicated "Stamped without Duty" then this additional reserve can be removed.

Collateral

The mixed asset receivables pool consists of:

1. Unsecured loans originated by Colonial Finance (UK) Ltd and Paragon Personal Finance Ltd, comprising personal general purpose loans. Colonial originated loans will only be purchased at closing, whereas personal loans originated by Paragon will be substituted during the revolving period. The percentage of Colonial personal loans will be 34% at closing. As these loans redeem, the limit for Paragon originated loans will be 30%;
2. Unsecured loans originated by Colonial Finance (UK) Ltd and Paragon Personal Finance Ltd, comprising retail loans. Colonial originated loans will only be purchased at closing, whereas retail loans originated by Paragon will be substituted during the revolving period. There is no limitation on the percentage of retail loans in the pool;
3. Secured loans originated by Paragon Personal Finance Ltd. The assets included in the portfolio will comprise the benefit of loans to individuals in the United Kingdom secured by second or subsequent-ranking charges over residential property in England, Wales and Scotland, together with all security relating to those loans. Secured loans will not exceed 30% of the total pool; and
4. Car finance contracts made to individuals, partnerships and corporate bodies. The assets include the benefit of motor vehicle hire purchase agreements and motor vehicle conditional sale agreements and the beneficial ownership of the vehicles that are concerned. Car finance contracts will not exceed 30% of the total pool.

Moody's believes that the Colonial section of the portfolio is of a relatively poor quality, as it includes substantially all of the assets owned by Colonial and purchased by Paragon, irrespective of their arrears status. Some 20% of the of the Colonial loans in the provisional pool were more than 1 month in arrears, including 7% where the loans are more than 12 months in arrears. However, as the proportion of Paragon originated assets will increase as the transaction revolves, Moody's analysis assumes some improvement in the quality of the asset portfolio over time.

In addition, the Colonial section of the portfolio contains the greatest degree of potential non-compliance with the Consumer Credit Act. To mitigate this risk, Paragon Finance PLC has agreed to repurchase loans which prove to be unenforceable due to the Act, or which are subject to set-off. Repurchases from the initial Colonial portfolio, in respect of loans which are unenforceable, are subject to a floor of £ 1 m and a cap of £ 20 m.

Moody's also believes that Car Finance Contracts may be relatively riskier assets for the Issuer. Although the expected loss on these contracts is low, Moody's Notes that the Investors may have exposure to individual dealers and that there is some risk that the agreements may be re-characterised as secured loans to the dealer. The Issuer would not therefore enjoy ownership rights in the vehicle financed. However this risk is mitigated by the fact that exposure to dealerships will be limited to £ 250,000 on an aggregate basis.

Substitution

The criteria which must be met for substitution of further assets during the 4 year substitution period include:

i) New receivables can only be added if the Asset Test is 1 to 1;

ii) The First Loss Fund is fully funded;

iii) Secured loans which are more than 3 months in arrears should represent less than 10% of the secured loans originated by Paragon or, the amount of interest that is due to be generated by the pool divided by the actual amount of interest generated must be equal to/or greater than 95% (or such other percentages as may be agreed with Moody's from time to time);

iv) Car finance contracts which are more than 3 months in arrears should represent less than 4% of the car finance contracts originated by Paragon, or the amount of interest that is due to be generated by the pool divided by the actual amount of interest generated must be equal to/or greater than 96% (or such other percentages as may be agreed with Moody's from time to time);

v) Personal unsecured loans which are more than 3 months in arrears should represent less than 10% of the secured loans originated by Paragon or, the amount of interest that is due to be generated by the pool divided by the actual amount of interest generated must be equal to/or greater than 95% (or such other percentages as may be agreed with Moody's from time to time);

vi) Retail unsecured loans which are more than 3 months in arrears should represent less than 4% of the retail unsecured loans originated by Paragon, or the amount of interest that is due to be generated by the pool divided by the actual amount of interest generated must be equal to/or greater than 96% (or such other percentages as may be agreed with Moody's from time to time);

vii) The ratio of car finance contracts, secured loans and unsecured loans must remain within the respective caps (car finance contracts maximum 30%, secured loans maximum of 30%, unsecured loans: maximum of 30% for personal loans and 100% for retail loans); and

viii) A minimum weighted average margin over the swap rate of 5% must be maintained for any pool of substituted loans.

These criteria assist in mitigating the risk that the volatility of the pool may worsen due to substitution. If such deterioration is detected, then the substitution period will end and the transaction will amortise.

In addition to these eligibility criteria, a Performing Assets Balance Test Ratio (the Asset Test) will act as an early amortisation trigger. The test defined as the balance of performing assets plus available funds (principal and interest receipts) net of over-collateralisation divided by the outstanding Notes will have to be maintained, via the use of available funds, at a 1 to 1 level. If the amount of available fund is not sufficient to maintain the 1 to 1 Asset Test, then the Notes will amortise.

Principal Paying Interest

The structure allows the deferment of interest payment on the Class C and B Notes to repay Class A principal. If the Asset Test is less than ***0.915 to 1*** (and less than ***0.71 to 1***) then amounts due to pay interest on the Class C (and Class B) Notes will be used to repay Class A principal. This provides substantial protection for investors in the Class A Notes against a gradual deterioration in the arrears performance of the portfolio. Moody's believes, however, that the fact that the Issuer is unable to use all receipts to pay interest on the Class B or Class C Notes exposes the Class B and Class C Notes to greater liquidity risk.

HEDGING

Interest Rate Risk

On the Closing Date, the Issuer will enter into hedging arrangements with RBS, as Swap Counterparty to hedge any loans which are fixed, capped or collared rate. These asset pool cashflows are at fixed rates of interest, whereas the Notes will pay fixed spreads over three month LIBOR. The fixed/floating interest rate mismatch is hedged by the Issuer entering into hedging arrangements which may consist of swaps, caps or floors with RBS.

CREDIT ENHANCEMENT

Investors in the Notes are protected from the effect of credit losses on the pool in a number of ways.

Excess Spread

The first layer of protection for investors in the Notes is the Excess Spread in the transaction, which is the difference between:

1. The income receivable by the Issuer under the auto loans, secured and unsecured loans, and its other investments and swap arrangements; and
2. The amounts of interest due by the Issuer on account of its various ongoing costs and expenses and under the Notes.

The credit enhancement value of Excess Spread also depends on the timing of principal losses. Excess Spread is available on a "use it or lose it" basis and so, if not used to top up the first Loss Fund or to reduce the Debtor Ledger, it is paid back to Paragon via the Subordinated Loan and other profit extraction mechanisms. This might occur before losses on the portfolio have shown through. The value of the Excess Spread was assessed by Moody's under a variety of adverse conditions, including high pre-payment scenarios.

Over-Collateralisation

The transaction provides credit enhancement for the Notes through over-collateralisation, i.e. the principal value of the assets is greater than that of the Notes. The level of over-collateralisation is ***4.87***% at closing. As the over-collateralisation is subtracted from the numerator of the Asset Test, the level of over-collateralisation is maintained during the life of the transaction in normal conditions.

First Loss Fund

The third layer of protection which is available for Investors in the Notes is the First Loss Fund. On closing, Paragon will make a Subordinated Loan to the Issuer of an amount equal to ***4.3***% of the aggregate initial principal amount outstanding of the Notes to be issued.

This loan will be paid into a designated account to be used to provide on-going liquidity support, to meet senior expenses and to provide credit support to the transaction. Any amounts utilised will be replenished from future excess spread in the transaction.

On each Interest Payment Date, revenue of the Issuer in excess of the amounts required to pay or provide for priority payments will be applied to replenish the First Loss Fund to the Required Amount. After the latter of the June 2006 interest payment date and the moment when the Class A Notes are fully redeemed, the Required Amount reduces to half its level at closing providing that the Asset Test is 1 to 1.

Debtor Ledger

If on any Interest Payment Date the Issuer has insufficient income to meet its Priority Expenses (which include Servicer fees, Note Trustee, and Class A Note interest due on that date) it will use principal receipts to meet the deficiency and debit the amount to the Debtor Ledger.

For auto, secured and unsecured loans, 100% of accounts in arrears will be written off to the Debtor Ledger at twelve months delinquent, if they have not been previously written off.

To the extent that on any subsequent Interest Payment Date there is income available to the Issuer in excess of the amount then required to meet Priority Expenses, it will be applied in reducing or extinguishing any such debit.

Principal and Interest Subordination

The Class A Notes rank first in priority. The Class B Notes will be subordinated to the Class A Notes. The Class C Notes will be subordinated to the Class B Notes in priority. Accordingly, upon enforcement of the security and after utilising the transaction's Over-Collateralisation and the transaction First Loss Fund, losses will be borne first by the Class C Noteholders then by the Class B Noteholders and then by the Class A Noteholders.

Pro Rata B and C Note Amortisation

The pro-rata paydown of the Class B and Class C Notes will be subject to the relative percentage of the Class B and C Notes to the total Notes having doubled and the Asset Test being greater than 1 to 1

VAT Grouping

In common with other Paragon transactions rated by Moody's, but unlike the vast majority of UK transactions, the Issuer is grouped with the rest of the Paragon Group for VAT purposes. The VAT grouping means that services or goods provided between members of the VAT group are not subject to VAT (which would otherwise be payable on servicing fees); but, as a consequence, each member of the VAT group is jointly and severally liable for VAT liabilities of all other members of that group. A long standing arrangement is in place with Morgan Guaranty Trust Company of New York (**Aa3**, **Prime-1**) to mitigate this risk.

Servicer

Moody's believes that Paragon Finance PLC has a well-developed servicing business with a track record of successful collections and arrears management in the United Kingdom. There is no stand-by servicer in place, however the level of credit enhancement and liquidity provisions present in the transaction gives Moody's comfort that this risk is sufficiently mitigated.

Moody's Rating Methodology

Moody's structured finance rating methodology is based upon an "expected loss" approach, which is based upon the probability of default of assets in the pool and the severity of loss in the event of default, (i.e. the level of subsequent recoveries, if any).[1,2] Moody's calculated the expected loss for the transaction by analysis of historical data provided by the originator together with Moody's expectation of the future. The expected loss and its likely volatility were then used by Moody's to model the transaction assuming a log-normal distribution of that loss.[3] This analysis took account of structural features such as the revolving period, early amortisation triggers, over-collateralisation and the mechanism for capture of excess spread. The loss for each Note tranche by the model was then converted into a rating using Moody's idealised default probability tables.

Based on the above analysis, Moody's believes that the Credit Enhancement available for the transaction is consistent with the ratings on the Notes.

Monitoring

Moody's will monitor the transaction and the ratings of the Notes on an ongoing basis until the Notes mature. The monitoring will include the review of the monthly servicing reports and other performance data including supporting ratings, together with discussions with the servicer and other parties, as Moody's considers appropriate.

1 "Rating Mezzanine Securities in Structured Finance Transactions: The impact of an Expected Value Approach", *Moody's International Structured Finance Special Report* (February 1999).
2 "Subordination, Diversification and the Expected-Loss Approach to Credit Risk", *Moody's International Structured Finance Special Report* (February 1997).
3 "The Lognormal Method Applied to ABS Analysis", *Moody's International Structured Finance Special Report* (July 2000).

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