Finance for People (No. 2) PLC, Multi Class Mortgage Backed FRNs

UK – MBS

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TRANSACTION IN BRIEF

	Class A1	Class A2	Class B	Class C
Rating:	**Aaa**	**Aaa**	**A2**	**Baa3**
Amount:	£55m	£77m	£33m	£10m
Coupon:	Libor + 10 bp	Libor + 18bp	Libor + 40bp	Libor + 92bp
Step Up Date:	Mar. 2000	Mar. 2004	Mar. 2004	Mar. 2004
Step Up Margin:	Libor+ 20bp	Libor+ 45bp	Libor+ 85bp	Libor + 195bp
Final Maturity:	Dec. 2034	Dec. 2034	Dec. 2034	Dec. 2034

Interest Payment Dates:	March, June, September and December (last business day)
Issuer:	Finance for People (No.2) PLC
Originator:	Paragon Mortgages Limited (50.7%), Paragon Finance PLC (49.1%) and Local Authorities (0.2%).
Servicer:	Paragon Finance PLC
Servicer of Last Resort:	Barclays Bank PLC (**Aa2**)
Trustee:	JP Morgan Trustee Ltd (**Aa1**)
Lead Manager:	HSBC Markets
Asset Characteristics:	First residential mortgages in England, Wales and Scotland

Summary of Provisional Pool (31 December 1997)

Count:	3,365 residential loans		
Prin. Amt.	£185,761,329		
LTV:	Avg.: 85%	Max. 100+%	(18%)
Loan Size:	Avg.: £55,204	Max. £250,000+	(3.7%)
Performance:	*Current* (inc <=1 month arrears) 55%		
	Arrears: 1-3 months 4 %, 3-6 months 4%, 6-12 months 8%, 12+ months 30%		
Loan Usage:	Purchase 54%, Remortgage 46%		
Interest Rate:	Administered Variable Rate 85%., Other 3%		
	Fixed Rate (that reverts to variable) 12%		
Concentration:	39% SE, 19% Ldn, 2% North, 8% SW, 4% E Anglia, 5% NW		
	5% E Mid, 5% W Mid, 3% Wales, 5% Yorks, 5% Scot		
Seasoning:	86 2%, 87 4%, 88 8%, 89 16%, 90 11%, 91 9%, 97 51%		
Mtg. Indem. Ins.	Sun Alliance Insurance Group (**Aa3**), Legal and General Assurance Society Limited (**Aa1**) C.E. Heath (Lloyd's of London)		
Credit Support:	First Loss Fund 2% of the initial current balance of the mortgages, £33,000,000 Class B Notes, £10,000,000 Class C Notes, and Spread		
Mortgage Overcollateralisation:	Approximately 5.35% of the initial current balance		
Launch Date:	27 Jan 1998		

Moody's Investors Service

February 1998

OPINION

Moody's has assigned long term credit ratings of **Aaa** to the Class A1 and A2 Notes, **A2** to the Class B Notes and **Baa3** to the Class C Notes (together the "ratings").

The rating of the Class A Notes is based upon an analysis of the characteristics of the mortgage pool backing the Notes, the protection the Notes receive from the credit enhancement relative to defaults and arrears in the mortgage pool, and the legal and structural integrity of the issue.

The ratings of the Class B and Class C Notes are based on the above factors, and on an assessment of the extent of their subordinate position within the structure.

The ratings of each of the Notes address the timely payment of interest, and ultimate payment of principal.

STRUCTURE SUMMARY

Structure

The issuer is a special purpose vehicle incorporated in England and ultimately owned by The Paragon Group of Companies PLC.

The assets backing the structure are first mortgages secured by residential properties in England, Wales or Scotland that have been sold by various companies within the Paragon Group to the issuer.

The Issuer funds the purchase price of the loans by issuing the Class A, Class B and Class C Notes (together the "Notes") and the Loan Stock.

Start up expenses of the issuer are funded by Paragon Mortgages Limited (PML). These costs are repayable by the issuer though such payments are subordinated to payments of both interest and principal to the Class A, Class B and Class C noteholders. Paragon Finance PLC (PFPLC) has also advanced a separate Subordinated Loan to the issuer to fund a First Loss Fund equal to 2% of the initial current balance of the mortgages.

The First Loss Fund also acts as a source of liquidity for the structure and assists the payment of interest in the event that income from the mortgages is insufficient to pay Note interest and various costs. Proceeds from the sale of possessed properties are treated first as income and then principal and this also enhances liquidity. Finally replenishment of the First Loss Fund is senior to the reduction in the Principal Deficiency Ledger, until Class A Notes are no longer outstanding.

The structure does not possess a Reserve Fund to fund mandatory further advances on the mortgage portfolio or the potential for the deferral of interest on the stabilised rate mortgages. Moody's believes that the liquidity provided by the First Loss Fund and by the structure of the transaction, is consistent with the ratings assigned to the Notes.

No purchases of new mortgages with redemption moneys is permitted, though the Issuer may, subject to various conditions, utilise principal receipts to make discretionary further advances on existing mortgages of up to £31,500,000.

Interest Rate Risk

The issuer receives either an administered or an externally set variable mortgage rate or a temporarily fixed rate on its mortgage assets while paying Libor plus a margin on the Notes.

The structure does not contain the Threshold Rate Mechanism found in some previous Paragon securitisations, and thus there is a small risk that the interest rate charged on the mortgage portfolio may be less than that payable on the Notes, plus various expenses. However, the servicer is obliged to set a mortgage rate on the administered variable rate mortgages within the portfolio so as to charge an "Average Margin" on the whole pool of at least 150bp (200bp after step-up) pa over 3 Month Libor.

A Shortfall Fund, may be established by the Servicer to enable it to set an Average Margin on the mortgage pool below the minimum level, to the extent that the fund is able to make good the difference.

The structure also benefits from interest rate swaps provided by Morgan Guaranty Trust Company of New York (**Aa1**), in respect of the fixed rate mortgages that represent 12.3% of the pool. The support that this swap provides to the transaction is reduced as the swap may require the SPV to pay certain break costs to the swap provider in the event that mortgages default or prepay.

The Servicer may also agree to convert fixed rate into floating rate mortgages and vice versa, and may also alter the payment method between repayment, endowment and pension linked. There is no requirement to hedge such further interest rate exposure, unless the then current rating of the Notes would be adversely affected.

Credit Enhancement

The first layer of protection is *spread* in the transaction, which is the difference between (1) the income received from the mortgages and other investments, and (2) the coupon on the Notes plus various ongoing costs. The value of this spread was assessed under a variety of adverse conditions which would minimise its effectiveness, including high prepayment speeds, and back-ended losses. Excess spread leaves the transaction to the extent that it is not required to meet ongoing or past losses, to add to one of the various funds or to amortise the Class A Notes.

The existence of mortgages that are currently in arrears with their payments within a structure, may increase the protection provided by excess spread, as losses are more likely to occur early in the life of the structure, when excess spread may otherwise leave the transaction.

The second layer of protection for investors in the rated Notes is the *over-collateralisation* of the Notes, equal to approximately 5.35% of the initial current balance of the mortgage pool. This is funded through the sale of some of the mortgages at a discount to their principal amount outstanding, and through the issuance of Loan Stock, such that approximately £185m of mortgage assets (or principal redemption funds) support £175m of Notes.

The structure also benefits from the provision that requires the issuer to use the excess spread (1% of the initial balance of the mortgages), that would leave the transaction), to amortise the Class A Notes thus increasing the overcollateralisation to 6.35%.

The third layer of protection for investors in the rated Notes is the *First Loss Fund,* which is 2% of the initial balance of the initial mortgage pool. Excess spread is also used to replenish any drawings from the First Loss Fund in prior periods, throughout the life of the transaction.

The balance of the First Loss Fund may amortise in line with the mortgage collateral, subject to certain severe triggers, to the extent that the remaining balance of the First Loss Fund equals 4% of the principal balance of the outstanding mortgage pool.

The Class B Notes and Class C Notes also provide protection for the Class A Notes.

On each payment date on the Notes, interest on the Class A Notes is paid in priority to payment of interest to the Class B Notes, and both are paid in priority to interest on the Class C Notes.

If outstanding principal losses and any interest arrears on the Notes, after the effect of spread, exceed the First Loss Fund plus the Class B and Class C Note balance, then the payment of Class B and Class C Note interest is subordinated to the rebuilding of the First Loss Fund and to the reduction of the principal deficiency ledger. Class B and Class C interest is therefore effectively subordinate to A Note interest and principal but not Class B and Class C principal.

No principal is paid to the Class B and Class C Noteholders until the Class B and Class C Notes together represent approximately 49% of the total Class A, Class B and Class C Notes. Thereafter, and subject to certain triggers, prepayments are allocated so as to restore the 49% ratio. Principal payments allocated to the Class B and Class C Notes are divided in proportion to their respective original principal balances. The Class B and Class C Notes are subject to a minimum balance of £4,000,000 while any Class A Notes remain outstanding.

Collateral

The Notes are backed by residential first mortgage loans on properties in England, Wales or Scotland. With the exception of a small proportion of loans purchased by PFPLC from Local Authorities (0.2% of the pool), the mortgages were originated by PFPLC and by PML. The deal represents a refinancing of the NHL(3) mortgage backed transaction together with newly originated business.

As in the previous Paragon transaction (FFP1) the arrears accrued on non performing loans were sold to the structure, and financed through the issue of Notes.

The Pool Credit Quality was Negatively Affected By:

1. The inclusion of mortgages currently in arrears with their payments (approximately 45.5% the provisional portfolio).This is the most substantial negative feature of the portfolio. It is however partially offset by the fact that many arrears loans, are making full or partial payments on their account each month. Of the arrears mortgages, 34% are described as Arrangement Mortgages whereby the borrower is making payments under an agreed arrangement and where a payment has been received in 5 of the last 6 months totalling at least 75% of the amount due over the 6 month period.
2. Relatively high LTV ratios (18% of the pool has an LTV ratio above 100%).
3. The proportion (potentially 30% of Self Certified loans in the pool). Self Certified mortgages allowed little or no formal verification of a borrower's declared income level provided that certain other criteria, (such as a low LTV) were met.
4. A degree of collateral concentration in the South East (39%) and in Greater London (19%).
5. The presence of a relatively high degree of non-commodity products within the portfolio. These include fresh start mortgages (2%), Self employed products (20%) and let properties (30%).
6. The relatively large loan size (3.7% of the pool represents loans in excess of £250,000)

Moody's believes that these factors are addressed by the substantial amount of credit enhancement present in the structure.

The loans originated by PML with a LTV in excess of 75% (approximately 10% of the pool) have the benefit of Mortgage Indemnity policies provided by Lloyd's of London. A substantial element of this policy is re-insured on a cut through basis by highly rated entities.

Many of the older loans originated by PFPLC at LTV's in excess of 75%, benefit from Mortgage Indemnity contracts from one of Sun Alliance Insurance Group (**Aa3**) or Legal and General Assurance Society Limited (**Aa1**). These cover approximately 24% of the pool.

Servicer

PFPLC is the servicer for the transaction. PFPLC currently employs approximately 360 staff in administering a mortgage portfolio of approximately £1.1bn for the Paragon Group and associated securitisation vehicles. It has substantial expertise in servicing non or partially performing mortgage assets. Paragon also has entered the consumer loan business in 1997 and administers a £10m portfolio. Barclays Bank PLC (**Aa2**) is the servicer of last resort.

The Paragon Group of Companies PLC was previously known as National Homeloans Holdings PLC, Paragon Finance PLC was previously The National Homeloans Corporation plc, and Paragon Mortgages Limited was known as Homeloans Direct Limited.

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