

## **FITCH AFFIRMS PARAGON MORTGAGE PLC SERIES; REVISES OUTLOOKS**

Fitch Ratings-London-19 January 2010: Fitch Ratings has today affirmed 27 tranches from four UK buy-to-let (BTL) RMBS and one 100% second-lien UK prime RMBS transaction, containing loans originated by The Paragon Group of Companies PLC (Paragon). The agency has also revised Outlooks on four tranches.

In line with other UK prime and BTL RMBS transactions, the Paragon BTL securitisation deals have shown signs of borrower performance deterioration through 2009, although not to a level that results in a change to the current ratings. One of the key supporting factors is that BTL lenders have a statutory right to have a receiver of rent appointed to collect rental payments directly from tenants. All of the Paragon transactions have seen an increase in the use of receiver of rent cases, and this has helped keep transaction cash flows stable, and limit the level of loans in arrears.

Fitch also believes that the effect of tighter lending criteria over the last year has helped support the BTL market as people have delayed purchasing their own property, strengthening tenant demand and maintaining upward pressure on rents. The rising rents and shorter void period have helped to ensure that arrears remain low compared to the rest of the mortgage market. The Paragon transactions are principally loans to professional landlords, and therefore these are the type of borrowers best placed to take advantage of the recent market conditions for rental properties.

In addition to the low arrears levels, until recently, the majority of these transactions had a sequential note pay-down structure, with non-amortising reserve funds. This allowed credit enhancement to build steadily, which supported the affirmations of the current ratings. However, despite the strong credit enhancement levels, Fitch has revised its Outlook on the junior notes to Stable from Positive for Paragon Mortgages (No.7) PLC and Paragon Mortgages (No.8) PLC. The revisions reflect the limited future growth of credit enhancement due to the possibility of a switch to pro-rata note pay-down, the effect of step-up margins limiting available revenue to cover losses and the negative outlook the agency maintains on the UK housing market as a whole.

Fitch notes that all reviewed transactions feature fully funded reserve funds, which would increase by trapping excess spread if certain arrears triggers were to be breached. Given the current strong performance of underlying collateral portfolios, these transactions are expected to be able to trap enough excess spread to increase their reserve funds to their new target level within a short time. Paragon has also provided these transactions with a subordinated loan facility. This facility would allow these transactions to make a drawing to cover interest shortfalls. Fitch has not given credit to this facility.

Paragon Secured Finance (No. 1) PLC, which comprises wholly second-lien loans, has current three months plus arrears totalling 7.88%. This has been an increase of 88bps since July 2009. Due to the rising level of arrears and concerns over adverse selection within the collateral portfolio and high realised losses, Fitch has kept its Outlook on Negative for the most junior, Class C tranche. The transaction features a fully funded reserve fund which would increase to 5.3% from 4.5% if the level of loans in arrears for more than three months exceeds 10% of the current balance. Should this occur Fitch believes the transaction is currently generating sufficient excess revenue to allow for the reserve to increase, although an increase in the level of arrears is likely to indicate an increase in future losses that may result in the reserve fund needing to be utilised. Along with the fully funded reserve fund, the underlying collateral portfolio has generated enough excess spread to cover losses realised to date. As of October 2009, transaction had 118bps of net excess spread to cover losses.

Rating actions are as follows:

Paragon Mortgages (No.7) PLC:

Class A1a (ISIN XS0193405890): affirmed at 'AAA'; Outlook Stable; assigned a Loss Severity

Rating of 'LS-1'

Class A1b (ISIN XS0193406195): affirmed at 'AAA'; Outlook Stable; assigned a Loss Severity Rating of 'LS-1'

Class A1c (ISIN XS0193406351): affirmed at 'AAA'; Outlook Stable; assigned a Loss Severity Rating of 'LS-1'

Class B1a (ISIN XS0193406435): affirmed at 'A'; Outlook revised to Stable from Positive; assigned a Loss Severity Rating of 'LS-2'

Class B1b (ISIN XS0193406609): affirmed at 'A'; Outlook revised to Stable from Positive; assigned a Loss Severity Rating of 'LS-2'

Paragon Mortgages (No.8) PLC:

Class A2a (ISIN XS0203410922): affirmed at 'AAA'; Outlook Stable; assigned a Loss Severity Rating of 'LS-1'

Class A2b (ISIN XS0203411144): affirmed at 'AAA'; Outlook Stable; assigned a Loss Severity Rating of 'LS-1'

Class B1a (ISIN XS0203411730): affirmed at 'A'; Outlook revised to Stable from Positive; assigned a Loss Severity Rating of 'LS-2'

Class B1b (ISIN XS0203412548): affirmed at 'A' ; Outlook revised to Stable from Positive; assigned a Loss Severity Rating of 'LS-2'

Paragon Mortgages (No.11) PLC:

Class A1 (ISIN XS0246900756): affirmed at 'AAA' / 'F1+'; Outlook Stable; assigned a Loss Severity Rating of 'LS-1'

Class A2a (ISIN XS0246902026): affirmed at 'AAA'; Outlook Stable; assigned a Loss Severity Rating of 'LS-1'

Class A2b (ISIN XS0246902885): affirmed at 'AAA'; Outlook Stable; assigned a Loss Severity Rating of 'LS-1'

Class B1a (ISIN XS0246904238): affirmed at 'AA'; Outlook Stable; assigned a Loss Severity Rating of 'LS-3'

Class B1b (ISIN XS0246905391): affirmed at 'AA'; Outlook Stable; assigned a Loss Severity Rating of 'LS-3'

Class C1b (ISIN XS0246905805): affirmed at 'A'; Outlook Stable; assigned a Loss Severity Rating of 'LS-3'

Class C1b currency swap obligation; affirmed at 'A'; Outlook Stable

Paragon Mortgages (No.13) PLC:

Class A1 (ISIN XS0272533935) affirmed at 'AAA'/F1+'; Outlook Stable; assigned a Loss Severity Rating of 'LS-1'

Class A2a (ISIN XS0272534313) affirmed at 'AAA'; Outlook Stable; assigned a Loss Severity Rating of 'LS-1'

Class A2b (ISIN XS0272534586) affirmed at 'AAA'; Outlook Stable; assigned a Loss Severity Rating of 'LS-1'

Class A2c (ISIN XS0272535393) affirmed at 'AAA'; Outlook Stable; assigned a Loss Severity Rating of 'LS-1'

Class B1a (ISIN XS0272535633) affirmed at 'AA'; Outlook Stable; assigned a Loss Severity Rating of 'LS-3'

Class B1b (ISIN XS0272536011) affirmed at 'AA'; Outlook Stable; assigned a Loss Severity Rating of 'LS-3'

Class C1a (ISIN XS0272536284) affirmed at 'A'; Outlook Stable; assigned a Loss Severity Rating of 'LS-3'

Class C1b (ISIN XS0272536524) affirmed at 'A'; Outlook Stable; assigned a Loss Severity Rating of 'LS-3'

Paragon Secured Finance (No.1) PLC:

Class A (ISIN XS0208202415): affirmed at 'AAA'; Outlook Stable; assigned a Loss Severity Rating of 'LS-2'

Class B (ISIN XS0208202688): affirmed at 'A'; Outlook Stable; assigned a Loss Severity Rating of 'LS-3'

Class C (ISIN XS0208202845): affirmed at 'BBB'; Outlook Negative; assigned a Loss Severity

## Rating of 'LS-3'

Fitch has employed its credit cover multiple methodology in reviewing the deals to assess the level of credit support available to each class of notes.

Applicable criteria 'EMEA RMBS Surveillance Criteria', dated 9 April 2009 and 'Global Structured Finance Rating Criteria', dated 30 September 2009 are available at [www.fitchratings.com](http://www.fitchratings.com).

Further commentary and performance data on the transaction are also available at [www.fitchratings.com](http://www.fitchratings.com).

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