

FITCH TAKES VARIOUS RATING ACTIONS ON PARAGON RMBS SERIES

Link to Fitch Ratings' Report: Fitch Takes Various Rating Actions On Paragon RMBS Series
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=745995

Fitch Ratings-London-09 April 2014: Fitch Ratings has taken various rating actions on 12 transactions originated by Paragon Mortgage Limited, Mortgage Trust Limited and Paragon Personal Finance Limited, all subsidiaries of The Paragon Group.

Fitch has upgraded two tranches, affirmed 61 along with six currency swap obligations of the 12 transactions Fitch has also revised the Outlooks on eight tranches and four currency swap obligations to Stable from Negative.

The series comprises 12 Paragon buy-to-let (BTL) deals (including Paragon 19) and one non-conforming RMBS transaction, Paragon Secured Finance (PSF1), which comprises 100% of second-charge loans. Paragon 19 which closed in March 2014 and was not considered in this annual review. A full list of rating actions is available at www.fitchratings.com or by clicking the link above.

KEY RATING DRIVERS

Continued Stable Arrears Performance for 11 BTL Transactions

The volume of loans in the three-month plus arrears buckets has remained stable in all 11 BTL transactions. As of the most recent interest payment dates, loans in arrears by more than three months ranged between 0.2% (Paragon 8) and 0.5% (Paragon 13) of the current portfolios for the Paragon transactions that closed prior to 2007. No arrears greater than three months have been reported for Paragon 16, 17 or 18, while the most recently closed Paragon 19 has not incurred an interest payment date yet.

Given the BTL nature of the underlying pools, borrowers in arrears by more than three months are predominantly managed by Paragon via its receiver of rent policy, where the full rental stream it receives from properties is diverted onto Paragon as administrator towards clearing arrears. Fitch acknowledges that Paragon's extensive use of its receiver of rent policy, currently ranging between 1.9% (Paragon 7) to 3.5% (Paragon 10) of the respective portfolios, has contributed towards the low level of arrears across the series. As performing loans under this policy are excluded from published arrears figures, the agency has increased its default probability assumptions on these performing loans to reflect the greater likelihood of such borrowers falling back into arrears, particularly in an increased interest rate environment.

Sufficient Credit Enhancement (CE) Levels

The steady build-up in CE, combined with the robust performance to date, has resulted in the upgrade of the B1a and B1b notes of Paragon 11 to 'AA+sf' from 'AAsf'. Additionally, the Outlooks on the junior notes of Paragon 11, 12, 13, 14 and 15 have been revised to Stable from Negative. This was supported by the low levels of cumulative losses across these transactions (between 0.33% and 0.65% of original principal balances) and the evident effectiveness of the Receiver of Rent mechanism that has resulted in the stable performance of these transactions.

Increased Quick Sale Adjustment (QSA) based On Loan Level Repossession Data

Based on the analysis of loan level repossession data previously provided by Paragon, the agency has applied an increased QSA of 36% compared with the standard criteria assumption of 22%. This has resulted in lower recovery rate assumptions being applied across the Paragon BTL RMBS series.

Stable Arrears Performance in Paragon Secured Finance 1

The affirmation of all notes of PSF1 is based on the stable performance over the past year. As of January 2014, loans in arrears by more than three months stood at 10.9% of the current outstanding portfolio, compared with 10.4% a year ago. Additionally, the transaction's structure allows for the full provisioning of defaulted loans (defined as loans in arrears by more than 12 months). At present, robust levels of annualised excess spread, standing at 6.4% of the outstanding collateral balance, have enabled the issuer to comfortably clear defaults, without having to draw on its reserve fund. The high principal prepayment rate, averaging an annualised 14.36% over the past year (and 23.86% over the lifetime of the transaction) has led to a significant increase in credit enhancement levels. Fitch believes that the credit support available to the rated notes, coupled with robust excess spread levels continue to offset the relatively high levels of arrears and higher losses incurred on these second-lien loans, which is why the ratings have been affirmed.

RATING SENSITIVITIES

A moderate rise in interest rates could lead to a rise in loans in arrears greater than three months and potentially an increase in defaults. Additionally, a decrease in future house prices could exacerbate a decline in recovery rates.

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Sources of Information:

Investor and Servicer Reports, as well as loan-by-loan level data provided by the Paragon group.

Fitch's analysis of Representations, Warranties & Enforcement Mechanisms (RWEs) for transactions rated on or after 26 September 2011, can be found in the appendixes of new issue reports for the respective transaction. In addition see "Representations, Warranties, and Enforcement Mechanisms in Global Structured Finance Transactions" dated 17 April 2012 at www.fitchratings.com. A

comparison of the transaction's RW&Es to those typical for that asset class is available by accessing the presale or new issue reports.

Applicable criteria, 'EMEA Residential Mortgage Loss Criteria' dated 6 June 2013, 'EMEA Residential Mortgage Loss Criteria Addendum - United Kingdom' dated 9 August 2012, 'Exposure Draft: EMEA Criteria Addendum - United Kingdom' Dated 25 March 2014, 'Counterparty Criteria for Structured Finance Transactions' and 'Counterparty Criteria for Structured Finance Transactions: Derivative Addendum', dated 13 May 2013 and 'Global Structured Finance Rating Criteria' dated 24 May 2013 are available at www.fitchratings.com.

Applicable Criteria and Related Research:

Exposure Draft: EMEA Criteria Addendum – UK - Amended

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=710741

EMEA Residential Mortgage Loss Criteria

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=709915

EMEA Criteria Addendum - United Kingdom - Mortgage and Cashflow Assumptions

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=685433

Counterparty Criteria for Structured Finance and Covered Bonds

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=707155

Counterparty Criteria for Structured Finance and Covered Bonds: Derivative Addendum

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=707156

Global Structured Finance Rating Criteria

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=708661

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