

**Rating Action: Moody's takes multiple actions on Paragon Mortgages (No. 9), (No.11), (No.12) PLC**

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Global Credit Research - 06 May 2014

London, 06 May 2014 -- Moody's Investors Service has today downgraded 5 notes and confirmed 2 notes in Paragon Mortgages (No. 9) PLC (Paragon 9). Moody's has further placed the 5 downgraded notes in Paragon 9 on review with rating direction uncertain. All notes in Paragon Mortgages (No. 11) PLC (Paragon 11), and Paragon Mortgages (No. 12) PLC (Paragon 12) remain on review for downgrade. Swap counterparty exposure has prompted today's action.

Moody's placed all notes in all three transactions on review for downgrade in relation to swap counterparty exposure on 14 November 2013 following the introduction of the rating agency's updated approach to assessing swap counterparty linkage in structured finance transactions ([https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBS\\_SF344857](https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBS_SF344857)).

For a detailed list of affected ratings, see towards the end of the press release before the regulatory disclosures section.

**RATINGS RATIONALE**

Today's rating actions reflect the impact on the three transactions of their exposure to the Royal Bank of Scotland plc (RBS rated Baa1/P-2) in the case of Paragon 9 and Barclays Bank PLC (Barclays, A2/P-1) in the case of Paragon 11 and Paragon 12 as their currency swap counterparties. The rating actions follow the introduction of Moody's updated approach to assessing swap counterparty linkage in structured finance cash flow transactions ("Approach to Assessing Swap Counterparties in Structured Finance Cash Flow Transactions", published 12 November 2013).

-- Paragon 9

As part of its review, Moody's incorporated the risks of additional losses on the notes in the event of them becoming unhedged following a swap counterparty default. RBS (Baa1/P-2) is the currency swap counterparty in this transaction.

Moody's concludes that the current ratings on Classes Aa, Ab, Ac, Ba and Bb are affected by the exposure to RBS as swap counterparty which is not mitigated through available credit enhancements. Their ratings are consequently downgraded to Aa1 (sf), Aa1 (sf), Aa1 (sf), A1 (sf) and A1 (sf) respectively. The downgrade of RBS's long-term rating to Baa1 from A3 on 13 March 2014 resulted in a rating event under the swap agreement. Remedial actions resulting in a significant reduction in swap counterparty risk, such as a transfer to or a guarantee from a highly rated entity, could result in an upgrade to the Classes Aa, Ab, Ac, Ba and Bb notes. However, lack of remedial actions can result in a further downgrade of the notes. For this reason, Moody's has decided to place the Classes Aa, Ab, Ac, Ba and Bb notes on review with rating direction uncertain.

Moody's concluded that the credit enhancement available to Classes Ca and Cb mitigates the swap counterparty risks. As a result, their ratings are both confirmed at A2 (sf).

-- Paragon 11 and Paragon 12

Moody's incorporated the risks of additional losses on the notes in the event of them becoming unhedged following a swap counterparty default. Barclays (A2/P-1), the currency swap counterparty in both transactions, has communicated to Moody's its intention to restructure the currency swaps. As part of its review, Moody's has taken into consideration Barclays' swap restructuring proposal, and gives partial benefit to this restructuring until it is fully executed.

Moody's concluded that the credit enhancement available to all classes of notes in Paragon 11 and Paragon 12 mitigates the swap counterparty risks in a scenario that Barclays fully implements its swap restructuring proposal. Moody's maintains that all notes in Paragon 11 and Paragon 12 remain on review for downgrade pending final execution of the swap restructuring.

## UPDATE TO TRANSACTION ASSUMPTIONS

During this review, Moody's conducted a detailed loan-by-loan analysis and transaction performance review of all three transactions. All three transactions are performing in line with Moody's current expected loss assumptions. Borrower concentration in Paragon 11 improved since closing. As a result, Moody's reduced MILAN in Paragon 11 from 19.48% to 17.50%.

## FACTORS THAT WOULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS:

Upward pressure on the ratings could result from (1) better-than-expected performance of the underlying assets; (2) implementation of remedial actions in paragon 9 or restructuring in paragon 11 and 12 that could fully mitigate the swap counterparty risk ; and (3) a decline in counterparty risk or country risk.

Downward pressure on the ratings could result from (1) worse-than-expected performance of the underlying collateral; (2) failure to properly implement remedial actions in paragon 9 or restructuring in paragon 11 and 12 that could mitigate the swap counterparty risk; and (3) deterioration in the counterparties' credit quality or a rise in country risk.

The principal methodology used in these ratings was "Moody's Approach to Rating RMBS Using the MILAN Framework" published in March 2014. Please see the Credit Policy page on [www.moody.com](http://www.moody.com) for a copy of this methodology.

## LIST OF AFFECTED RATINGS:

Issuer: Paragon Mortgages (No. 9) PLC

....GBP 346M Aa Notes, Downgraded to Aa1 (sf) and Placed Under Review Direction Uncertain; previously on Nov 14, 2013 Aaa (sf) Placed Under Review for Possible Downgrade

....EUR 355M Ab Notes, Downgraded to Aa1 (sf) and Placed Under Review Direction Uncertain; previously on Nov 14, 2013 Aaa (sf) Placed Under Review for Possible Downgrade

....US\$ 60M Ac Notes, Downgraded to Aa1 (sf) and Placed Under Review Direction Uncertain; previously on Nov 14, 2013 Aaa (sf) Placed Under Review for Possible Downgrade

....GBP 7M Ba Notes, Downgraded to A1 (sf) and Placed Under Review Direction Uncertain; previously on Nov 14, 2013 Aa3 (sf) Placed Under Review for Possible Downgrade

....EUR 29.5M Bb Notes, Downgraded to A1 (sf) and Placed Under Review Direction Uncertain; previously on Nov 14, 2013 Aa3 (sf) Placed Under Review for Possible Downgrade

....GBP 3M Ca Notes, Confirmed at A2 (sf); previously on Nov 14, 2013 A2 (sf) Placed Under Review for Possible Downgrade

....EUR 66M Cb Notes, Confirmed at A2 (sf); previously on Nov 14, 2013 A2 (sf) Placed Under Review for Possible Downgrade

Issuer: Paragon Mortgages (No. 11) PLC

....US\$ 985M A1 Notes, Aaa (sf) Remains On Review for Possible Downgrade; previously on Nov 14, 2013 Aaa (sf) Placed Under Review for Possible Downgrade

....GBP 149.5M A2a Notes, Aaa (sf) Remains On Review for Possible Downgrade; previously on Nov 14, 2013 Aaa (sf) Placed Under Review for Possible Downgrade

....EUR 219.7M A2b Notes, Aaa (sf) Remains On Review for Possible Downgrade; previously on Nov 14, 2013 Aaa (sf) Placed Under Review for Possible Downgrade

....GBP 16M B1a Notes, Aa2 (sf) Remains On Review for Possible Downgrade; previously on Nov 14, 2013 Aa2 (sf) Placed Under Review for Possible Downgrade

....EUR 82.4M B1b Notes, Aa2 (sf) Remains On Review for Possible Downgrade; previously on Nov 14, 2013 Aa2 (sf) Placed Under Review for Possible Downgrade

...EUR 87.5M C1b Notes, A2 (sf) Remains On Review for Possible Downgrade; previously on Nov 14, 2013 A2 (sf) Placed Under Review for Possible Downgrade

Issuer: Paragon Mortgages (No. 12) PLC

...US\$ 1500M A1 Notes, Aaa (sf) Remains On Review for Possible Downgrade; previously on Nov 14, 2013 Aaa (sf) Placed Under Review for Possible Downgrade

...GBP 145M A2a Notes, Aaa (sf) Remains On Review for Possible Downgrade; previously on Nov 14, 2013 Aaa (sf) Placed Under Review for Possible Downgrade

...EUR 245M A2b Notes, Aaa (sf) Remains On Review for Possible Downgrade; previously on Nov 14, 2013 Aaa (sf) Placed Under Review for Possible Downgrade

...US\$ 311M A2c Notes, Aaa (sf) Remains On Review for Possible Downgrade; previously on Nov 14, 2013 Aaa (sf) Placed Under Review for Possible Downgrade

...GBP 25M B1a Notes, Aa2 (sf) Remains On Review for Possible Downgrade; previously on Nov 14, 2013 Aa2 (sf) Placed Under Review for Possible Downgrade

...EUR 126M B1b Notes, Aa2 (sf) Remains On Review for Possible Downgrade; previously on Nov 14, 2013 Aa2 (sf) Placed Under Review for Possible Downgrade

...GBP 17M C1a Notes, A2 (sf) Remains On Review for Possible Downgrade; previously on Nov 14, 2013 A2 (sf) Placed Under Review for Possible Downgrade

...EUR 106M C1b Notes, A2 (sf) Remains On Review for Possible Downgrade; previously on Nov 14, 2013 A2 (sf) Placed Under Review for Possible Downgrade

## REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions of the disclosure form.

Moody's did not receive or take into account a third-party assessment on the due diligence performed regarding the underlying assets or financial instruments related to the monitoring of these transactions in the past six months.

The analysis relies on an assessment of collateral characteristics to determine the collateral loss distribution, that is, the function that correlates to an assumption about the likelihood of occurrence to each level of possible losses in the collateral. As a second step, Moody's evaluates each possible collateral loss scenario using a model that replicates the relevant structural features to derive payments and therefore the ultimate potential losses for each rated instrument. The loss a rated instrument incurs in each collateral loss scenario, weighted by assumptions about the likelihood of events in that scenario occurring, results in the expected loss of the rated instrument.

As the section on loss and cash flow analysis describes, Moody's quantitative analysis entails an evaluation of scenarios that stress factors contributing to sensitivity of ratings and take into account the likelihood of severe collateral losses or impaired cash flows. Moody's weights the impact on the rated instruments based on its assumptions of the likelihood of the events in such scenarios occurring.

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