



Fitch Affirms Paragon Mortgages No. 14 and 15; Outlook Stable

Fitch Ratings-London-14 March 2018: Fitch Ratings has affirmed Paragon Mortgages No. 14 and 15 and revised the Outlook on the class C notes to Stable from Positive.

The Paragon Mortgages No. 14 and 15 are buy-to-let (BTL) RMBS transactions backed by loans originated between 2006 and 2007 by Paragon Mortgage Limited and Mortgage Trust Limited, all subsidiaries of The Paragon Group.

Fitch's Criteria for Rating Currency Swap Obligations of an SPV in Structured Finance Transactions and Covered Bonds expects that a rating action with respect to a note tranche results in a corresponding rating action with respect to the related rated swap obligations.

KEY RATING DRIVERS

Stable Asset Performance

Loans with more than three unpaid monthly instalments have remained stable over the 12 months prior to the last reporting dates, standing at 0.06% and 0.13% (Paragon 14 and 15, respectively) of the current portfolio balance. 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 is diverted to Paragon, as administrator, and used towards clearing arrears. Paragon's extensive use of its receiver of rent policy has therefore contributed towards the low level of delinquencies across the series.

Sufficient Credit Enhancement

The stable asset performance together with non-amortising reserve fund and sequential notes amortisation has contributed to a steady build-up of credit enhancement. Fitch considers the available CE as sufficient to maintain the ratings, as reflected in the affirmations.

BTL Interest-Only Concentration

In both transactions 97.6% of the pool is made up of interest-only loans with more than 50% maturity concentration spikes between 2030 and 2032. Interest-only loans bring additional tail risk to transactions especially on the most junior notes. However, this risk is mitigated since the notes maturity date is seven years after the peaks of interest-only maturity concentration. Nevertheless, the negative

outlook for the BTL sector leaves some concerns around the overall future performance of BTL mortgages.

Low Excess Spread

The excess spread for both transactions is low (around 1%) and both transactions' structures are more sensitive to back-loaded defaults and high prepayment scenarios. High prepayments in UK deals usually materialise in the first two to five years of the transaction when loans revert from fixed rate to floating rate. The two transactions are highly seasoned (11 years since close) and prepayments have stabilised at lower levels of around 5%.

Stressed Quick Sale Adjustment Assumptions

Based on the analysis of loan level data provided by Paragon on properties taken into possession and sold, the agency applied a quick sale adjustment (average 34.3%) higher than the criteria assumption (29.9%). Fitch's analysis showed that the credit enhancement was sufficient to withstand the lower recoveries.

Class C Outlooks

The class C notes' ratings for both transactions could potentially be constrained by the ratings of the account bank provider (Barclays Bank Plc A/Rating Watch Positive/F1) due to the reserve fund providing the only source of credit enhancement. Model-implied ratings lead us to affirm the ratings and revise the Outlook to Stable from Positive.

RATING SENSITIVITIES

The UK asset performance outlook for BTL mortgages is negative due to the impact of tighter affordability tests introduced in 2017 and due to Brexit uncertainty causing concerns about future rental growth for the main BTL hotspots (London and southeast England), and the performance of BTL mortgages overall. Paragon Mortgages No. 14 and 15 pools are 100% BTL and could be impacted by changes in the market conditions and economic environment.

Fitch analysed the impact of negative payments being payable within the cross currency swap agreements. If EURIBOR decreases to the extent the all in rate payable by the swap counterparty is negative, the issuer is expected to pay this amount to the swap counterparty. Fitch's analysis showed the impact on the note ratings to be immaterial.

USE OF THIRD-PARTY DUE DILIGENCE PURSUANT TO RULE 17G-10

Form ABS Due Diligence-15E was not provided to, or reviewed by, Fitch in relation to this rating action.

DATA ADEQUACY

Fitch has checked the consistency and plausibility of the information it has received about the performance of the asset pools and the transactions. There were no findings that affected the rating analysis. Fitch has not reviewed the results of any third-party assessment of the asset portfolio information or conducted a review of origination files as part of its ongoing monitoring.

Fitch did not undertake a review of the information provided about the underlying asset pools ahead of the transactions' initial closing. The subsequent performance of the transactions over the years is consistent with the agency's expectations given the operating environment and Fitch is therefore satisfied that the asset pool information relied upon for its initial rating analysis was adequately reliable.

Overall and together with the assumptions referred to above, Fitch's assessment of the information relied upon for the agency's rating analysis according to its applicable rating methodologies indicates that it is adequately reliable.

SOURCES OF INFORMATION

The information below was used in the analysis.

- Loan-by-loan data provided by Paragon Finance plc as at 30 November 2017
- Transaction reporting provided by Paragon Finance plc as at 30 November 2017
- Updates from the servicer dated 09 March 2018

MODELS

ResiEMEA

ResiEMEA. (<https://www.fitchratings.com/site/structuredfinance/rmbs/resiemea>)

EMEA RMBS Surveillance Model

EMEA RMBS Surveillance Model.

(<https://www.fitchratings.com/site/structuredfinance/rmbs/emearsm>)

EMEA CashFlow Model

EMEA Cash Flow Model.

(<https://www.fitchratings.com/site/structuredfinance/emeacfm>)

The rating actions are as follows:

Paragon Mortgages No. 14 plc

Class A1 affirmed at 'AAAsf'; Outlook Stable

Class A2a affirmed at 'AAAsf'; Outlook Stable

Class A2b affirmed at 'AAAsf'; Outlook Stable

Class A2c affirmed at 'AAAsf'; Outlook Stable

Class B1a affirmed at 'AAAsf'; Outlook Stable

Class B1b affirmed at 'AAAsf'; Outlook Stable

Class C1a affirmed at 'A-sf'; Outlook revised to Stable from Positive

Class C1b affirmed at 'A-sf'; Outlook revised to Stable from Positive

Class C1b - CSO affirmed at 'A-sf'; Outlook revised to Stable from Positive

Paragon Mortgages No. 15 plc

Class A1 affirmed at 'AAAsf'; Outlook Stable

Class A2a affirmed at 'AAAsf'; Outlook Stable

Class A2b affirmed at 'AAAsf'; Outlook Stable

Class A2c affirmed at 'AAAsf'; Outlook Stable

Class B1a affirmed at 'AAAsf'; Outlook Stable

Class B1b affirmed at 'AAAsf'; Outlook Stable

Class C1b affirmed at 'BBB+sf'; Outlook revised to Stable from Positive

Class C1b - CSO affirmed at 'BBB+sf'; Outlook revised to Stable from Positive

Contacts:

Lead Surveillance Analyst

Henrik Nilsson

Associate Director

+44 20 3530 1738

Fitch Ratings Limited

30 North Colonnade

London E14 5GN

Committee Chairperson

Robbie Sargent

Senior Director

+44 20 3530 1404

Media Relations: Athos Larkou, London, Tel: +44 203 530 1549, Email:
athos.larkou@fitchratings.com

Additional information is available on www.fitchratings.com

Applicable Criteria

Criteria for Rating Currency Swap Obligations of an SPV in Structured Finance Transactions and Covered Bonds (pub. 11 Aug 2016)

(<https://www.fitchratings.com/site/re/885925>)

EMEA RMBS Rating Criteria (pub. 27 Oct 2017)

(<https://www.fitchratings.com/site/re/905358>)

Fitch's Interest Rate Stress Assumptions for Structured Finance and Covered Bonds - Excel File (pub. 02 Feb 2018)

(<https://www.fitchratings.com/site/re/10018863>)

Global Structured Finance Rating Criteria (pub. 03 May 2017)

(<https://www.fitchratings.com/site/re/897411>)

Structured Finance and Covered Bonds Counterparty Rating Criteria (pub. 23 May 2017) (<https://www.fitchratings.com/site/re/898537>)

Structured Finance and Covered Bonds Counterparty Rating Criteria: Derivative Addendum (pub. 23 May 2017) (<https://www.fitchratings.com/site/re/898538>)

Structured Finance and Covered Bonds Country Risk Rating Criteria (pub. 18 Sep 2017) (<https://www.fitchratings.com/site/re/903496>)

Structured Finance and Covered Bonds Interest Rate Stresses Rating Criteria (pub. 02 Feb 2018) (<https://www.fitchratings.com/site/re/10018549>)

UK Residential Mortgage Rating Criteria Addendum - Residential Mortgage Assumptions (pub. 08 Dec 2017) (<https://www.fitchratings.com/site/re/905920>)

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(<https://www.fitchratings.com/site/dodd-frank-disclosure/10023580>)

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