



RATING ACTION COMMENTARY

Fitch Upgrades Paragon Mortgages (No. 27) and Paragon Mortgages (No. 28)

Tue 12 Oct, 2021 - 4:53 PM ET

Fitch Ratings - London - 12 Oct 2021: Fitch Ratings has upgraded Paragon Mortgages (No. 27) PLC (Paragon 27), except the class A notes, and Paragon Mortgages (No. 28) PLC (Paragon 28), except the class A and D notes. Paragon 27 class C and D notes have been removed from Rating Watch Positive (RWP).

RATING ACTIONS

ENTITY/DEBT	RATING			PRIOR
Paragon Mortgages (No. 27) plc				
● A XS2132036737	LT	AAAsf Rating Outlook Stable	Affirmed	AAAsf Rating Outlook Stable
● B XS2132137337	LT	AA+sf Rating Outlook Stable	Upgrade	AAsf Rating Outlook Stable
● C XS2132137410	LT	A+sf Rating Outlook Stable	Upgrade	Asf Rating Watch Positive

ENTITY/DEBT **RATING**
[VIEW ADDITIONAL RATING DETAILS](#)

PRIOR



TRANSACTION SUMMARY

The transactions are the 27th and 28th from the Paragon series consisting of buy-to-let (BTL) mortgages originated by Paragon Mortgages (2010) Limited, Paragon Bank plc and other members of the Paragon Banking Group.

KEY RATING DRIVERS

Stable Asset Performance: Asset performance has remained strong, with arrears by more than one monthly payment at 0.15% (Paragon 27) and 0% (Paragon 28) as of 30 June 2021 and 31 August 2021, respectively. Given the BTL nature of the underlying pool, borrowers in arrears by more than two 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. Prepayments for both transactions have not peaked at as high levels as previous Paragon transactions, as the pools are still mostly on a fixed rate.

Off RWP: Fitch placed the class C and D notes of Paragon 27 on RWP following the retirement of its coronavirus-related additional stress analysis scenario (see 'Fitch Retires UK and European RMBS Coronavirus Additional Stress Scenario Analysis, except for UK Non-Conforming'). Fitch has retired its additional stress scenario analysis applied in conjunction with its UK RMBS Rating Criteria for UK BTL pools, resulting in improved foreclosure frequency (FF). Together with the accumulated credit enhancement and stable asset performance, this has led to today's upgrades.

Interest Rate Mismatch Hedged: As of the latest payment dates, 99.5% (Paragon 27) and 100% (Paragon 28) of the pool pays a fixed rate of interest (reverting to Paragon's standard variable rate (SVR) or discounted SVR), while the notes pay a SONIA-linked floating rate. The issuer entered a swap at closing to mitigate the interest rate risk arising from the fixed-rate mortgages in the pool. The swap features a defined notional balance that was derived to reflect the interest rate reset dates of the mortgage pool.

Product Switches: While switches in the repayment types are limited, before the step-up date there are only minor limitations on potential switches regarding any interest rate conversions. Fitch has therefore modelled extensive use of the interest rate conversions to stress any excess spread in the asset portfolio and hedging interest rate mismatches.

Desktop Valuation Adjustment: Paragon 28 pool includes 9.5% of properties valued at origination through a desktop valuation during in the first 2020 lockdown when physical valuations were not allowed. A desktop valuation process was conducted by Paragon's in-house team of regional surveyors, restricted to a limited number of non-complex properties with up to four tenants sharing. Fitch notes that a rigorous process has been put in place and that desktop valuations have only been applied to a minority of the total originations, representing a limited number of cases. For this reason, Fitch has applied a 0% adjustment to the desktop valuations in this pool (instead of the 5% standard adjustment) in line with its criteria.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to negative rating action/downgrade:

The transactions' performance may be affected by changes in market conditions and economic environment. Weakening economic performance is strongly correlated to increasing levels of delinquencies and defaults that could reduce credit enhancement available to the notes.

Additionally, unanticipated declines in recoveries could also result in lower net proceeds, which may make certain note ratings susceptible to negative rating action, depending on the extent of the decline in recoveries. Fitch conducts sensitivity analyses by stressing both a transaction's base-case FF and recovery rate (RR) assumptions, and examining the rating implications for all classes of issued notes. Fitch tested a sensitivity scenario by applying 15% increase in the weighted average (WA) FF and a 15% decrease in the WARR. The results indicated downgrades of up to two notches for both transactions.

Factors that could, individually or collectively, lead to positive rating action/upgrade:

Stable to improved asset performance driven by stable delinquencies and defaults would lead to increasing credit enhancement levels and, potentially, upgrades. A decrease in the WAFF of 15% and an increase in the WARR of 15% indicate upgrades of up to two notches for both transactions.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Structured Finance transactions have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of seven notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of seven notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from

'AAAsf' to 'Dsf'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>.

USE OF THIRD PARTY DUE DILIGENCE PURSUANT TO SEC 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. 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.

Prior to the transactions' closing, Fitch reviewed the results of a third-party assessment conducted on the asset portfolio information and concluded that there were no findings that affected the rating analysis.

Overall, and together with any 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.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entities, either due to their nature or the way in which they are being managed by the entities. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

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APPLICABLE CRITERIA

[Structured Finance and Covered Bonds Counterparty Rating Criteria \(pub. 29 Jan 2020\)](#)

[Structured Finance and Covered Bonds Counterparty Rating Criteria: Derivative Addendum \(pub. 29 Jan 2020\)](#)

[Structured Finance and Covered Bonds Country Risk Rating Criteria \(pub. 23 Sep 2020\)](#)

[Global Structured Finance Rating Criteria \(pub. 24 Mar 2021\) \(including rating assumption sensitivity\)](#)

[Structured Finance and Covered Bonds Interest Rate Stresses Rating Criteria \(pub. 20 Sep 2021\)](#)

[UK RMBS Rating Criteria \(pub. 23 Sep 2021\) \(including rating assumption sensitivity\)](#)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Multi-Asset Cash Flow Model, v2.11.0 (1)

ResiGlobal Model: UK, v1.3.2 (1)

ADDITIONAL DISCLOSURES

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UK Issued, EU Endorsed

Paragon Mortgages (No. 28) PLC

UK Issued, EU Endorsed

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Structured Finance Structured Finance: RMBS Europe United Kingdom
