

paragon



## Full-year results

12 months ended 30 September 2011

The Paragon Group of Companies PLC

# Agenda

Section 1

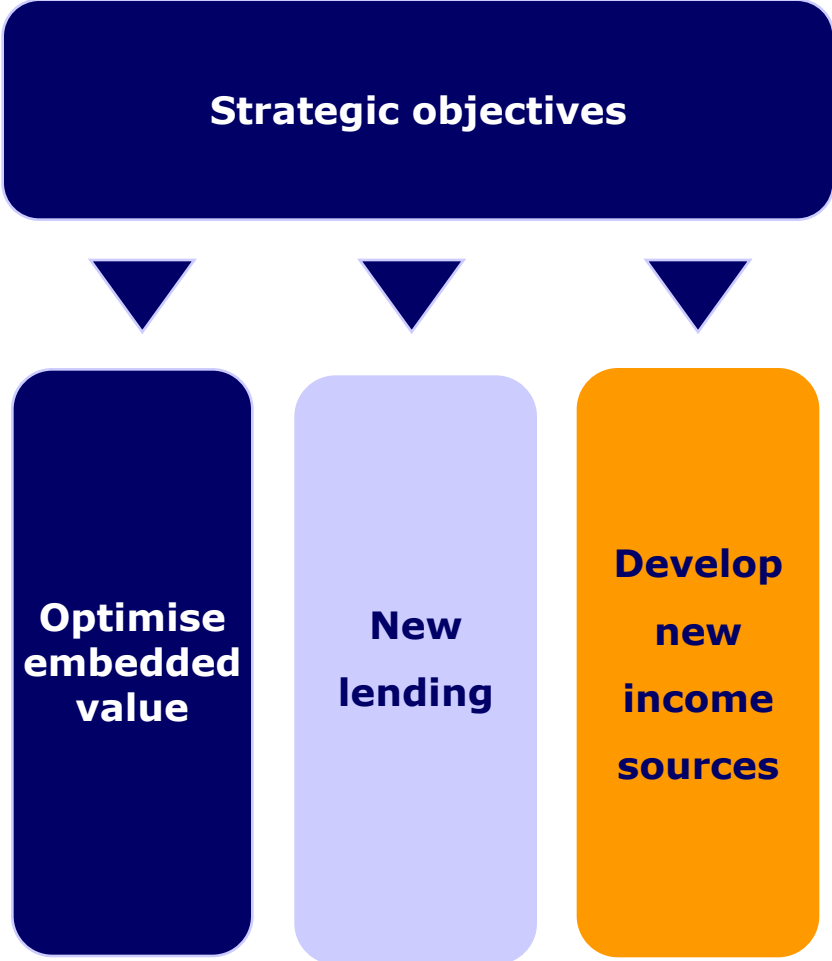
Financial results

Section 2

Strategy

# Highlights

- Strong financial performance with considerable progress on strategic developments
  - Profits up 22.7%
  - Strong credit performance
  - Strong customer retention
  - New investments in portfolios
  - New servicing contracts
  - New lending re-established
  - First securitisation since 2007
- Well positioned for further growth, despite environment uncertainties





## **Financial results**

12 months to 30 September 2011

# Financial highlights

	2010 £m	2011 £m	% change
Pre-tax profit	71.8	<b>80.8</b>	12.5%
Of which:			
Exceptionals	5.7	<b>0.0</b>	
Fair value	0.0	<b>(0.3)</b>	
Underlying profit	66.1	<b>81.1</b>	22.7%
Tax rate	24.9%	<b>26.2%</b>	
Dividend per share (total)	3.6p	<b>4.0p</b>	11.1%
Earnings per share	18.3p	<b>20.2p</b>	10.4%
Shareholder funds @ 30 September	692.0	<b>742.0</b>	7.2%

# FY:FY analysis

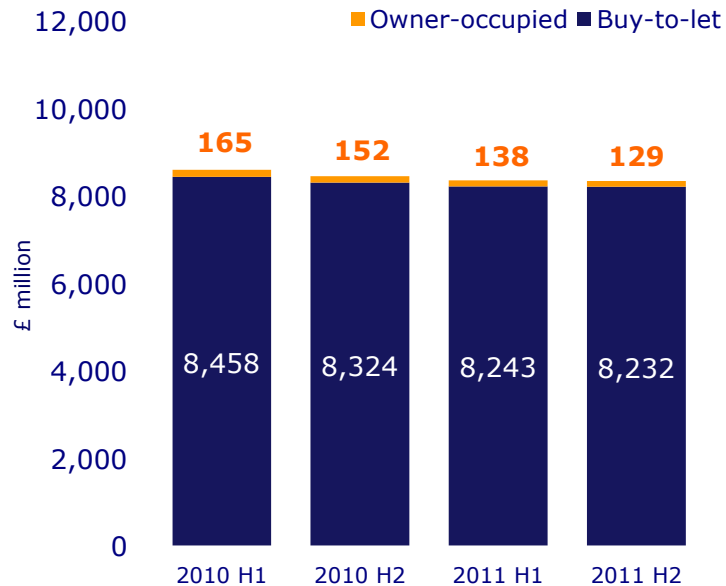
	2010 £m	2011 £m	% change
Income	147.9	150.9	2.0%
Expenses	(42.6)	(45.4)	6.6%
Impairments	(39.2)	(24.4)	(37.8%)
Cost:income	28.8%	30.1%	
Underlying profit	<b>66.1</b>	<b>81.1</b>	22.7%

# Half-year progression

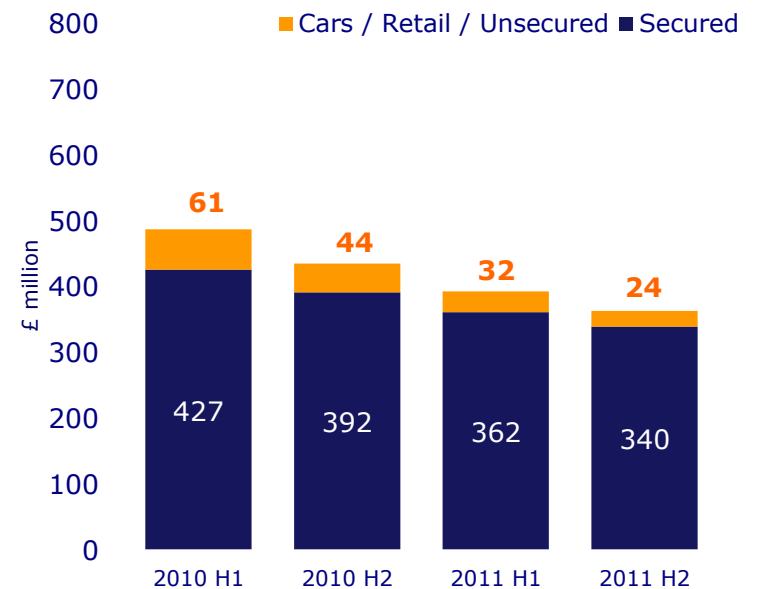
	H1 2010 £m	H2 2010 £m	H1 2011 £m	H2 2011 £m	2010:H2 – 2011:H2 % change
Income	77.4	70.5	74.5	76.4	8.4%
Expenses	(21.0)	(21.6)	(22.8)	(22.6)	4.6%
Impairments	(26.7)	(12.5)	(13.3)	(11.1)	(11.2%)
Cost:income	27.1%	30.6%	30.6%	29.6%	
<b>Underlying profit</b>	<b>29.7</b>	<b>36.4</b>	<b>38.4</b>	<b>42.7</b>	<b>17.3%</b>

# Segmental loan assets

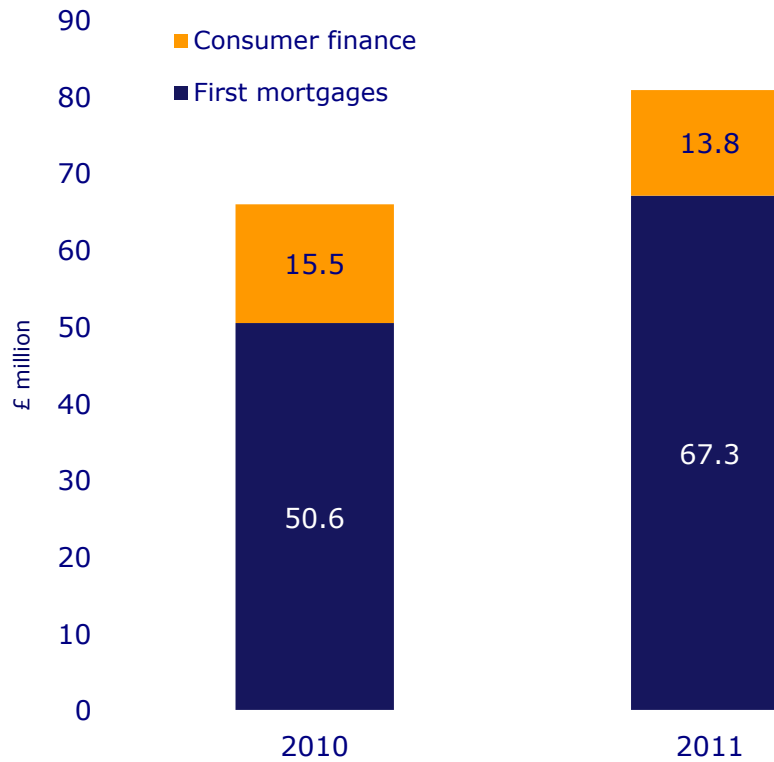
## First mortgages



## Consumer finance



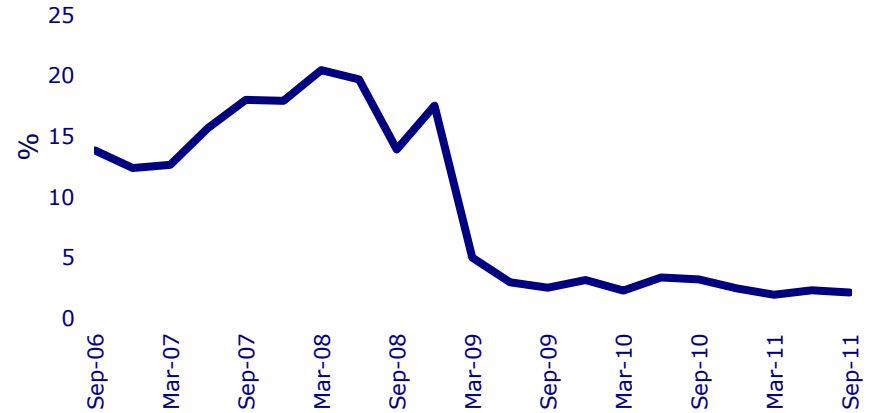
# Segmental profit analysis



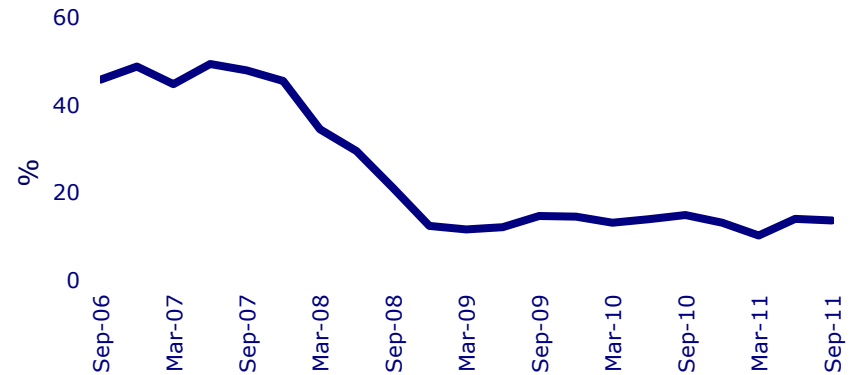
# Customer retention

- Redemption rates remain low and stable
- Strong tenant demand
- Rents continue to rise
- Landlords retain long-term investment horizon
- Product availability remains restricted

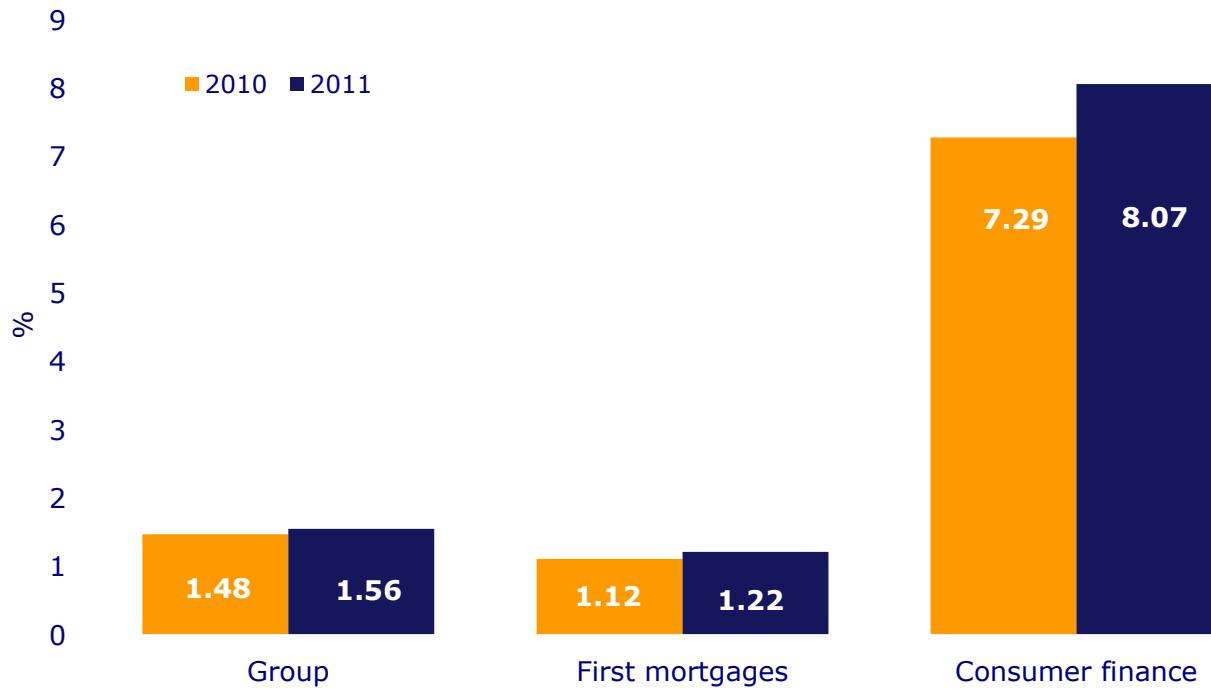
### Paragon buy-to-let redemption rate



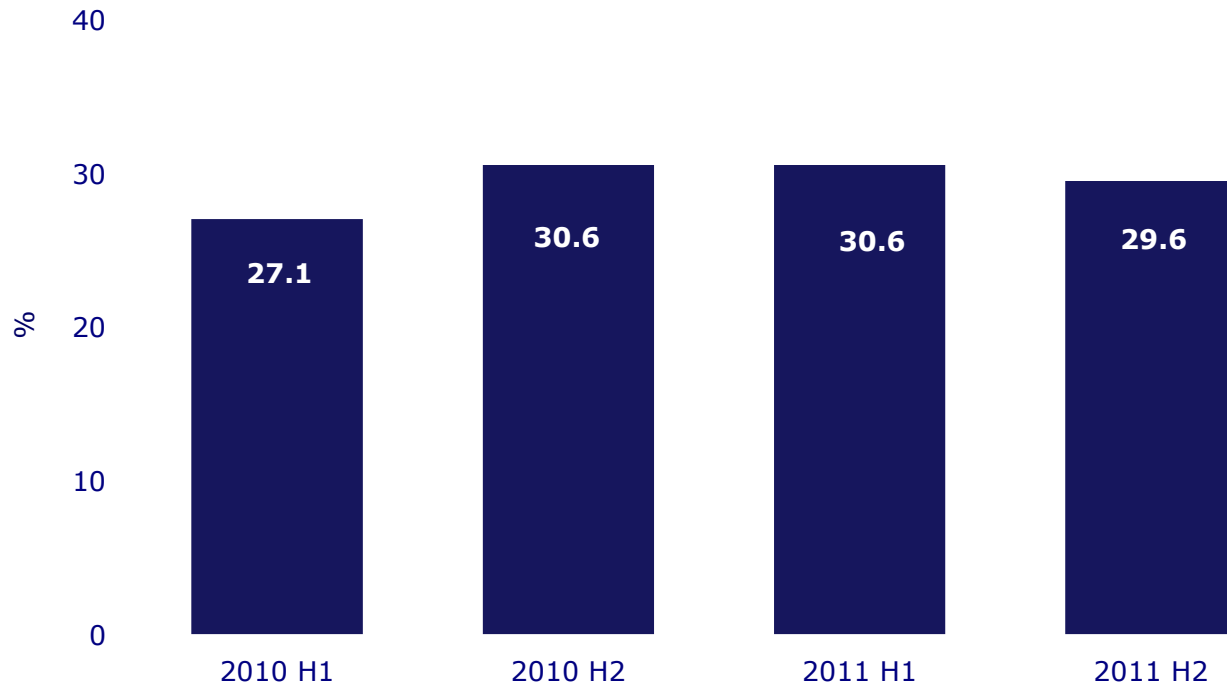
### Paragon secured redemption rate



# Net interest margin

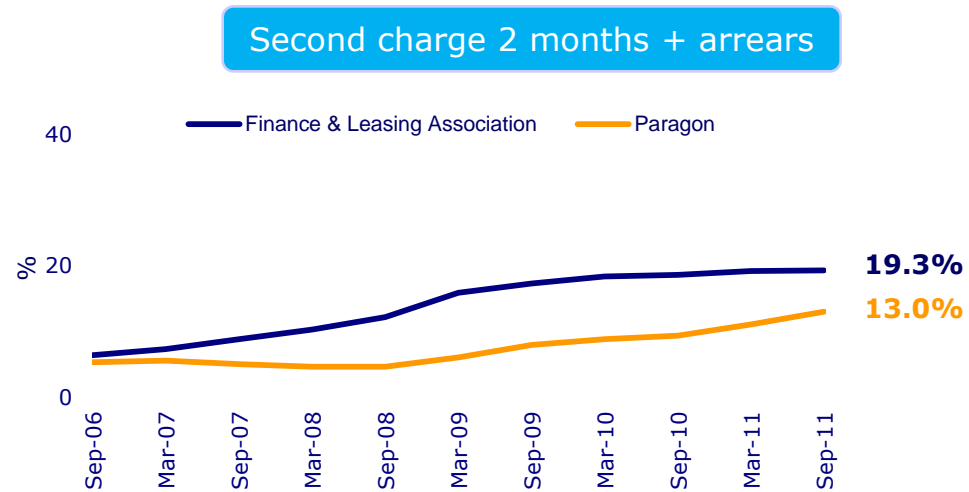
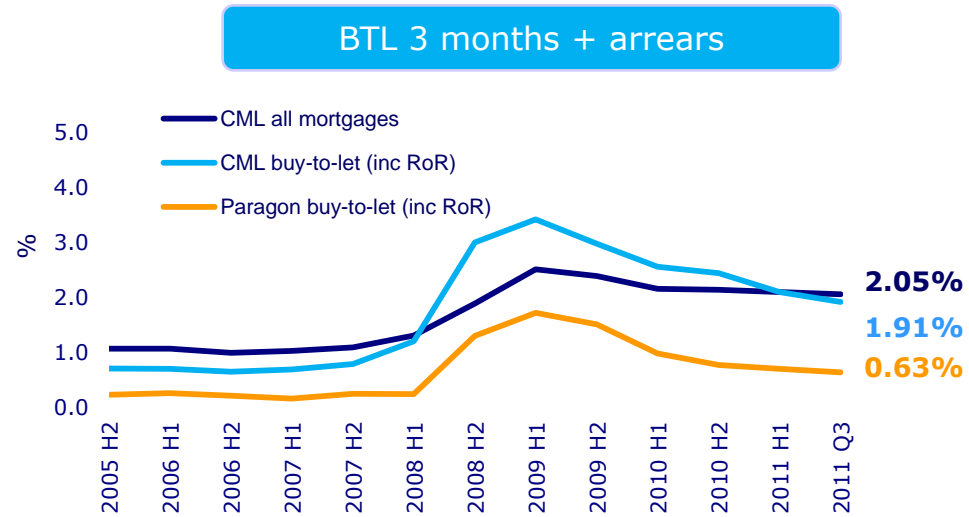


# Cost:income ratio



# Credit quality

- Paragon assets significantly outperform wider industry
  - Buy-to-let 3 months + arrears fell to 63 bps
- Second charge arrears cash collections remain strong
  - 76% average RvD on 2 months + arrears accounts



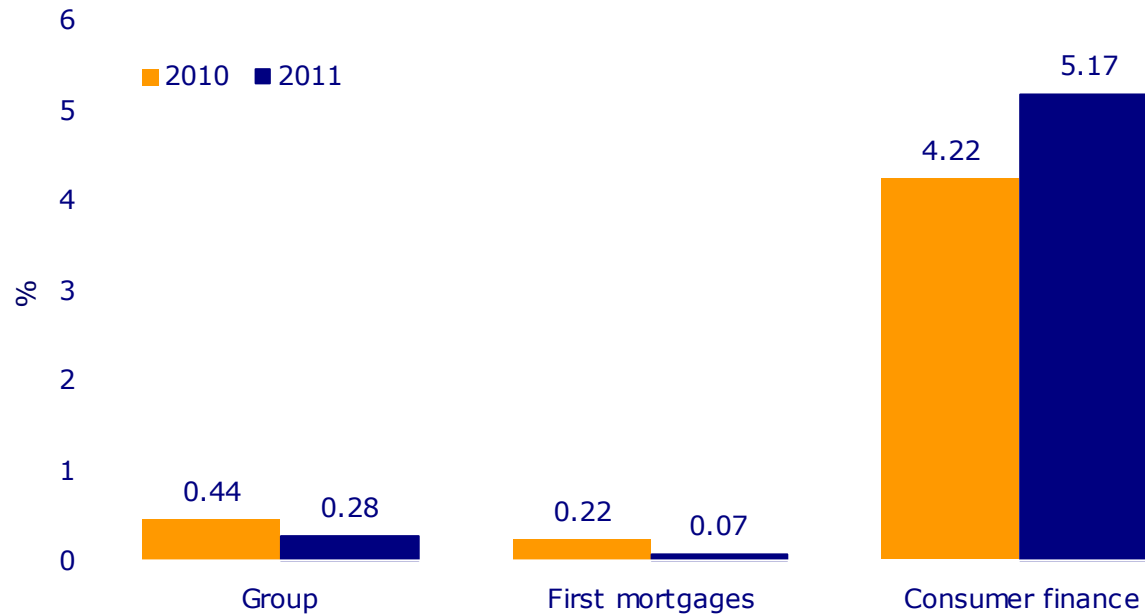
# Receiver of Rent (RoR)

- 86% of buy-to-let 3 months + arrears subject to RoR
- RoR is most effective arrears management strategy
  - for lender, landlord and tenant
- 1,483 properties in RoR - 94% of available RoR properties are let
- Majority of buy-to-let provision charge, current and historic, relates to RoR properties

## Paragon's RoR process

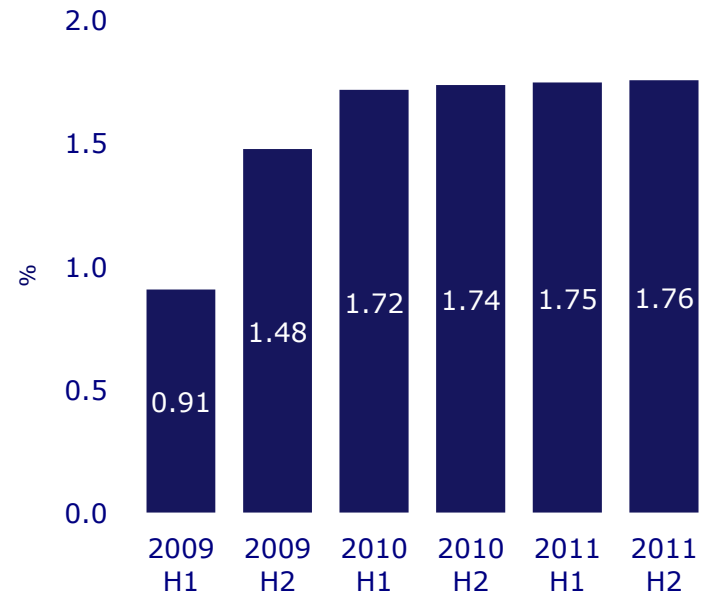
- Aim is to return loan to performing status, whilst recognising landlord's financial difficulties
- Paragon takes control of the rents
- Rental income is paid by tenant direct to Paragon
- Properties may be returned to landlord, if financial difficulties resolved, or sold
- Of all cases ever in RoR
  - approx 64% resolved (of which half sold and half returned to landlord)
  - 36% remain in ROR
- Case-by-case decision-making

# Impairment charge as % of total loan assets



# Cash margins

- Cash flow remains strong
- Free cash balances £195 million





## Strategy

# Strategy

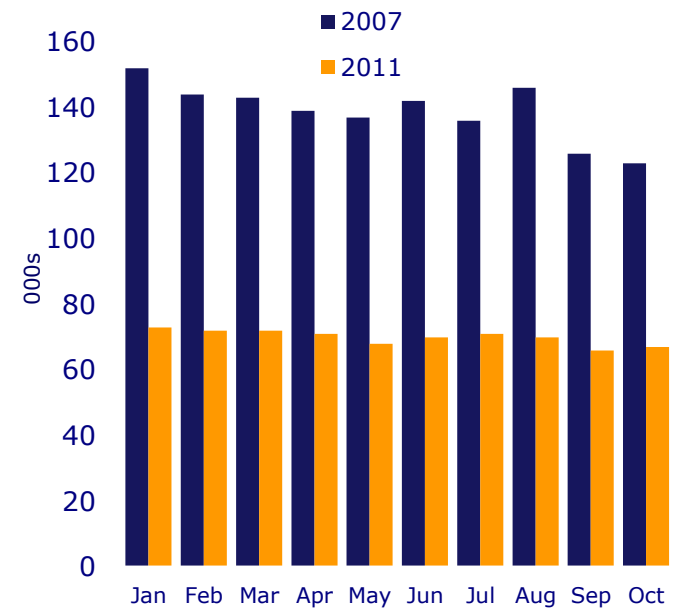


## **Loan origination**

# UK housing market

- Market characterised by low level of transactions:
  - Average 70,000 transactions per month during 2011 to date (2007 average: 135,000 per month)
- House prices remain broadly flat
- Housing market in equilibrium, just at a lower level
- New Government initiatives

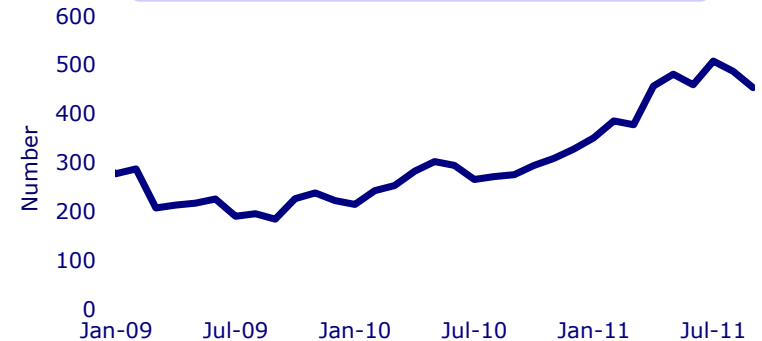
## Monthly number of housing transactions



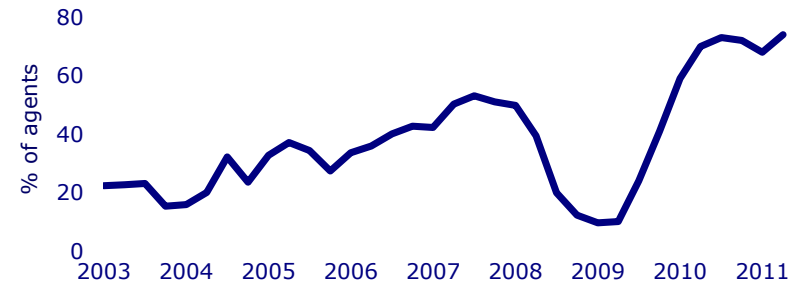
# Buy-to-let market

- Conditions improving
  - More products available, but focussed on smaller scale landlords
  - 88% below 2007 peak
- Strong rental demand
  - 74% of ARLA agents reported more tenants than properties in Q3 2011
  - Savills forecasting rental growth of 21% for next 5 years
- Buy-to-let gross lending
  - 9 months to 30/9/11 up 41% to £9.7 billion
  - 71% below 2007 peak

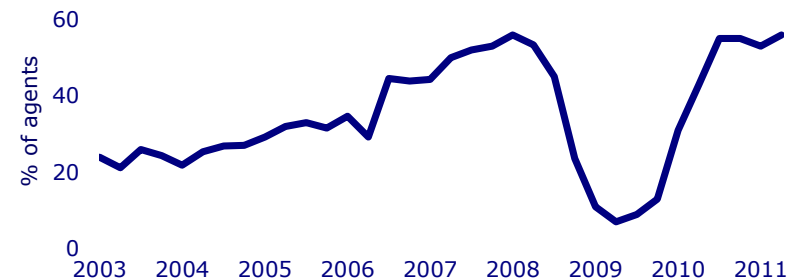
## Number of available BTL products



## More tenants than properties



## Increase in rent levels



# Regulation: update

- Regulatory environment continues to develop
- Buy-to-let
  - EU Directive relating to residential property still in drafting/negotiation stage
  - “Consumer” buy-to-let may be included
- Mortgage Market Review
  - New consultation announcement imminent
  - Second charge mortgages to be regulated by FSA – however, significant delays expected
  - Non-bank lenders to be regulated - no retrospection
- Paragon is already FSA authorised for mortgages and insurance - well placed to be fully compliant with likely regulatory framework

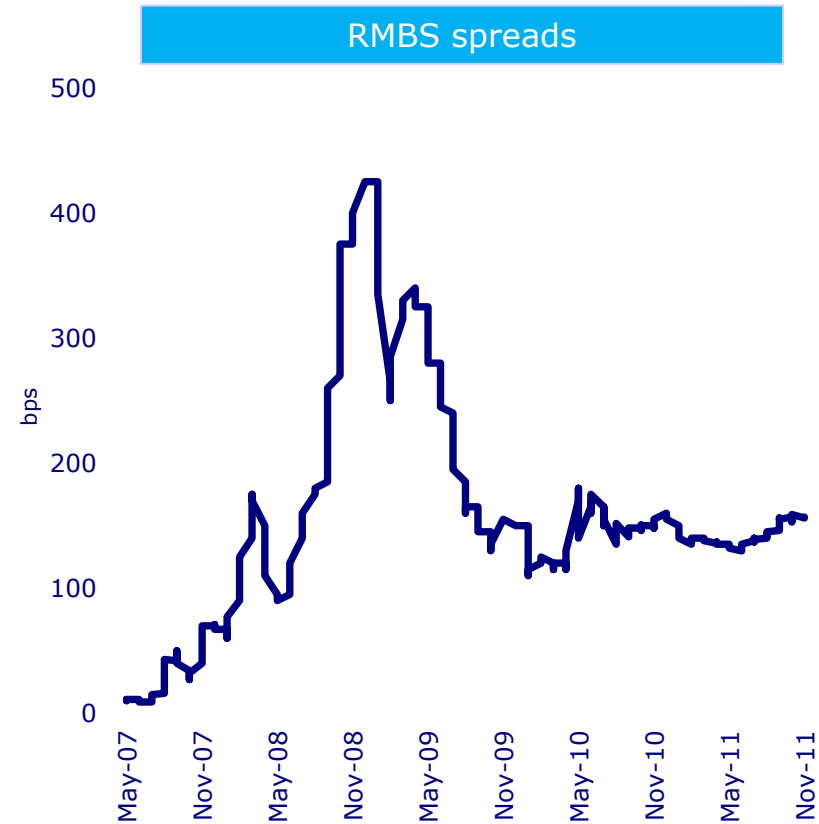
# 2011 new lending

- Paragon's return to buy-to-let market well received
- Focus in 2011 on re-establishing distribution
- High quality new originations
  - Average LTV 69.2%
  - Average ICR 155.0%

Buy-to-let	At 30-09-11
Advances	£127.0m
Further advances	£5.8m
	£132.8m
Pipeline	£67.5m
Redemptions	£181.2m

# Funding

- £200 million warehouse facility with Macquarie
- PM16 securitisation:
  - High levels of investor demand
  - £163.8 million, upsized and provided pre-funding
  - Class A senior notes (AAA)- £131.7 million
  - 275bps over 3 month LIBOR
  - Junior notes retained
    - Strong capital and liquidity position
- Debt markets generally impacted by Eurozone crisis
  - RMBS performance robust
  - General price volatility may push up mortgage spreads
- Additional warehouse capacity in due course



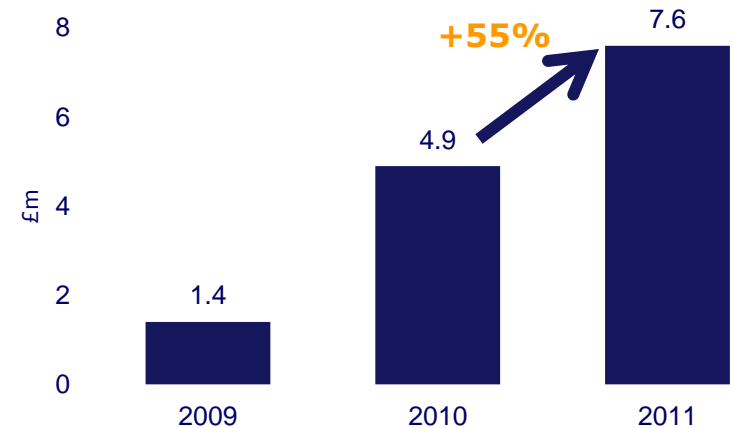
## Portfolio acquisitions



# Portfolio opportunities

- Opportunities include:
  - Portfolio acquisitions
  - Loan servicing
    - Servicing opportunities arise from portfolio sales
- Contributed £7.6 million in 2011 (2010: £4.9 million)
- 200,000 accounts under management
  - 69% consumer assets  
Long-term sector experience
  - 59% are serviced on behalf of third parties
- Idem making significant and increasing contribution to Group profits

## Loan servicing and portfolio acquisitions operating profit



# Idem Capital - investments

- Total investment to date
  - Six portfolios, total investment £89.5 million
    - £77.5 million direct investment
    - £12 million co-investments
  - First mortgage, second mortgage and unsecured asset classes
  - Portfolios performing well
  
- Portfolio investments during 2011
  - Two unsecured loan portfolios acquired in partnership with 3<sup>rd</sup> party investment companies
    - Servicing contracts with promote structure
  - Direct investment to acquire a portfolio of second mortgages
  - Investment in RBS unsecured loan portfolio announced in October
  
- Accounting
  - Fair value accounted under IFRS
  - Tested at each reporting date
  - EIR applied through interest income
  - Acquired assets included in loans on balance sheet, JVs held as investments
  
- Structure
  - Non-recourse SPVs, including JVs
  - Any leverage located within SPV

# Idem Capital - investment process

- Idem deals structured in two main ways:
  - **Principal:** Idem bids in its own right, raising debt to support the deal as required
  - **Co-investor:** Larger funds / banks acquire portfolios and appoint Idem (or Moorgate) as servicer, with Idem taking a minority equity position
- Proven specialist servicing capabilities with 'skin-in-the-game'

## Idem Capital – deal process

### Diligence

- Financial
- Credit
- Operational
- Legal
- Property
- Historic servicing

All supported by highly experienced teams

### Pricing

- Stress testing applied
- Historic operational practices affect value / provide opportunities

### Migration

- Expert operational teams in place
- Highly flexible and scalable technology
- First class track record

# Market opportunities

- Bank de-leveraging being driven by:
  - EU bail out requirements
  - Basel III
  - Revised stress tests, SIFIs, Vickers
  - On-going banking funding pressures
  
- European banking market de-leveraging (asset sale forecasts)
  - PriceWaterhouseCoopers - €1.3 trillion (40% UK) - €800 billion non-performing
  - Morgan Stanley - €2 trillion
  - Royal Bank of Scotland - €2 trillion
  
- Staged process
  - Phase 1
    - Par value assets
    - Short-term receivables
    - Regulatory-driven actions eg EU bailout requirements
    - Written down assets
    - High RWA
  
  - Phase 2
    - Long duration assets
    - Low/sub market yields, but high quality assets
    - Low RWA
    - Mortgages more likely to be in Phase 2

# Conclusion

- 2011 strong financial and operational performance
- Excellent progress on strategy
- Environment likely to remain challenging
  - High quality lending re-established
  - Increasing opportunities from bank deleveraging
- Well positioned to meet these opportunities



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