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Q2 2018 HIGHLIGHTS

- Rental market fundamentals strong
- Fewer landlords optimistic about portfolio prospects
- Buying intentions at lowest level ever

LANDLORDS DOWNBEAT DESPITE STRONG RENTAL MARKET

The fundamentals underpinning the UK's rental market are as relevant today as they have ever been. Population growth, more flexible lifestyles and tighter mortgage affordability continue to drive strong tenant demand, low voids and stable yields. However, despite positive market indicators, landlords in the Private Rented Sector (PRS) have never felt less optimistic about the future.

Even though more than eight out of ten landlords (85%) report that tenant demand is either stable or increasing, just over one in ten (12%) say they feel optimistic about the prospects for their property portfolio.

Landlords' downbeat assessment of the future also contrasts sharply with their experience of property voids and rental yields.

Void periods, which capture the amount of time a property lies empty each year, are low at just 2.7 weeks on average.

Similarly, gross rental yield, which measures rent before tax as a percentage of a property's value, is running in line with the long-term average at 6.4%.

Given that market indicators remain strong, it would appear it's the onslaught of tax and regulatory changes more than anything else that's impacting sentiment and feeding through to weaker buying intentions.

Only 7% of landlords say that they expect to purchase buy-to-let property in the next quarter compared with 23% who say they plan to sell.

The survey results also suggest a fall in the average portfolio size of participating landlords from a peak of 14.9 properties in 2014 to 12.4 in the current period, tying in with recent figures from the DHCLG¹ which show a 46,000 drop in Private Rented Sector (PRS) dwelling stock to 4.78 million - the first reduction since 2001.

In addition, landlords are de-leveraging to deal with the changing landscape, reducing their debt funding relative to the value of their portfolios to bring average portfolio gearing down from around 40% in 2014 to 32% today.

While landlords have options to shape and manage their affairs to cope with changes, tenants have less choice.

If the flow of new property into the PRS is materially reduced, tenants will not only have less property to choose from but could potentially face higher rents.

Positive sentiment is a key ingredient in encouraging investment and policy makers ignore it at their peril.

**John Heron, Managing Director
Mortgages, Paragon**

PRS
Trends
Q2 2018

OUR LANDLORD PANEL

Our panel is an experienced group of 201 buy-to-let landlords, with 81% of those surveyed having been residential landlords for more than ten years and 38% having been involved for more than 20 years.

Three quarters (75%) of landlords surveyed in Q1 2018 are classed as professional – owning three or more properties – and our sample is both an accurate reflection of the rented residential sector and Paragon’s customer base of residential landlords.



81%

LANDLORDS
FOR 10 YEARS +



38%

LANDLORDS
FOR 20 YEARS +



75%

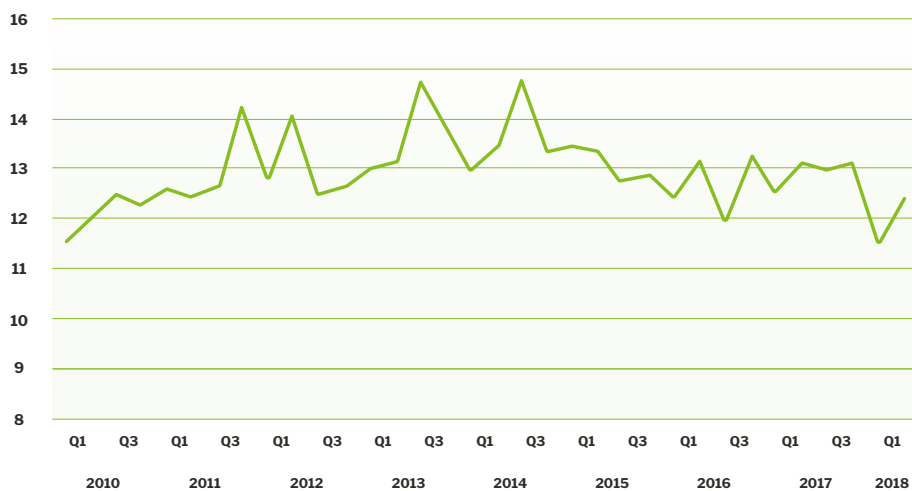
OWNING THREE OR
MORE PROPERTIES

PORTFOLIO SIZE

On average, residential landlords have 12.4 properties in their rental portfolio in Q2 2018, down from a peak of 14.9 properties in Q3 2014.

The average portfolio value for landlords is now £1.61 million. After peaking in 2014, the trend for average portfolio value has generally been downwards.

Average number of rented residential properties in portfolio



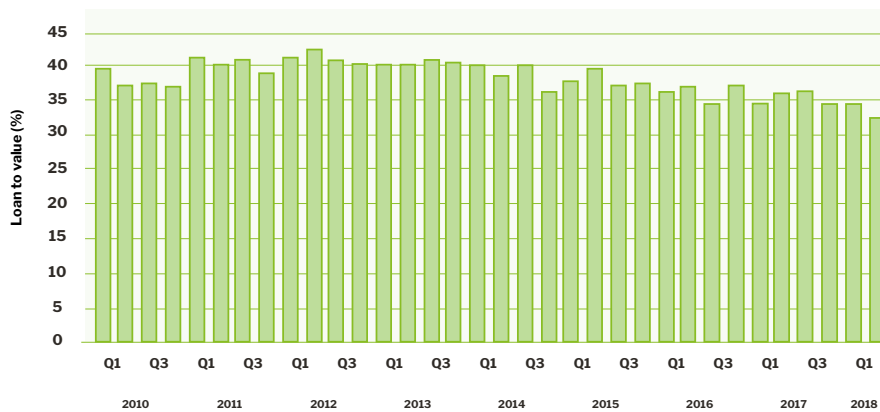
GEARING

As well as reducing the number of properties in their portfolio, landlords have also been trimming borrowing relative to portfolio value, reducing average portfolio gearing from a peak of 43% in 2012 down to 32%.

This steady reduction in gearing suggests landlords are committed to maintaining borrowing at manageable and sustainable levels.

Perhaps as a result, landlords also report a fall in the proportion of rent spent on mortgage payments, down from 30% at the beginning of 2017 to 27% today.

Average gearing of investment property portfolios

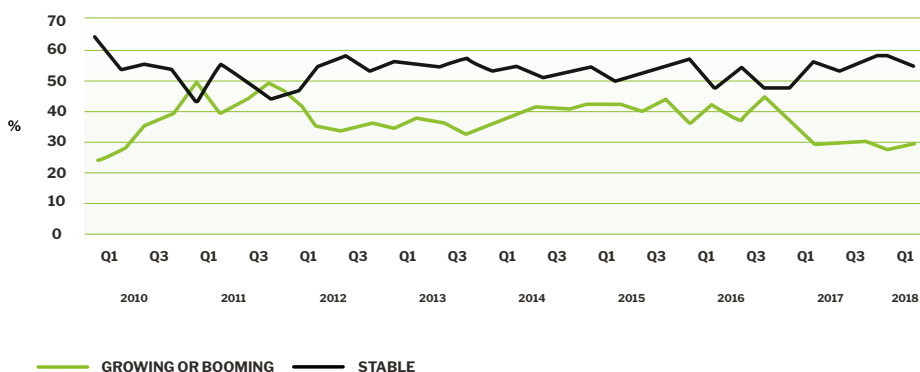


TENANT DEMAND

While the strength of tenant demand has moderated since 2015, an overwhelming 85% of landlords continue to report stable or growing demand for rental property.

Population growth, people’s need for flexibility and tighter mortgage affordability are as relevant today as ever before and rental property remains in high demand.

Proportion of landlords who say tenant demand is growing or booming

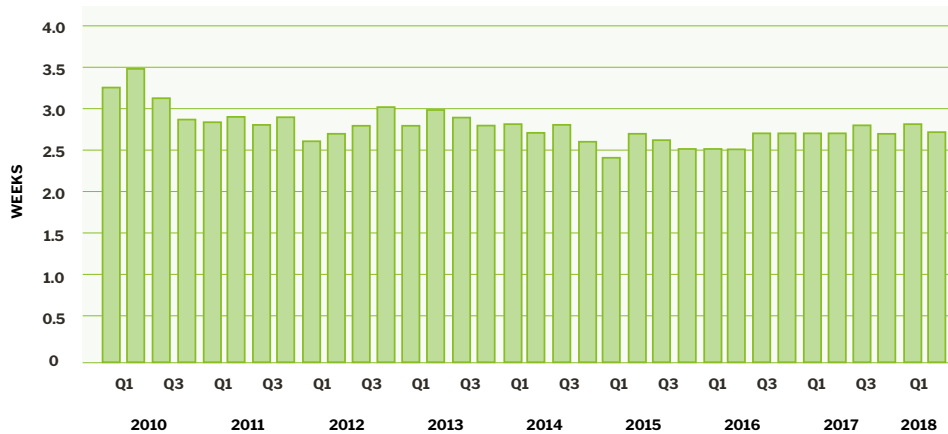


VOID PERIODS

Strong demand for rental property means that void periods remain firmly within a long-established range of 2.5 to 3 weeks.

The void period measures the average amount of time rental properties are vacant each year, with this quarter's survey recording a void period of 2.7 weeks.

Average void period



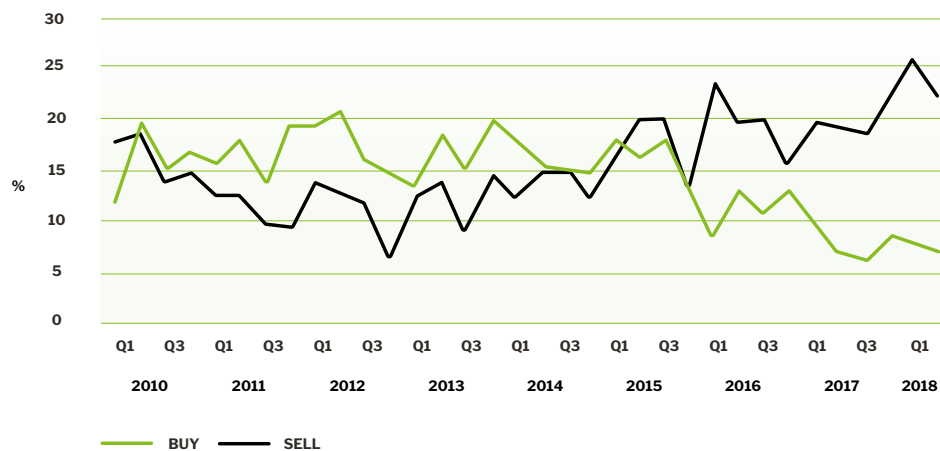
BUYING VS. SELLING EXPECTATIONS

In spite of the relatively strong fundamentals underpinning the rental market, landlords say they are still more likely to sell property in the next quarter than to buy.

Almost one quarter of landlords (23%) indicated an intention to sell compared with just 7% who said they were considering a new purchase.

Those indicating an intention to sell first overtook potential buyers in early 2015 and the gap has widened progressively since.

Proportion of landlords expecting to buy and sell property in the next quarter

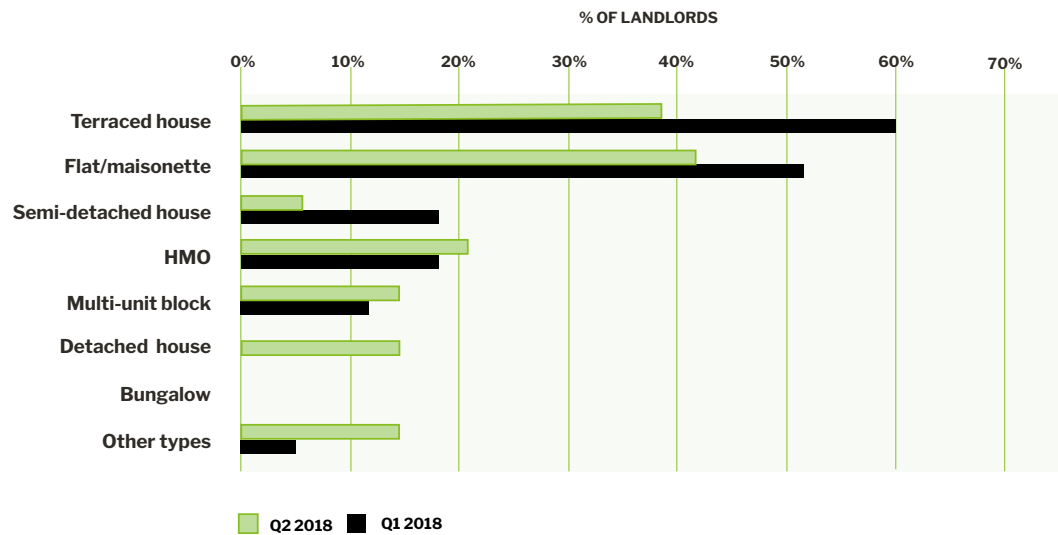


PROPERTY TYPES

For those landlords who plan to buy property in the next quarter, terraced houses and flats are in the highest demand, with around four out of ten potential purchasers interested in these property types.

Landlords also indicated increased interest in Houses in Multiple Occupation (21%), and detached homes (14%).

Type of property expected to purchase

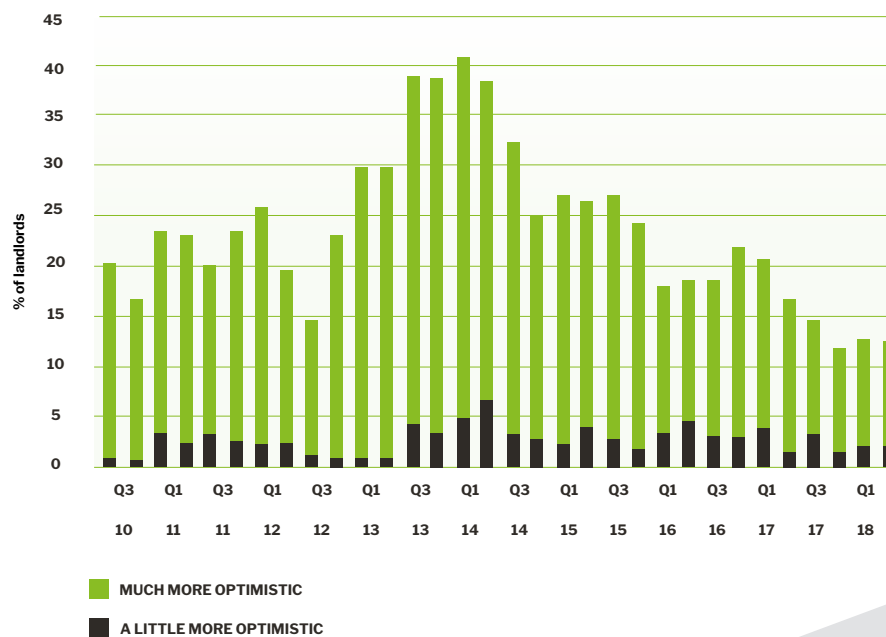


VIEW OF PROSPECTS FOR PROPERTY PORTFOLIO

Landlords continue to feel progressively less optimistic about the prospects for their portfolio.

Back in 2014, four out of ten landlords (41%) said they felt optimistic about the prospects for their portfolio in the months ahead. However, since then, following progressive tax and policy changes aimed at landlords and targeting buy-to-let in particular, optimism among landlords has dwindled, reaching a low of 12% in this quarter's results.

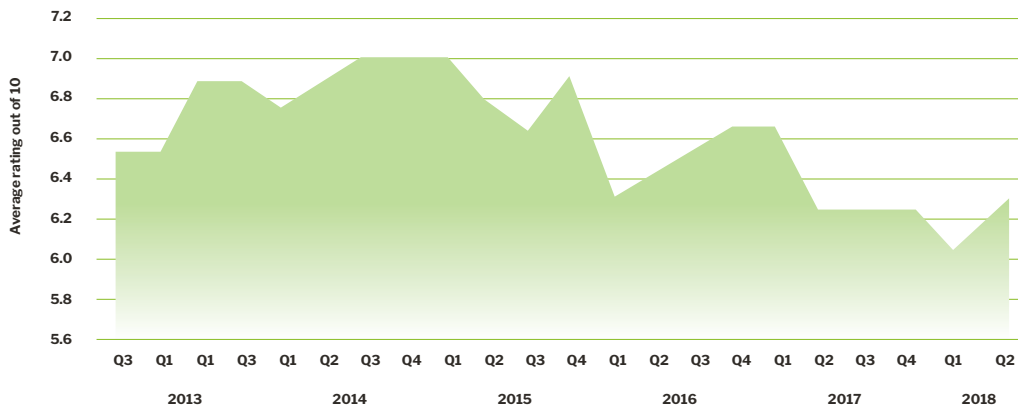
Landlords optimism about portfolio prospects



OVERALL PROSPECTS FOR THE PRS

When asked to score the prospects for the PRS in the next 12 months, landlords returned an average score of 6.3 out of ten. This remains close to the lowest level recorded in Q1 2018 of 6.1 and appears to be indicative, once again, of the dampening of landlord optimism as the various tax and regulatory measures take effect.

Overall prospects for the PRS in the next 12 months



ABOUT PARAGON

Paragon is a leading provider of buy-to-let mortgages for landlords with property portfolios, both big and small, through its portfolio and non-portfolio range. Paragon also offers second charge and specialist residential mortgages.

Paragon lends to private individuals and limited companies and has mortgages suitable for single, self-contained properties, as well as HMOs and multi-unit blocks. Paragon can accommodate higher aggregate lending limits and more complex letting arrangements including local authority leases and corporate leases along with standard ASTs.

Paragon introduced its first product aimed at the professional property investor in 1995 and is a member of UK Finance, the Intermediary Mortgage Lenders Association (IMLA), National Landlords Association (NLA) and the Association of Residential Letting Agents (ARLA).

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