

THE PARAGON GROUP OF COMPANIES PLC

Trading Update

The Paragon Group of Companies PLC ("the Group" or "Paragon") today publishes its Trading Update based upon the business performance from 1 October 2015 to date, including a commentary on the unaudited financial information for the period from 1 October to 31 December 2015.

Financial performance

The Group's financial performance remains strong, in line with management's expectations. Underlying operating profits (before fair value items and acquisition related costs) of £35.2 million were 13.9% higher than the £30.9 million reported for the corresponding period in the previous year. This figure excludes costs of £2.2 million incurred in connection with the Group's acquisition of the Five Arrows Leasing Group ("Five Arrows Leasing"), completed on 3 November 2015. Net of these expenses, operating profits were £33.0 million for the period. Pre-tax profit, after a credit of £0.9 million for fair value hedging items, was £33.9 million for the period (Q1 2015: £30.2 million), an increase of 12.3% including the absorption of the costs associated with the acquisition. The Group's capital base is strong, reflected by its Core Tier 1 ratio which stood at 16.8% at 31 December 2015 and its leverage ratio of 7.0% at the same date.

Trading activity

The Group's loan portfolios continue to perform well, generating strong profits and cash flows. Buy-to-let originations were 80.6% higher than the same period in 2015, at £400.9 million. The period end buy-to-let pipeline stood at £595.7 million, 43% higher than at the same point in 2014. Whilst there is uncertainty around the buy-to-let market, the Group remains on track to deliver further growth in new lending this year.

Within Paragon Bank, car finance volumes rose to £20.6 million for the period (Q1 2015: £6.3 million) reflecting the continued development of the distribution base and second mortgage lending grew to £11.4 million (Q1 2015: £0.8 million). Paragon Bank launched its residential development finance business during the period, as part of its product diversification strategy. In its first two months post-acquisition, Five Arrows Leasing has performed well, originating £18.1 million of asset finance business across its four sub-brands. The acquisition of Five Arrows Leasing has taken Paragon Bank into profit on a monthly basis, this being achieved within two years of its authorisation.

Idem Capital investments totalled £9.8 million in the quarter. It continues to see a range of interesting investment opportunities, including those made possible through its collaboration with Paragon Bank.

Buy-to-let

The credit performance of the Group's buy-to-let portfolio remains exemplary, with 16 basis points of arrears (using the CML's three month plus measure) at 31 December 2015 compared to 22 basis points at 31 December 2014, remaining materially below broader market rates.

The redemption levels seen in the summer months continued into the December quarter. Total buy-to-let redemptions grew slightly to £175.8 million from the £170.1 million reported in the quarter to September 2015, representing an annualised rate of 7.5%. The Group expects the redemption rate for its new lending portfolio to move towards more normalised levels as the portfolio seasons.

A number of fiscal and regulatory changes and proposals affecting the buy-to-let market have been introduced in the last six months; these are commented on below. However, to date, there has been no change to existing customer behaviour.

Acquisition

The acquisition of Five Arrows Leasing was completed on 3 November 2015. The business has been re-branded as Paragon Bank Asset Finance Limited ("PBAF"). The Group's 90-day post acquisition review of PBAF is well progressed and the Group is optimistic regarding the growth prospects for the asset finance business. The review will establish the division's strategic priorities together with final plans for integrating IT and operational functions within the wider Group where, as previously advised, a further investment of approximately £1 million is anticipated.

Funding

Retail deposit balances were £1,046.3 million at the quarter end, having increased by £337.6 million across the period, demonstrating the effectiveness and scalability of Paragon Bank's savings proposition and its role in diversifying Group funding and facilitating broader income generation. The Group completed its latest securitisation in November 2015 with Paragon Mortgages (No.24) PLC packaging £350.0 million of buy-to-let loans in a transaction that successfully issued both Sterling and Euro-denominated notes in challenging market conditions. The increasing proportion of buy-to-let originations being funded via retail deposits (£174.0 million during the quarter) has allowed the Group to cancel £100.0 million of its warehouse capacity, taking the aggregate facility size to £850.0 million at the quarter end and improving the cost efficiency of the broader new business financing strategy. Available warehouse facilities at 31 December 2014 were £550.0 million.

During the quarter, Idem Capital raised a new £121.4 million facility with Citibank to finance its unsecured loan portfolio, including the refinancing of an existing financing line (£39.8 million).

The Group remains highly cash generative, with strong cash flow performance from its various loan portfolios. These flows, together with the re-levering of the Idem Capital assets during the period, resulted in free cash balances of £159.6 million at 31 December 2015. In addition to an injection of an additional £100.0 million of equity into Paragon Bank to finance its Five Arrows Leasing acquisition, the Group provided a further £37.7 million to Paragon Bank as capital support for its planned organic mortgage and consumer finance activities during 2016. The Group also provided credit enhancement for its new lending, financed the quarter's Idem Capital investments and commenced the 2016 share buy-back programme during the quarter.

Capital

The Group notes the consultation paper issued by the Basel Committee on Banking Supervision on 15 December 2015 regarding the standardised risk weighting approach for capital adequacy calculation purposes and, in particular, its application to buy-to-let lending. The Group considers that the proposed risk weightings do not properly reflect the strong credit performance of the asset class in the UK and looks forward to further updates as the consultation progresses. Notwithstanding the outcome to the consultation, Paragon has a wealth of data and excellent credit metrics to support the use of an Internal Ratings Basis ("IRB") approach for assessing the appropriate buy-to-let risk weightings. Other UK institutions that use the IRB measure for their buy-to-let portfolios achieve materially lower risk weightings than the 35% used by Paragon under the current standardised approach, with figures typically in the low to mid-teen percentages. Paragon's preparations for an IRB application are now underway.

Strong progress has been made on delivering the additional £50.0 million share buy-back announced in November 2015, with £11.6 million having been invested by the Group as at the date of this announcement.

Outlook

The Board remains committed to its strategy of improving shareholder returns through its four key levers of organic growth, further diversification, M&A activity and capital management. The acquisition of the Five Arrows Leasing business, Paragon Bank's retail deposits exceeding the £1 billion level during the quarter and the re-levering of the Idem Capital assets are each notable steps in executing this strategy.

The buy-to-let market has seen strong growth in recent years, driven by increasing levels of tenant demand. The fiscal and regulatory changes and proposals, introduced over the last six months, may soften the rate of growth for buy-to-let lending as time progresses towards their full implementation in 2021. However, demand for rental properties will remain strong for the foreseeable future. The changes are likely to result in an increasing trend towards investment by professional landlords, a customer group where Paragon already has extensive experience and capability.

Nigel Terrington, the Group's Chief Executive, said: *"I am delighted with yet another strong financial performance by the Group which has been achieved alongside further significant progress in our diversification strategy. Paragon Bank has passed through the milestones of £1 billion of deposit balances and on a monthly basis is in profit, less than two years after launch. The acquisition of Five Arrows Leasing is an exciting prospect and we believe it will provide a platform for further growth into the future."*

"Our buy-to-let lending continues to display an exemplary credit performance and whilst the recent and proposed changes may soften the rate of growth in the sector, the drivers supporting the long term structural changes in the housing market remain as valid today as they have over the last three decades".

The Group intends to announce its results for the six months ending 31 March 2016 on Tuesday 24 May 2016.

For further information, please contact:

Nigel S Terrington
Chief Executive
Tel: 0121 712 2024

Richard Woodman
Finance Director
Tel: 0121 712 2607

Deborah Bateman
External Relations Director
Tel: 0121 712 2025