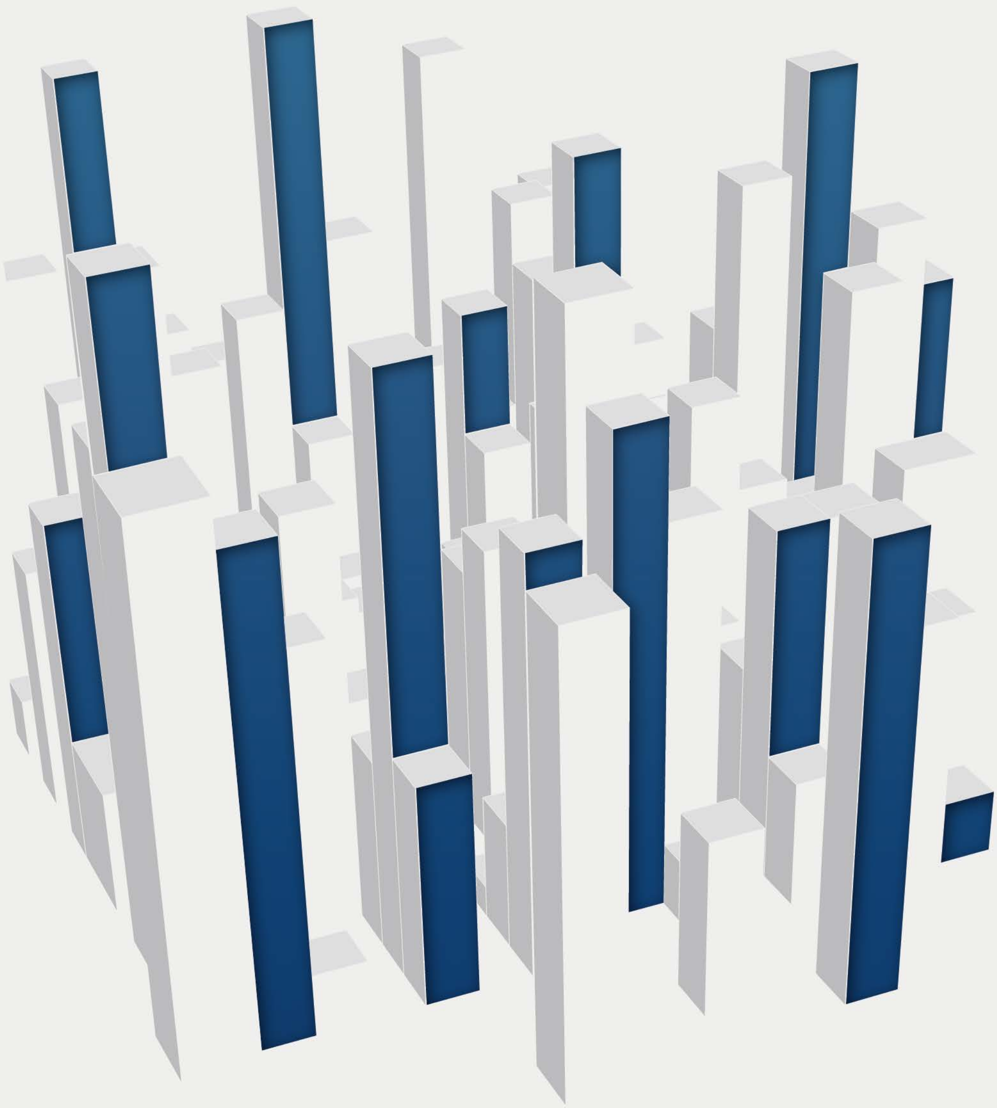


The Paragon Group of Companies PLC

2016 Half-Year Financial Report

paragon

paragon

The Paragon Group of Companies uses its core risk and credit expertise to develop lending products for specialist target markets. Best known as the UK's largest, independent buy-to-let lender, Paragon is growing its business by expanding further in buy-to-let lending and diversifying into small and medium sized business and consumer lending markets through its subsidiary, Paragon Bank PLC. The Group is also one of the UK's largest debt purchasers through its Idem Capital subsidiary, where it purchases, co-manages and services secured and unsecured consumer loan portfolios.

CONTENTS

CAUTIONARY STATEMENT

Sections of this half-yearly report, including but not limited to the Interim Management Report, may contain forward-looking statements with respect to certain of the plans and current goals and expectations relating to the future financial condition, business performance and results of The Paragon Group of Companies PLC and its subsidiaries ('Paragon' or the 'Group'). These have been made by the directors in good faith using information available up to the date on which they approved this report. By their nature, all forward-looking statements involve risk and uncertainty because they relate to future events and circumstances that are beyond the control of the Group and depend upon circumstances that may or may not occur in the future. There are a number of factors that could cause actual future financial conditions, business performance, results or developments to differ materially from the plans, goals and expectations expressed or implied by these forward-looking statements and forecasts. Nothing in this document should be construed as a profit forecast.

FINANCIAL HIGHLIGHTS

Nigel S Terrington
Chief Executive

"This has been another outstanding performance from Paragon, with strong profit growth complemented by significant progress in our lending activity and further development in our diversification strategy.

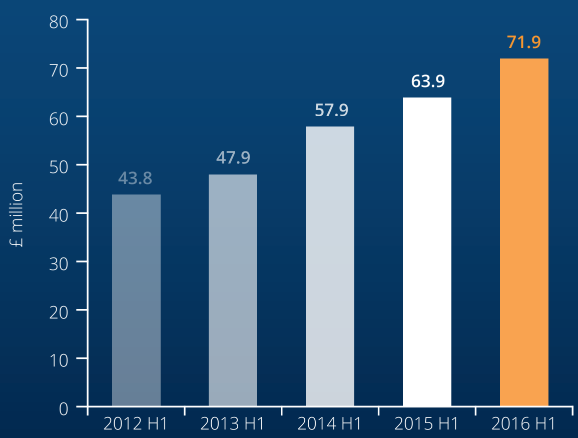
The Group's progress was evident across each of our operating divisions. Paragon Bank reported its maiden profit, achieving this in less than two years after launch, whilst also completing the acquisition of Five Arrows providing an entry platform to the SME asset finance sector. Idem Capital saw extensive acquisition activity supporting further growth in the consumer finance loan book, particularly through co-investment opportunities with Paragon Bank. Finally buy-to-let, whilst maintaining our disciplined approach to credit and pricing, witnessed strong new lending levels influenced in part by the increase in Stamp Duty, pulling forward some business into the first half of the year. Strong tenant demand is set to continue to drive the need for rented property in the UK for the foreseeable future. Whilst there is some uncertainty over the longer term growth prospects in buy-to-let, we expect the tax and regulatory changes to provide relative benefits for the Group's specialist lending focus, in particular, the more complex requirements of professional landlords.

Paragon operates with a strong capital base and an enviable credit record. Its leading position in the specialist buy-to-let market is now being complemented by a broader and more diversified series of business lines, including SME lending. This leaves the Group well placed to continue to develop and deliver increasingly broad product offerings for our customers, which in turn supports improving returns for our shareholders."

Underlying profits

£71.9 million

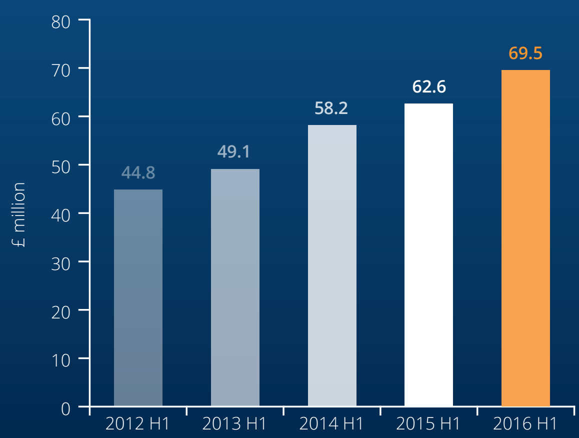
12.5% higher, compared with £63.9 million in H1 2016



Statutory profits

£69.5 million

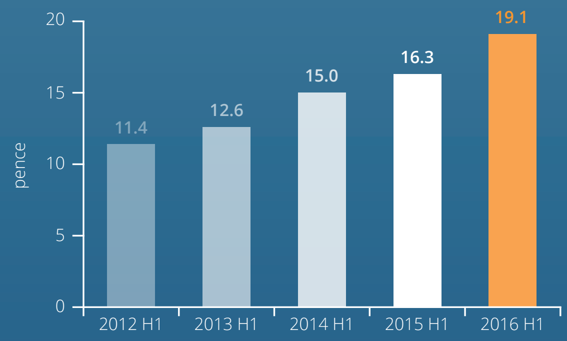
11.0% higher, compared with £62.6 million in H1 2016



Basic earnings per share

19.1 pence

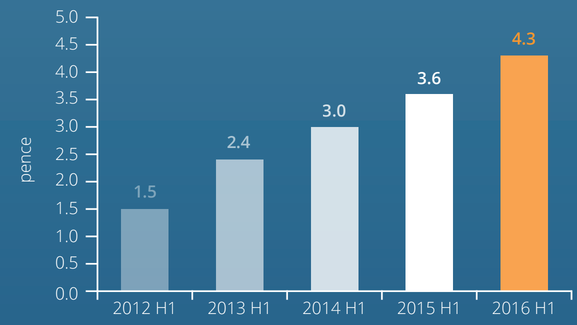
17.2% higher, compared with 16.3 pence in H1 2015



Dividend per share

4.3 pence

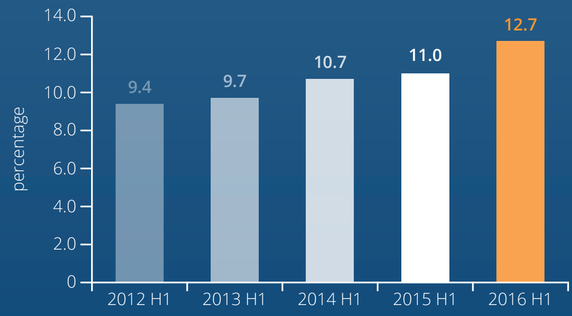
19.4% increase, compared with 3.6 pence in H1 2015



Return on tangible equity

12.7%

compared with 11.0% in H1 2015

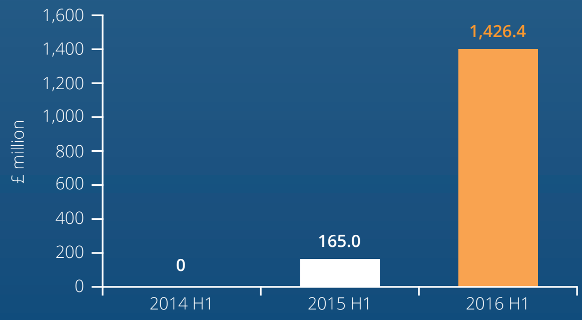


Savings deposits

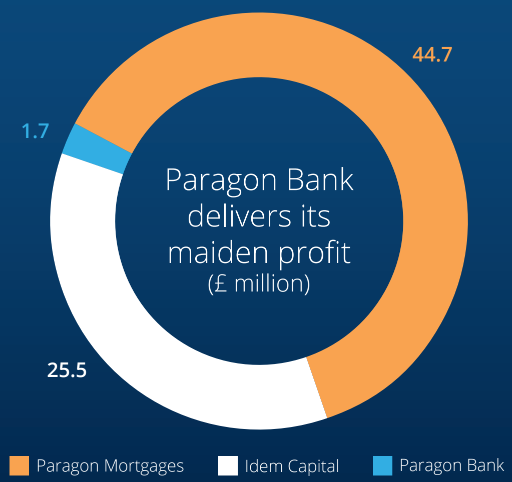
Paragon Bank retail savings deposits over

£1.4 billion

Strong growth in savings deposits



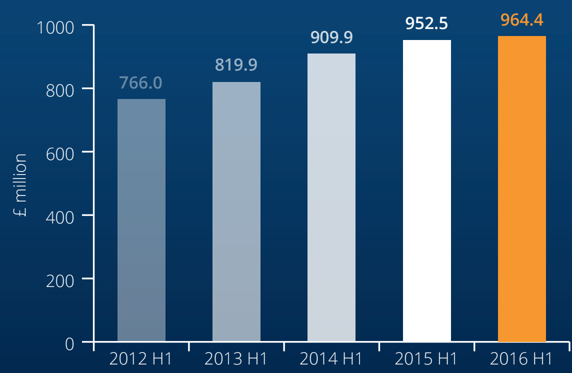
Underlying segmental profit



Shareholders' funds

£964.4 million

compared with £952.5 million at 31 March 2015



HALF-YEAR FINANCIAL STATEMENTS

INTERIM MANAGEMENT REPORT

Strategy Report

Paragon has seen strong lending growth whilst also taking significant steps in progressing its strategy during the six months to 31 March 2016, a period which has witnessed changes in the broader operating environment.

Profit growth has continued, with underlying profits rising by 12.5% to £71.9 million (2015 H1: £63.9 million) and profits on the statutory basis increasing by 11.0% to £69.5 million (2015 H1: £62.6 million). The combined effects of this growth and the Group's share buy-back programme have resulted in strong earnings per share growth (rising by 17.2% to 19.1p from 16.3p in the equivalent period in 2015) and a further improvement in return on tangible equity ('RoTE') to 12.7% (2015 H1: 11.0%) (note 4b).

The first half of the year has been particularly busy with strong levels of new organic lending, debt purchase activity and M&A. Group wide new advances were £949.5 million compared to £465.7 million in the equivalent period last year, taking net loan growth to £1,384.8 million over the last 12 months.

We have made strong progress in changing the profile of the Group, placing Paragon Bank at the heart of our development plans. In addition to organic balance sheet growth, the Bank has worked with the wider group to participate in debt purchases and also to refinance previously securitised or externally financed portfolios. The Bank has continued to extend its loan offerings, with the launch of its development finance proposition and, more significantly, the completion of its acquisition of the Five Arrows Leasing Group in November 2015.

As a key element in its funding diversification strategy, the Group has increasingly accessed retail deposit funding, with securitisation playing a more tactical role as and when conditions suit. The scale of retail deposits more than doubled over the last six months, standing at £1,426.4 million at 31 March 2016 (31 March 2015: £165.0 million). Further evidence of the Bank's growing scale and maturity is also provided by its imminent first draw down under the Funding for Lending Scheme, with £109.0 million expected to be accessed during the coming quarter.

The £117.0 million acquisition of Five Arrows Leasing Group (subsequently re-branded as Paragon Bank Asset Finance) marked a scale change in the Group's lending diversification strategy. A well respected business with a long history, the business operated in a number of niche sectors in the asset finance market, in some of which volumes and growth prospects were limited. The results of our post-acquisition strategy review are particularly encouraging, suggesting that with only modest additional investment in systems, the asset finance business is well placed to compete effectively in the mid-tier of the market, delivering material scope to increase volumes and earnings. The separation from Rothschild & Co has progressed well and we expect further systems enhancements to be operational within the next 12 months, at which point the capacity of the asset finance business will be materially increased.

Buy-to-let lending still dominates the Group's balance sheet, reflecting the early stages of our diversification strategy. Whilst the private rented sector remains the second largest form of housing tenure in the UK, a number of regulatory, legislative and fiscal developments have contributed to create uncertainty over the future shape and scale of the buy-to-let market. The recent Stamp Duty changes had a temporary disruptive effect on volumes, accelerating completions in the period up to March 2016 and consequently reducing pipelines. We expect the second half of the year to be slower as a result. Over the long term it is likely that the rate of growth of buy-to-let lending will be lower than the strong expansion witnessed in recent years, though it will remain a significant market, with strong tenant demand continuing to underpin further growth in the private rented sector. Furthermore, the regulatory and fiscal changes are expected to result in increasingly complex underwriting requirements which should play to the strengths of specialist lenders, consequently improving their market share and margins. There is already some evidence to this effect. The Group has a reputation of being a highly prudent lender, with the strong skills, systems and experience to advance loans effectively to customers with complex requirements, as evidenced by its ongoing delivery of market leading buy-to-let credit performance.

Idem Capital and Paragon Bank have formed a strong combination in acquiring loan portfolios, accessing appropriate leverage for high quality assets. This joint approach will be used on an increasing basis going forward. Idem Capital has also refinanced a number of legacy portfolios during the period, improving returns made on the capital it employs and returning surplus funds to the Group.

Enhancing shareholder returns is a key objective. The 17.2% growth in EPS has supported a 19.4% increase in the interim dividend to 4.3 pence, with the Group targeting a three-times dividend cover ratio for the full year in line with policy. The share buy-back programme has also progressed well, with £33.8 million being invested in the period.

Organic growth, product diversification, M&A activity and capital management have each played an important part in delivering a strong set of results for the period. Despite uncertainties in the buy-to-let business, the Group remains well placed to operate in the more specialist buy-to-let market that is expected to emerge as a result of recent interventions. Paragon Bank is increasingly providing the Group with the funding flexibility to drive growth and the prospects for the new asset finance business look particularly promising. Further product diversification is scheduled for the second half of the year and the Group remains focused on M&A opportunities, particularly in areas that complement existing operations.

Business Report

Paragon's operations are organised into three divisions, each with responsibility for delivering asset and profit growth. The Paragon Bank segment includes similar assets to those that appear in the Paragon Mortgages and Idem Capital segments but which are retail deposit funded.

The Group's investments in loans and the amounts invested in the period for each division are summarised below.

	Advances and investments in the period			Investments in loans at the period end		
	Six months ended 31 Mar 16	Six months ended 31 Mar 15	Year ended 30 Sep 15	**31 Mar 16**	31 Mar 15	30 Sep 15
	£m	£m	£m	**£m**	£m	£m
Paragon Mortgages	**479.5**	384.3	976.6	**9,105.3**	8,993.5	9,221.7
Idem Capital	**24.0**	20.9	104.4	**306.8**	406.9	451.0
Paragon Bank	**654.8**	81.4	409.1	**1,441.0**	85.6	407.8
	1,158.3	486.6	1,490.1	**10,853.1**	9,486.0	10,080.5

Paragon Mortgages

Paragon Mortgages is one of the longest established lending brands in the buy-to-let mortgage market. Alongside its sister brand, Mortgage Trust, Paragon Mortgages maintains a significant presence for the Group in this important sector of the UK mortgage market. Trading activity in the period has been particularly strong, with the segment contributing £44.7 million to underlying Group profit (2015 H1: £44.7 million). Paragon Mortgages' stable profit level resulted from underlying growth from net new lending being broadly counterbalanced by the sale of seasoned assets to Paragon Bank in the period, together with the higher funding costs allotted to the segment following the Group's retail bond issue in August 2015.

Total loan assets of the division at 31 March 2016 were £9,105.3 million, 1.2% higher than the £8,993.5 million a year earlier, of which £8,920.2 million were buy-to-let mortgage assets (31 March 2015: £8,749.2 million).

Buy-to-let

Total Group buy-to-let completions increased by 84.6% to £823.6 million for the period (2015 H1: £446.2 million). Paragon Bank increased its proportion of new business flows and it should be noted that at 31 March 2016 the pipeline at Paragon Bank exceeded that of the Paragon Mortgages division.

	Completions in period			Pipeline at period end		
	Six months ended 31 Mar 16	Six months ended 31 Mar 15	Year ended 30 Sep 15	**31 Mar 16**	31 Mar 15	30 Sep 15
	£m	£m	£m	**£m**	£m	£m
Paragon Mortgages	**479.5**	384.3	976.6	**151.5**	493.7	404.2
Idem Capital	**-**	-	-	**-**	-	-
Paragon Bank	**344.1**	61.9	350.0	**199.1**	207.7	309.5
	823.6	446.2	1,326.6	**350.6**	701.4	713.7

Further expansion of the Group's mortgage capacity, supported by the progress made by Paragon Bank in retail markets, facilitated lending growth in the period. This was further boosted towards the end of the half year with the introduction of a 3% Stamp Duty Land Tax ('SDLT') surcharge to landlords accelerating transactions in an effort to beat the deadline. This resulted in March 2016 having the highest number of monthly completions since the Group re-entered the buy-to-let market in 2010.

Market data continues to indicate strong and growing rental demand although UK government policy around the buy-to-let sector has become more complex. Whilst we expect that the disruption caused by the introduction of the SDLT surcharge will be short-lived, we have seen some change in customer behaviour as a result of the changes announced in the 2015 summer budget. In particular, we have experienced a marked increase in applications from incorporated landlords in recent months. This trend, combined with proposals from the Prudential Regulation Authority ('PRA') on buy-to-let underwriting standards, discussed under 'Regulation' below, will, we believe, change the competitive structure of the market going forward. These changes will favour specialist lenders such as the Group where systems, skill sets and experience are already in place to respond to more complex customer needs.

The Group tightened its buy-to-let lending criteria in January, increasing the stressed interest rate in its minimum interest coverage ratio ('ICR') test from 5.00% to 5.35% and embedding forward-looking affordability tests. This represented an early move towards the 5.50% level proposed in the recent consultation paper issued by the PRA. Similar changes by competitor lenders have been noted and more are anticipated over the coming months. The Group's criteria changes led to a depressed level of applications following their introduction which, together with the accelerating effect of the SDLT changes, resulted in the pipeline at the half year falling to £350.6 million (31 March 2015: £701.4 million). This reduced pipeline is expected to result in lower completion levels in the second half year.

The private rented sector remains the second largest form of residential tenure in England according to data in the annual Survey of English Housing for 2014-15, published in February 2016 by the Department of Communities and Local Government. This indicated that the private rented sector, comprising 19% of households, remains larger than the social rented sector (17%) with the level of owner-occupation stable. The Royal Institution of Chartered Surveyors reported that in its survey of members in March 2016, respondents continue to anticipate rents rising at an average rate of 4.5% per annum, driven by strong tenant demand.

This market sentiment has continued to drive demand for buy-to-let mortgages with Council of Mortgage Lenders ('CML') data for the six months ended 31 March 2016 indicating £25.3 billion of gross lending, an increase of 66.4% over the comparable period in the previous year (2015 H1: £15.2 billion). Strong market growth, coupled with the impact of the SDLT changes meant that this was the highest total for any six month period since 2006. Completion levels are, to a degree, exaggerated by the proportion of remortgages, which represented 55.2% of the Group's buy-to-let business in the period (2015 H1: 61.2%) and represented 52.6% of the buy-to-let market in general, according to the CML (2015 H1: 57.9%). Market data indicates that rented properties with a buy-to-let mortgage represent around 30% of property in the private rented sector, a proportion which has been stable since 2008.

The Group has been the beneficiary of growth in the buy-to-let market in recent years and has been able to capitalise on this as a result of its strong relationships in mortgage distribution and its dynamic approach to product development. In offering a comprehensive range of solutions for landlords, including those that choose to hold their properties in a corporate vehicle, we believe the business is well placed in a rapidly changing environment.

The Group's outstanding buy-to-let balances are analysed below.

	Outstanding balances		
	31 Mar 2016	31 Mar 2015	30 Sep 2015
	£m	£m	£m
Paragon Mortgages	**8,920.2**	8,749.2	8,999.1
Idem Capital	**13.9**	15.3	14.5
Paragon Bank	**802.2**	62.1	349.6
	9,736.3	8,826.6	9,363.2

During the period certain buy-to-let loans were sold from the Paragon Mortgages segment to Paragon Bank, when a securitisation transaction was repaid. This portfolio totalled £110.8 million at the end of March 2016.

At 31 March 2016 the Group's buy-to-let portfolio stood at £9,736.3 million, compared with £8,826.6 million a year earlier. The annualised redemption rate on the overall buy-to-let book, although higher than the 4.4% reported for the first half of 2015, still remains low at 9.2%. This is despite the increasing numbers of post credit crisis accounts included in the portfolio, which would be expected to redeem more quickly than the extant book. The annualised redemption rate on these loans, at 16.0% (2015 H1: 7.3%), is, as expected, approaching the levels seen before the credit crisis as the book matures. The annualised redemption rate on pre-crisis lending, at 6.7%, has increased from the 3.8% seen in the half year ended 31 March 2015. This includes an uplift in March 2016 related to the market disruption from the SDLT changes but remains comparatively low. This performance indicates that the Group's landlord customers continue to display a long-term commitment to property investment.

The Group's approach to underwriting remains robust. The focus on the credit quality and financial capability of our customers is underpinned by a detailed and thorough assessment of the value and suitability of the property as security. This was enhanced in the period by the adoption of the stricter ICR requirements described above. This approach continues to deliver market leading credit performance across historic and current lending.

The quality of new lending remains high, with a good affordability profile, low average loan-to-value ratios and strong customer credit profiles. The credit performance of the portfolio over the period continued to be exemplary, with the percentage of loans three months or more in arrears (note 6) standing at 0.14% at 31 March 2016 (31 March 2015: 0.20%, 30 September 2015: 0.19%). This remains considerably better than the CML's comparable market average of 0.56% at that date (31 March 2015: 0.74%, 30 September 2015: 0.66%).

Security values have also benefitted from the effect of increased house prices. The Nationwide House Price Index showed appreciation in residential property values of 3.1% over the six month period. The indexed loan-to-value ratio of the buy-to-let portfolio at 31 March 2016 was 69.5%, broadly similar to its level at 30 September 2015 (note 6). The Group maintains a specialist team of in-house surveyors to maximise its understanding of particular markets, both from a valuation and lettings standpoint.

The number of properties with an appointed receiver of rent reduced by 13.4% to 1,004 at 31 March 2016 (31 March 2015: 1,159), and 96.9% of the properties available for letting in the receiver of rent portfolio were let at that date (31 March 2015: 96.9%).

Other assets

The Paragon Mortgages division also includes income generated from legacy loan books. These include owner-occupied mortgages, car loans, secured consumer loans and unsecured consumer loans. These assets form a very small part of the division's results, when compared to buy-to-let assets, and performed in line with our expectations.

The values of these legacy portfolios are shown below.

	31 Mar 2016	31 Mar 2015	30 Sep 2015
	£m	£m	£m
Owner-occupied mortgages	**25.0**	53.6	47.6
Secured loans	**155.7**	184.9	170.0
Unsecured loans	**4.4**	5.8	5.0
	185.1	244.3	222.6

The Group has returned to lending in the car finance and secured loan market through Paragon Bank. This activity is reported with that division's results.

Idem Capital

Idem Capital is one of the UK's principal consumer debt buyers and is a servicer of loans for third parties and co-investment partners. The strong performance of the division's portfolios in the six month period ended 31 March 2016 saw Idem Capital's underlying profit contribution increase by 8.1% to £25.5 million (31 March 2015: £23.6 million).

The UK debt purchase market continues to provide significant investment opportunities, with UK based financial institutions disposing of both secured and unsecured loan portfolios, either as business-as-usual sales or through deleveraging activity. The latest research by Apex Insight reported the market size in 2015 as £1.0 billion of debt sales, forecast to rise over the next five years to £1.3 billion. Secondary portfolio sales are also now coming to market in greater volumes, as investment funds seek to liquidate assets. Idem Capital continues to be an active panel member for the major UK based debt sellers and intermediaries, ensuring access to all appropriate portfolio disposal processes.

Idem Capital, working in partnership with Paragon Bank, invested £208.8 million in loan portfolio acquisitions in the period to 31 March 2016 (31 March 2015: £20.9 million). This included purchases of loan assets in which Idem Capital had previously had an interest under co-investment arrangements. The table below shows the Group's investments in purchased debt, sourced by Idem Capital, including those funded by Paragon Bank through retail deposits, at 31 March 2016.

	Outstanding balance			Current period net investment		
	31 Mar 2016	31 Mar 2015	30 Sep 2015	**31 Mar 2016**	31 Mar 2015	30 Sep 2015
	£m	£m	£m	**£m**	£m	£m
Idem Capital portfolios	**306.8**	389.2	432.9	**24.0**	20.9	104.4
Co-investments	**-**	17.7	18.1	**-**	-	-
Idem Capital division assets	**306.8**	406.9	451.0	**24.0**	20.9	104.4
Paragon Bank division assets	**286.7**	-	-	**184.8**	-	-
	593.5	406.9	451.0	**208.8**	20.9	104.4

During the period balances to the value of £102.0 million were sold by Idem Capital to Paragon Bank and the related funding was repaid.

The outstanding value of the Group's debt purchase investments at 31 March 2016 totalled £593.5 million (31 March 2015: £406.9 million). Of this balance, 64.3% related to loans secured on property.

At the end of March 2016, the 120 month gross estimated remaining collections ('ERC') for the Idem Capital portfolio stood at £509.6 million (31 March 2015: £639.2 million) (note 6). This reduction was primarily attributable to the intra-group sale of assets into Paragon Bank. ERC is a standard measure of scale in the debt purchase industry, reflecting likely future cash flows from acquired portfolios over the next ten years, which reduces over time as balances are collected. At 31 March 2016, cumulative cash receipts across the Group's portfolio acquisitions totalled 108.2% of the values predicted at the point the loans were acquired (31 March 2015: 105.8%).

The acquisition of loan portfolios during the period has resulted in the number of loan assets owned by Idem Capital increasing to 293,024 at 31 March 2016 (31 March 2015: 212,346). After taking into account portfolio run-off, acquired accounts under Idem Capital management increased by 44.8%. Total accounts under Idem Capital management (including third-party serviced assets) increased by 11.1% in the 12 months ended in March 2016.

The division utilises the Group's highly developed loan servicing and collection capability both for its own purchases and for co-invested and third party assets. The Group has invested heavily in its compliance infrastructure and the division's operational activities are regulated through Paragon Finance PLC, which achieved full authorisation from the FCA under the CONC regime in March of this year.

During the period, Idem Capital successfully raised external finance for both its secured and unsecured portfolios, optimising leverage against these portfolios on more favourable terms. In addition, a partial sale of Idem Capital's secured loan portfolio to Paragon Bank contributed to improving the leverage and funding terms across the Group's acquired portfolios. This is discussed further in the funding report below.

Paragon Bank

The six months to March 2016 represented a period of rapid development for Paragon Bank. In addition to its deposit book more than doubling to just over £1.4 billion, the Bank also broadened its product offerings, acquired loan portfolios and completed the acquisition of Five Arrows Leasing Group, marking its entry into the important asset finance market. The Bank also reported its first underlying profit during the period. The income generated from purchased portfolios progresses the Bank's objective of being viable and sustainable in its own right and also enabled it to acquire assets subsequently approved by the Bank of England for pre-positioning purposes.

Profit before tax of £5.1 million (before costs related to the acquisition of £2.5 million) generated by the asset finance business offset the continuing costs of organic development of the Bank's business. This resulted in the Bank reporting an underlying profit for the period of £1.7 million (2015 H1: £4.4 million loss).

Paragon Bank funds its new lending advances and pipeline though savings deposits. The cost of these funds is discussed further in the funding report below. The Bank's funding position at 31 March 2016 is summarised below.

	Note	**31 Mar 2016**	31 Mar 2015	30 Sep 2015
		£m	£m	£m
Loans to customers	*15*	**1,441.0**	85.6	407.8
Retail deposits	*25*	**1,426.4**	165.0	708.7
Loan to deposit ratio		**101.0%**	51.9%	57.5%

The scale now achieved by Paragon Bank reduces the inefficiencies seen during its start-up phase, when deposit levels were dictated by pipeline requirements as well as income generating asset balances. This more efficient liquidity profile enhances profitability and creates a more normal relationship between deposit levels and the size of the loan portfolio.

The Group provided capital of £153.0 million to Paragon Bank during the period (2015: £nil), £121.0 million to provide funding for external investment and £32.0 million to support organic growth, and its policy is to provide the Bank with sufficient capital to cover its planned requirements over each 12 month period.

Paragon Bank has invested heavily both in the development of the risk and compliance structure required for regulatory purposes and to nurture organic growth across its business lines. All of these lines remain relatively immature and as they grow the Bank will naturally increase the utilisation of the present fixed cost base improving its overall cost effectiveness.

In addition to Paragon Bank providing a diversified funding base for the Group, its second strategic objective is to diversify the Group's income flows. At 31 March 2016 the Bank financed £638.8 million of assets other than buy-to-let mortgages, representing 44.3% of its balance sheet loan assets (31 March 2015: £23.5 million, 27.5%). An analysis of the Bank's loan portfolio is summarised below:

	Outstanding balance			Current period advances and investments		
	31 Mar 2016	31 Mar 2015	30 Sep 2015	**31 Mar 2016**	31 Mar 2015	30 Sep 2015
	£m	£m	£m	**£m**	£m	£m
Buy-to-let	**802.2**	62.1	349.6	**344.1**	61.9	350.0
Car finance	**73.4**	19.7	43.2	**41.2**	15.7	43.9
Personal finance	**325.9**	3.8	15.0	**210.8**	3.8	15.2
Asset finance	**224.9**	-	-	**57.7**	-	-
Other loans	**14.6**	-	-	**1.0**	-	-
	1,441.0	85.6	407.8	**654.8**	81.4	409.1

As well as entering the asset finance market through acquisition, Paragon Bank also launched a development finance offering during the review period. It continues to investigate further opportunities for development, both organically and by acquisition, where these match its risk appetite.

Buy-to-let

Paragon Bank continues to increase its buy-to-let lending, with £344.1 million of advances made (2015 H1: £61.9 million), representing 41.8% of the Group's total buy-to-let advances (2015 H1: 13.9%). At the end of the period its buy-to-let pipeline stood at £199.1 million (31 March 2015: £207.7 million). There have been no accounts over three months in arrears on business written by the Bank up to 31 March 2016 (2015 H1: none). The buy-to-let market is discussed in more detail under 'Paragon Mortgages' above. The products originated by the Bank are complementary to those offered by Paragon Mortgages and are operated across all brands.

In addition to newly originated assets, Paragon Bank acquired the portfolio of loans previously financed in the Group's Paragon Mortgages (No. 17) PLC securitisation. This portfolio, which stood at £110.8 million at 31 March 2016, contained well-seasoned loans which the Bank has pre-positioned with the Bank of England.

Car finance

Car finance volumes have continued to build, with total advances of £41.2 million in the half year (2015 H1: £15.7 million). Paragon Bank's car finance loan book was 69.9% higher than at the start of the period at £73.4 million. The quality of these loans remains high and the percentage of the Bank's car finance accounts which were more than two months in arrears at 31 March 2016 was 0.09% (31 March 2015: none).

Personal finance

The personal finance balances shown below comprise second charge mortgage assets originated by Paragon Bank or purchased by it from third parties or other Group entities:

	Outstanding balance			Current period advances and external investments		
	31 Mar 2016	31 Mar 2015	30 Sep 2015	**31 Mar 2016**	31 Mar 2015	30 Sep 2015
	£m	£m	£m	**£m**	£m	£m
Originations	**39.2**	3.8	15.0	**26.0**	3.8	15.2
Purchased debt	**286.7**	-	-	**184.8**	-	-
	325.9	3.8	15.0	**210.8**	3.8	15.2

The second charge mortgage market experienced further growth over the period with new business volumes for the six months ended 31 March 2016 showing a year on year increase by value of 33.4% to £479 million (2015 H1: £359 million) according to Finance and Leasing Association ('FLA') data. At the same time the average value of new second charge mortgage loans continued to rise, reaching £44,500 (2015 H1: £38,000), an increase of 17.1%.

Paragon Bank's advances in the half year were £26.0 million (31 March 2015: £3.8 million), and the pipeline of new business at the period end was £11.5 million (31 March 2015: £1.0 million). The average loan size is just over £53,000 and the average loan to value ratio is 63%. None of the Bank's originated second charge mortgage accounts were in arrears at 31 March 2016 (31 March 2015: none).

Debt purchase opportunities are sourced through the Group's Idem Capital debt purchase operation, where potential asset purchases fit with Paragon Bank's risk appetite and business model, thereby broadening the scope of both parts of the Group. During the period the Bank has also purchased certain personal finance balances, formerly disclosed in the Idem Capital segment. The UK debt purchase market is discussed further under 'Idem Capital' above.

Paragon Bank's purchased second charge mortgage assets were of high quality at the acquisition date and at 31 March 2016 only 4.22% of these accounts were two months or more in arrears, compared to an industry average of 13.4% reported by the FLA.

Second charge mortgages became regulated under the FCA's 'Mortgages: Conduct of Business' ('MCOB') regime on 21 March 2016 with Paragon Personal Finance completing the required systems enhancements, procedural developments and employee training during the period.

Asset finance

The Group acquired its asset finance business on 3 November 2015. This represents a significant strategic broadening of Paragon Bank's scope into the SME asset finance market and provides an attractive opportunity to deliver growth, addressing a different market to its existing offerings. During the period this business has added £5.1 million to the Bank's profits, before acquisition related costs of £2.5 million.

Paragon Bank Asset Finance was formed, as Five Arrows Leasing Group, in 1988 and was owned by Rothschild & Co from 1996 until its sale to the Group. It offers a range of asset finance products through its subsidiaries to UK SMEs, including equipment, vehicle and construction equipment finance and is also a provider of lease servicing.

The FLA reports the total market for asset finance for businesses at 31 March 2016 covered £60.4 billion of outstanding balances, an increase of 10.0% over the preceding 12 months (31 March 2015: £54.9 billion). Advances in that market in the year then ended were £19.4 billion, an increase of 9.0% on the £17.8 billion recorded in the previous year.

The finance lease assets acquired with the business were £209.1 million (note 5b), which had risen to £224.9 million by the period end, an increase of 7.6%, as a result of new advances in the period since acquisition of £57.7 million. The finance lease assets generated interest income of £10.7 million in the period and its operating lease activities generated a further £3.1 million. The asset finance business generates operating lease income from a fleet of vehicles with a book value of £8.8 million at the end of the period (£7.6 million at acquisition), with £1.5 million of new contracts initiated in the period. The number of loan accounts more than two months in arrears at 31 March at 1.23% remained very low (0.94% at acquisition).

The asset finance team is highly regarded, has a strong credit ethos and has a good cultural fit within the Group's wider business. The development of the current team and infrastructure will be supported by Paragon Bank and will provide the building blocks for further SME finance development, organically and, potentially, by further acquisitions. The current product suite addresses several distinct segments of the SME market, including some specialised niches, and has several growth opportunities in adjacent spaces.

Other loan assets

The other loan assets included in the Paragon Bank segment are set out below.

	Outstanding balance			Current period advances and investments		
	31 Mar 2016	31 Mar 2015	30 Sep 2015	**31 Mar 2016**	31 Mar 2015	30 Sep 2015
	£m	£m	£m	**£m**	£m	£m
Commercial mortgages	**3.4**	-	-	**-**	-	-
Factoring	**9.8**	-	-	*****	-	-
Development finance	**1.0**	-	-	**1.0**	-	
Other loans	**0.4**	-	-	**-**	-	
	14.6	-	-	**1.0**	-	-

The development finance balance represents the first advances through the Group's new operation to provide funding for small scale developments. The proposition launched during the period and has developed a strong network of relationships within the market that are expected to drive sustained growth, focussed on a robust assessment and credit proposition.

The factoring business supports the current customer base within the asset finance business and is well positioned to continue that support and to expand to new customers. The other loan balances above represent legacy portfolios of the acquired business.

* Factoring balances are agreed on a revolving basis and therefore it is not appropriate to quote an advances figure alongside those for other loan types.

Savings

The UK savings market continues to grow strongly, with household balances (including cash ISAs) reported by the Bank of England increasing by over £24.0 billion to £1,056.3 billion in the six months to 31 March 2016 (30 September 2015: £1,031.8 billion). This strong supply has helped to maintain the recent trend for low savings rates with the average annual interest on two year fixed interest bonds, reported by the Bank of England, having declined from 1.54% in September 2015 to 1.10% in March 2016.

Paragon Bank's retail deposits at 31 March 2016 had reached £1,426.4 million (30 September 2015: £708.7 million). The Bank's savings proposition provides customers with a range of transparent deposit options, offering value for money. This also provides the Bank with a stable funding platform, with a focus on attracting term funding to manage interest rate risk and often limiting product availability for short periods of time.

Our straightforward approach and consistently competitive products have been recognised in the industry and by our customers and Paragon Bank was nominated as a finalist for the Best Online Savings Provider award by Moneyfacts for the second consecutive year in October 2015.

Following the period end the Bank launched its first ISA product, initially to existing customers. This represents a significant broadening of the Group's offering into a key part of the UK savings market, with ISA accounts representing £265.5 billion, or 25.1%, of the savings balances reported in the Bank of England data at 31 March 2016.

In customer feedback 93% of those opening a savings account with Paragon Bank between October 2015 and March 2016, who provided data, rated the overall savings process as 'good' or 'very good', while 85% stated that they would 'probably' or 'definitely' take a second product with the Bank.

Financial Report

The acquisition of the Group's asset finance business took place on 3 November 2015. To aid comparison the Group's results for the period are analysed between the acquisition and extant business below. The acquisition results include transaction costs of £1.7 million and other consequential costs of £0.8 million.

Consolidated Results

For the six months ended 31 March 2016

	2016 H1 Acquisition £m	2016 H1 Extant £m	**2016 H1 Total £m**	2015 H1 £m
Interest receivable	10.7	192.7	**203.4**	164.7
Interest payable and similar charges	(2.4)	(91.2)	**(93.6)**	(67.5)
Net interest income	8.3	101.5	**109.8**	97.2
Other operating income	5.0	7.5	**12.5**	6.8
Total operating income	13.3	109.0	**122.3**	104.0
Operating expenses	(10.4)	(39.0)	**(49.4)**	(36.6)
Provisions for losses	(0.3)	(3.2)	**(3.5)**	(3.5)
	2.6	66.8	**69.4**	63.9
Fair value net gains / (losses)	-	0.1	**0.1**	(1.3)
Operating profit being profit on ordinary activities before taxation	2.6	66.9	69.5	62.6
Tax charge on profit on ordinary activities			**(13.6)**	(12.8)
Profit on ordinary activities after taxation			**55.9**	49.8
Basic earnings per share			**19.1p**	16.3p
Diluted earnings per share			**18.8p**	16.0p
Dividend – rate per share for the period			**4.3p**	3.6p

Total operating income increased by 17.6% to £122.3 million (2015 H1: £104.0 million). This represents a 4.8% organic increase combined with the £13.3 million of net income arising from the acquisition.

Within this, net interest income increased to £109.8 million from £97.2 million for the six months ended 31 March 2015. The increase reflects improving margins and growth in the size of the average loan book, which rose by 11.7% to £10,457.8 million (31 March 2015: £9,362.1 million) (note 32).

Annualised net interest margins increased in the six months to 31 March 2016 to 2.11% compared to the 2.09% achieved in the corresponding period last year (note 32), driven by new originations and portfolio purchases having higher margins than those assets redeeming in the period. The costs of the £112.5 million retail bond issued in August 2015 reduced the annualised margin in the period by 0.07 percentage points.

Other operating income was £12.5 million for the six months, compared with £6.8 million in the comparable period in 2015. The increase principally results from the acquisition which contributed £3.1 million of net leasing income and £1.5 million of third party servicing fees.

Operating expenses excluding the acquired business increased by 6.6% to £39.0 million from £36.6 million for the six months ended 31 March 2015. Costs in the acquired business were £10.4 million, including those relating to the acquisition. The asset finance business naturally operates with a cost to income ratio higher than the rest of the Group, in particular with respect to maintenance and specialist servicing options offered alongside the provision of asset finance. This resulted in the cost:income ratio increasing to 40.4% from 35.2% for the corresponding period last year (note 9), although it remains significantly below the industry average.

The cost:income ratio excluding the acquired business was broadly similar to that in the comparable period in the preceding year at 35.8%, despite the relative immaturity of many of the Paragon Bank business lines. The Board remains focused on controlling operating costs through the application of rigorous budgeting and monitoring procedures, and expects the cost:income ratio for the asset finance business to improve as it is integrated into the Group and starts to see the benefits of income growth from its expanded operations.

The charge of £3.5 million for loan impairment has remained stable at the levels seen in the first half of 2015 (2015 H1: £3.5 million), despite the additional provision arising in the asset finance business since acquisition. As an annualised percentage of average loans to customers the impairment charge has remained at 0.07%, the same value as for the six months ended 31 March 2015 (note 32). The Group has seen favourable trends in arrears performance over the period, both in terms of new cases reducing and customers correcting past arrears, whilst increasing property values have served to reduce overall exposure to losses on enforcement of security. The loan books continue to be carefully managed and the credit performance of the buy-to-let book remains exemplary.

Yield curve movements during the period resulted in hedging instrument fair value net gains of £0.1 million (2015 H1: £1.3 million net loss), which do not affect cash flow. The fair value movements of hedged assets or liabilities are expected to trend to zero over time, as such this item represents a timing difference. The Group remains economically and appropriately hedged.

Corporation tax has been charged at an effective rate of 19.6%, compared with 20.4% for the corresponding period last year; the reduction principally arising from the reduction in the rate of UK Corporation Tax applying to the Group in the period.

The identifiable net assets recognised on the acquisition of the asset finance business were £229.9 million, principally arising from its £221.7 million loan book and the goodwill recognised on acquisition was £78.3 million. The acquired business is included in the Paragon Bank segment and its contribution to the Group's consolidated profit for the period was £5.1 million, before costs related to the acquisition of £2.5 million (note 5).

Cash flows from the Group's loan portfolios remain strong, financing investments in each of its three operating divisions. Cash was also utilised for the acquisition, which generated a net cash outflow of £305.3 million, and in the share buy-back programme. This programme commenced during December 2014. In addition to purchases in the year ended 30 September 2015, a further £33.8 million had been deployed during the six months ended 31 March 2016, taking the total outlay under the programme to £83.5 million. Free cash balances were £152.7 million at 31 March 2016 (31 March 2015: £206.7 million) (note 19).

Decreasing gilt yields have increased the accounting value placed on the liabilities of the Group's defined benefit pension plan over the six months ended 31 March 2016, so despite investment return on the plan's assets being higher than expected, the deficit under IAS 19 has increased to £24.0 million from the year end amount of £21.5 million (31 March 2015: £26.0 million). This resulted in an actuarial loss in other comprehensive income of £2.7 million before tax (2015 H1: loss of £8.8 million).

Profits after taxation of £55.9 million (2015 H1: £49.8 million) have been transferred to shareholders' funds, which totalled £964.4 million at the period end (31 March 2015: £952.5 million).

The Group analyses its results between three segments, which are the principal divisions for which performance is monitored:

- Paragon Mortgages includes revenue, in the form of interest and ancillary income, from the Group's first mortgage operations, other than the buy-to-let lending of Paragon Bank, and from other assets remaining in legacy consumer portfolios

- Idem Capital includes revenue generated from assets purchased by the Group's debt investment business, Idem Capital Holdings Limited, other than those financed by Paragon Bank and from third party consumer loan administration activity

- Paragon Bank includes revenue generated from the Group's regulated banking business, Paragon Bank PLC and its subsidiaries including the acquired asset finance companies

The underlying operating profits of these divisions are detailed fully in note 11 and are summarised below.

	Six months to 31 Mar 2016	Six months to 31 Mar 2015
	£m	£m
Underlying profit / (loss)		
Paragon Mortgages	**44.7**	44.7
Idem Capital	**25.5**	23.6
Paragon Bank	**1.7**	(4.4)
	71.9	63.9

An analysis of the Group's financial assets by type is shown in note 15.

The information on related party transactions required by DTR 4.2.8(1) of the Disclosure and Transparency Rules is given in note 31.

Funding Report

During the period the Group has continued to pursue its funding strategy of diversifying its funding base, in particular by making increased use of its retail savings capability through Paragon Bank. The Group has a medium term strategic objective to achieve balance between securitised and retail deposit funding for its new lending activities.

The Group's funding at 31 March 2016 is summarised as follows:

	31 Mar 2016	31 Mar 2015	30 Sep 2015
	£m	£m	£m
Paragon Mortgages	**9,818.0**	9,574.5	9,597.1
Idem Capital	**107.3**	124.9	102.9
Paragon Bank	**1,426.4**	165.0	708.7
Business specific funding	**11,351.7**	9,864.4	10,408.7
Corporate borrowings	**405.0**	293.2	404.9
	11,756.7	10,157.6	10,813.6

Capital markets have remained subdued during the first half of the financial year. Concerns over the impact of negative rates on bank profitability and low European growth rates, together with indications that Chinese economic growth is stalling have dominated investor thinking. Declining commodity prices, particularly for oil, and the announcement during February 2016 of the EU referendum in the UK added to market volatility and credit spreads moved out sharply. Against this backdrop, new issuance has been below trend and, where transactions have completed, issuers have paid a premium compared with levels in preceding periods. Securitisation markets have been equally affected, with few transactions and margins wider, although markets have shown some stability at the wider levels.

This backdrop amplifies the importance of the Group's diversification plans. The Group has been able to fund the bulk of the £1,384.8 million growth in its loans to customers over the twelve months ended 31 March 2016 through its retail deposit taking capability in Paragon Bank, where deposit balances have increased by £1,261.4 million over the same period.

Paragon Mortgages funding

Buy-to-let mortgage originations outside of Paragon Bank are initially funded through three revolving warehouse facilities which totalled £850.0 million at 31 March 2016 (30 September 2015: £950.0 million, 31 March 2015: £550.0 million). Following a review of the available funding one facility, for £100.0 million, was closed in the period, having become redundant through the increased focus on retail deposit funding. This mix of funding sources supports the Group's growth plans in the buy-to-let market.

In the longer term these mortgage loans are funded through the securitisation markets. The Group's 62nd transaction, Paragon Mortgages (No. 24) PLC ('PM24'), for £350.1 million, completed during the period. It priced in difficult market conditions, reflecting an anticipation of increased issuance resulting from several very large portfolio acquisition transactions expected to be refinanced through the securitisation market. This expectation has led to higher margins being demanded by investors on new issues. The Group's warehouse capacity and Paragon Bank funding channel provide the Group with options regarding the timing of its next securitisation transaction.

During the period the mortgage assets held by Paragon Mortgages (No. 17) PLC were sold to Paragon Bank and are now financed with retail deposits.

Alternative markets for Paragon Mortgages funding to the traditional sterling investor base will continue to be rigorously assessed, including the potential for US dollar issuance alongside the euro issuance which has been a feature of the Group's transactions since its Paragon Mortgages (No. 22) PLC securitisation.

Idem Capital funding

Idem Capital has continued with its funding strategy of financing smaller scale acquisitions from the Group's equity while keeping under review the opportunities to introduce external funding when asset volumes make that economically appropriate.

In October 2015, an Idem Capital special purpose vehicle company ('SPV') entered into an agreement to issue £117.3 million of sterling floating rate notes to Citibank NA. These notes bear interest at a rate of one month LIBOR plus 3.5% and the funds raised were used to re-finance existing Idem Capital unsecured loan assets, previously funded intra-group and through an existing SPV, and are secured on those assets. The transaction raised net new funding of £65.5 million. This agreement was extended by £4.1 million in the period and a further £70.8 million was raised through this arrangement after the period end.

Later in the period other Idem Capital borrowings were repaid following the sale of the underlying assets to Paragon Bank, reducing funding costs, and the Bank joined with Idem Capital in a portfolio purchase transaction. As a result of these transactions, at 31 March 2016 the funding of the Group's debt purchase assets was distributed as shown below.

	31 Mar 2016	31 Mar 2015	30 Sep 2015
	£m	£m	£m
External funding	**195.6**	302.2	275.6
Retail funding	**286.7**	-	-
Group resources	**111.2**	87.0	157.3
	593.5	389.2	432.9

This demonstrates increased flexibility in the Group's funding for its debt purchase activities, broadening its sources of finance and demonstrating its ability to access third party funding on a more regular basis. The participation of Paragon Bank in transactions offers greater flexibility in terms of deal size and asset class, where increasingly the focus will move to more strongly performing portfolios.

Paragon Bank funding

The Bank currently targets the UK savings market. It accepts deposits through the internet, which are processed by a highly automated system with significant scope for future expansion. By 31 March 2016 Paragon Bank held deposits of £1,426.4 million (30 September 2015: £708.7 million).

Savings balances at the period end are analysed below.

	Average interest rate		Average initial balance		Proportion of deposits	
	31 Mar 2016	30 Sep 2015	**31 Mar 2016**	30 Sep 2015	**31 Mar 2016**	30 Sep 2015
	%	%	**£000**	£000	**%**	%
Fixed rate deposits	**2.31%**	2.33%	**33**	34	**62.4%**	71.7%
Variable rate deposits	**1.67%**	1.62%	**16**	16	**37.6%**	28.3%
All balances	**2.07%**	2.13%	**26**	28	**100.0%**	100.0%

The average initial term of fixed rate deposits at 31 March 2016 was 24 months (30 September 2015: 29 months).

During the period savings deposits were used to finance a large part of the cash requirement for the asset finance acquisition and were also used to refinance loan assets originally funded within the Paragon Mortgages and Idem Capital divisions. With the Bank expected to contribute increasingly to the Group's originations, the scale of its deposit-taking activities is expected to expand materially over the next few years.

Paragon Bank has also concluded arrangements to pre-position its acquired buy-to-let mortgages with the Bank of England, giving it access to standby funding. In addition the Bank anticipates making its first drawings under the Finance for Lending scheme during the coming quarter.

Corporate funding

While the Group's working capital has been primarily provided by equity since 2008, in recent years it has expanded its use of corporate debt funding, allowing it to diversify its funding base and extend the tenor of its borrowings.

The Group is rated by Fitch Ratings, which has ascribed it a BBB- rating and confirmed that rating with a stable outlook on 5 May 2016. With a strategy to increase holding company leverage levels over time, the rating will support long dated corporate debt issuance in both scale and pricing terms.

Further information on all of the above borrowings is given in note 26.

Capital Management

The Group continues to be strongly cash generative with free cash balances of £152.7 million at 31 March 2016 (30 September 2015: £199.9 million) (note 19) after investing cash in developing business streams across each of its three divisions. The Company sees opportunities going forward to deploy capital to support organic growth and invest in portfolio purchases and potentially in M&A opportunities.

Dividend and dividend policy

In pursuance of its dividend policy and in view of the strong position of the Group and its confidence in the prospects for the business, the Board proposes an interim dividend of 4.3p per share (2015 H1: 3.6p) payable to shareholders on the register on 1 July 2016. This represents an increase of 19.4% from 2015. The Group's dividend policy is to achieve a dividend cover ratio of three times by the current financial year.

Regulatory capital

PRA supervision of the Group imposes consolidated capital adequacy rules upon it. The Group maintains extremely strong capital and leverage ratios, with a CET1 ratio of 16.1% at 31 March 2016 (30 September 2015: 19.1%) and a leverage ratio at 6.7% (30 September 2015: 7.7%) (note 4d), leaving the Group's capital at 31 March 2016 comfortably in excess of the regulatory requirement. The reduction in the CET1 ratio and leverage percentage during the period are principally effects of the asset finance acquisition and the Group's share buy-back programme.

The Group notes the consultation paper issued by the Basel Committee on Banking Supervision ('BCBS') on 15 December 2015 regarding the proposed amendments to the Standardised Approach ('SA') for assessing the capital adequacy of institutions. The most material proposal relates to a potential increase in the risk weightings applicable to buy-to-let lending assets. The Group considers that the proposed risk weightings do not properly reflect the strong credit performance of the asset class in the UK and has engaged with both the PRA and the BCBS as part of the consultation process. The BCBS has also issued a consultation paper in March 2016, proposing revisions to the Internal Ratings Basis ('IRB') for assessing capital, which is based on firms' own internal calculations and subject to supervisory approval. The proposals may serve to limit the comparative advantage available to IRB users over SA users through the use of floors.

Notwithstanding the outcome of these consultations, the Group has a wealth of data and excellent credit metrics to support the use of an IRB approach for assessing the appropriate buy-to-let risk weightings. Other UK institutions that currently use the IRB approach for their buy-to-let portfolios achieve materially lower risk weightings than the 35% required by the present SA, with figures reported by the PRA in July 2015 as being typically in the low to mid-teen percentages.

In addition to the potential risk weighting advantages from adopting the IRB approach, the Group sees broader business benefits from adopting the disciplines required by IRB as a core part of its risk management structure.

The Group will be closely monitoring developments in both of these consultations as they progress and is conducting investigatory and preparatory work so that it can progress an IRB application, if appropriate, once the regulatory position has been clarified.

Gearing and share buy-backs

In view of the strong capital base and low leverage in the Company's balance sheet, the Board has determined that the Group's debt and equity capital resources should be rebalanced to deliver returns at a higher rate to shareholders. To enhance this strategy the Group regularly reviews the opportunities available to add incremental long-dated debt to the Group balance sheet.

In November 2014 the Group announced a share buy-back programme, initially for up to £50.0 million and extended to £100.0 million in 2015, to be reviewed periodically to take account of anticipated investment opportunities and the balance of the Group's debt and equity capital resources. During the period the Group bought back a further 10.5 million of its ordinary shares at a cost of £33.8 million, which are held in treasury (note 23). This brings the total number of shares acquired to 22.3 million at a cost of £83.5 million. This programme will continue during the second half year with these shares also being held in treasury.

The Company currently has the necessary shareholder approval to undertake such share buy-backs under an authority granted at its 2016 Annual General Meeting, when a special resolution seeking authority for the Company to purchase up to 29.6 million of its own shares (10% of the issued share capital excluding treasury shares) was approved by shareholders.

The share buy-back programme, together with the issue of debt, has reduced the amount of the Group's central funding represented by equity at 31 March 2016 to 79.0% from 91.5% 12 months earlier (note 4c), with this trend expected to continue.

The Board keeps under review the appropriate level of capital for the business to meet its operational requirements and strategic development objectives. The strength of the Paragon Mortgages and Idem Capital businesses, the diversification which has been achieved in the funding base in recent years and the further opportunities for growth and sustainability provided by Paragon Bank, have now created the foundations on which to develop the Group's next phase of growth.

Operations Report

Management and People

The Group has always recognised that its people are key to its future growth and development. The training and development of employees together with a rigorous recruitment and selection process are a key part of the Group's organic growth strategy and underpin the strong progress made.

The Living Wage is an important part of the Group's values and people strategy and the Group supports the principle espoused by the Living Wage Foundation of it being good for business, good for the individual and good for society. The Group's pay levels meet the requirements of the National Living Wage and it continues to work with its supply chain in order to adopt the UK Living Wage Foundation standard by the end of the current financial year.

During the period the Group exceeded 1,250 employees as its operations expanded to welcome new colleagues within the acquired asset finance business, following its acquisition in November. Since acquisition a programme of rolling out the Group's standards in training and development to the new employees has been developed while existing employees learn from their skills and experience in asset finance, to further develop our future growth plans.

The Group prides itself on the high retention rate in its workforce. Its annual employee attrition rate of 12% is below the national average and 32% of its people have been with Paragon for more than ten years, with 10% having achieved over 20 years' service. We believe this is due to providing quality development opportunities and creating a place at which people want to work, which has in turn meant that knowledge and experience have been retained in each of our specialist areas. The Group has continued to add to the team over the past six months with an excellent set of people at all levels of the organisation, increasing numbers by 1.5% over the period, excluding the impact of the asset finance acquisition. In February 2016 the Group's Investors in People status was reaccredited with the Gold Standard, putting it in the top 1% of employers in the UK. We believe our people are well positioned to support the Group's future growth strategy.

During the period an internal mentoring programme, accredited by the Chartered Management Institute, was launched, helping to support succession planning strategy and develop future leaders. Further work has continued with local secondary schools, colleges and universities, with industrial placements and apprenticeships becoming a feature for some of the Group's specialist areas. Regulatory training programmes have been launched to ensure employees remain competent to deliver good customer outcomes and there are over 100 employees completing professional qualifications at any one time across the Group.

The health and wellbeing of the Group's employees is an important element of its people strategy. During the period the Group began offering lifestyle assessments and new discounted gym memberships, while updating its employee assistance programme with external occupational health support. The Group also ran its first annual health awareness week in April 2016.

Risk

The Group's risk governance framework is based upon a formal three lines of defence model which is being embedded in all areas. Credit, Asset and Liability and Operational Risk and Compliance committees, formed of senior management, report to the board level Risk and Compliance Committee, the membership of which comprises the Chairman and the independent non-executive directors of the Company.

In the last six months the Group has strengthened its risk resource in areas such as operational risk and credit risk. These appointments have been made to ensure that subject matter experts are in place ahead of planned future growth to help shape policy and process.

The Group's governance structure provides an effective basis for the management of risk within which:

- The **first line of defence**, comprising executive directors, managers and employees, holds primary responsibility for designing, operating and monitoring risk management and control processes

- The **second line of defence** is provided by the Risk and Compliance division, the Risk and Compliance Committee and its supporting sub-committees

- The **third line of defence** is provided by the Group Internal Audit function and the Audit Committee which are responsible for reviewing the effectiveness of the first and second lines of defence

The principal changes in the risk environment faced by the Group over the six month period are;

- Impact of the forthcoming EU referendum on the UK economy and capital markets

- Execution risk on the asset finance transaction as the business is integrated into the Group

- New operational risks arising from the acquired operations

- Potential impact of changes in the regulatory and fiscal environment for buy-to-let mortgages in the UK, in particular for the Group's future advances and redemption levels

- Impact of new proposals on capital regulation from the BCBS

The Group is carefully monitoring these risks as they develop and considers itself well placed to mitigate their impact.

A summary of the principal risks and uncertainties faced by the Group is given on page 70.

Regulation

In March 2015 the Mortgage Credit Directive Order introduced legislation to move second charge mortgages from the FCA's consumer credit regime to its residential mortgage regime and to implement a new regulatory regime, to be overseen by the FCA, in relation to consumer buy-to-let mortgage contracts. Having decided to continue offering such loans, the Group put in place the necessary processes and procedures to comply with both regimes from their implementation date of March 2016 and was granted the appropriate permissions by the FCA before this date. The changes involved did not have a material impact on the operation of any of the Group's business lines.

During the period the Financial Policy Committee of the Bank of England ('FPC') was granted powers to regulate owner-occupied mortgage lending. The FPC has also requested the power to regulate buy-to-let mortgage lending by reference to loan-to-value, debt to income and ICRs. The UK Government is currently consulting on this request. The PRA published a consultation paper during March 2016 which sets out a regulatory approach in relation to underwriting standards for buy-to-let mortgages, designed to address the risk of lenders relaxing underwriting standards to achieve higher lending volumes. The Group has, or will, respond to both of these consultation documents, whilst at the same time taking steps to determine what amendments to policy or process, if any, the proposed changes may require.

Paragon Bank is authorised by the PRA and regulated by the PRA and the FCA. The Group is subject to consolidated supervision by the PRA. The current and projected rate of regulatory change, driven by domestic and European policy, is significant, as further aspects of the Basel III supervisory regime are rolled out and the BCBS consults on further changes. The governance and control structure within Paragon Bank and the wider Group has been established and developed to ensure that the impacts of new requirements on the business are clearly understood and planned for. Regular reports on key regulatory developments are therefore received at both executive and board risk committees.

Current BCBS consultations on regulatory capital requirements and their potential impact on the Group are discussed under 'Capital Management' above.

Conclusion

This has been another outstanding performance by the Group, with strong profit growth complemented by significant progress in our lending activity and further development in our diversification strategy.

The Group's progress was evident across each of its operating divisions. Paragon Bank reported its maiden profit, achieving this in less than two years after launch, whilst also completing the acquisition of Five Arrows providing an entry platform to the SME asset finance sector. Idem Capital saw extensive acquisition activity supporting further growth in the consumer finance loan book, particularly through co-investment opportunities with Paragon Bank. Finally buy-to-let, whilst maintaining our disciplined approach to credit and pricing, witnessed strong new lending levels influenced in part by the increase in Stamp Duty, pulling forward some business into the first half of the year. Strong tenant demand is set to continue to drive the need for rented property in the UK for the foreseeable future. Whilst there is some uncertainty over the longer term growth prospects in buy-to-let, we expect the tax and regulatory changes to provide relative benefits for the Group's specialist lending focus, in particular, the more complex requirements of professional landlords.

Paragon operates with a strong capital base and an enviable credit record. Its leading position in the specialist buy-to-let market is now being complemented by a broader and more diversified series of business lines, including SME lending. This leaves the Group well placed to continue to develop and deliver increasingly broad product offerings for our customers, which in turn supports improving returns for our shareholders.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The directors confirm that, to the best of their knowledge:

- the condensed financial statements have been prepared in accordance with International Accounting Standard 34 – 'Interim Financial Reporting';
- the Interim Management Report includes a fair review of the information required by Section 4.2.7R of the Disclosure and Transparency Rules, issued by the UK Listing Authority (an indication of important events that have occurred during the first six months of the current financial year and their impact on the condensed financial statements and a description of the principal risks and uncertainties for the remaining six months of the financial year); and
- the Interim Management Report includes a fair review of the information required by Section 4.2.8R of the Disclosure and Transparency Rules, issued by the UK Listing Authority (disclosure of related party transactions that have taken place in the first six months of the financial year and that have materially affected the financial position or the performance of the enterprise during that period; and any changes in the related party transactions described in the last annual report which could do so)

Approved by the Board of Directors and signed on behalf of the Board.

Pandora Sharp

Company Secretary

24 May 2016

Board of Directors

Robert G Dench
Nigel S Terrington
Richard J Woodman
John A Heron
Fiona J Clutterbuck
Alan K Fletcher
Peter J N Hartill
Hugo R Tudor

CONDENSED FINANCIAL STATEMENTS

Consolidated Income Statement

For the six months ended 31 March 2016 (Unaudited)

	Note	**Six months to 31 Mar 2016 £m**	Six months to 31 Mar 2015 £m	Year to 30 Sep 2015 £m
Interest receivable		**203.4**	164.7	341.0
Interest payable and similar charges		**(93.6)**	(67.5)	(143.6)
Net interest income		**109.8**	97.2	197.4
Other operating income	*8*	**12.5**	6.8	14.1
Total operating income		**122.3**	104.0	211.5
Operating expenses		**(49.4)**	(36.6)	(71.2)
Provisions for losses		**(3.5)**	(3.5)	(5.6)
Operating profit before fair value items		**69.4**	63.9	134.7
Fair value net gains / (losses)	*10*	**0.1**	(1.3)	(0.5)
Operating profit being profit on ordinary activities before taxation		**69.5**	62.6	134.2
Tax charge on profit on ordinary activities	*12*	**(13.6)**	(12.8)	(27.1)
Profit on ordinary activities after taxation		**55.9**	49.8	107.1

	Note	**Six months to 31 Mar 2016**	Six months to 31 Mar 2015	Year to 30 Sep 2015
Basic earnings per share	*13*	**19.1p**	16.3p	35.5p
Diluted earnings per share	*13*	**18.8p**	16.0p	34.8p
Dividend – rate per share for the period	*22*	**4.3p**	3.6p	11.0p

The results for the periods shown above relate entirely to continuing operations.

Consolidated Statement of Comprehensive Income

Six months ended 31 March 2016 (Unaudited)

	Note	**Six months to 31 Mar 2016**	Six months to 31 Mar 2015	Year to 30 Sep 2015
		£m	£m	£m
Profit for the period		**55.9**	49.8	107.1
Other comprehensive income / (expenditure)				
Items that will not be reclassified subsequently to profit or loss				
Actuarial (loss) on pension plan	*27*	**(2.7)**	(8.8)	(4.3)
Tax thereon		**0.5**	1.8	0.9
		(2.2)	(7.0)	(3.4)
Items that may be reclassified subsequently to profit or loss				
Cash flow hedge gains / (losses) taken to equity		**1.5**	(2.5)	(3.1)
Tax thereon		**(0.3)**	0.5	0.6
		1.2	(2.0)	(2.5)
Other comprehensive (expenditure) for the period net of tax		**(1.0)**	(9.0)	(5.9)
Total comprehensive income for the period		**54.9**	40.8	101.2

Consolidated Balance Sheet

31 March 2016 (Unaudited)

	Note	31 Mar 2016 £m	31 Mar 2015 £m	30 Sep 2015 £m	30 Sep 2014 £m
Assets employed					
Non-current assets					
Intangible assets	14	**87.0**	7.6	7.7	7.9
Property, plant and equipment		**36.7**	22.8	22.1	22.9
Financial assets	15	**11,800.3**	10,300.2	10,745.8	9,969.6
		11,924.0	10,330.6	10,775.6	10,000.4
Current assets					
Other receivables		**9.5**	6.1	6.2	6.5
Short term investments	18	**17.3**	48.5	41.1	39.4
Cash and cash equivalents	19	**895.3**	812.6	1,056.0	848.8
		922.1	867.2	1,103.3	894.7
Total assets		**12,846.1**	11,197.8	11,878.9	10,895.1
Financed by Equity shareholders' funds					
Called-up share capital	20	**309.6**	308.9	309.3	307.3
Reserves	21	**793.4**	709.0	760.2	688.0
Share capital and reserves		**1,103.0**	1,017.9	1,069.5	995.3
Own shares	23	**(138.6)**	(65.4)	(100.0)	(48.2)
Total equity		**964.4**	952.5	969.5	947.1
Current liabilities					
Financial liabilities	24	**809.5**	101.3	339.6	54.4
Current tax liabilities		**16.7**	11.4	12.5	11.9
Other liabilities		**63.3**	36.2	43.0	40.1
		889.5	148.9	395.1	106.4
Non-current liabilities					
Financial liabilities	24	**10,958.4**	10,061.5	10,481.4	9,814.0
Retirement benefit obligations	27	**24.0**	26.0	21.5	17.3
Deferred tax		**8.1**	8.7	11.3	10.1
Other liabilities		**1.7**	0.2	0.1	0.2
		10,992.2	10,096.4	10,514.3	9,841.6
Total liabilities		**11,881.7**	10,245.3	10,909.4	9,948.0
		12,846.1	11,197.8	11,878.9	10,895.1

The condensed financial statements for the half year were approved by the Board of Directors on 24 May 2016.

Consolidated Cash Flow Statement

For the six months ended 31 March 2016 (Unaudited)

	Note	**Six months to 31 Mar 2016 £m**	Six months to 31 Mar 2015 £m	Year to 30 Sep 2015 £m
Net cash flow generated / (utilised) by operating activities	*28*	**243.1**	(47.5)	(25.9)
Net cash (utilised) by investing activities	*29*	**(285.9)**	(10.2)	(3.6)
Net cash (utilised) / generated by financing activities	*30*	**(118.2)**	22.4	237.1
Net (decrease) / increase in cash and cash equivalents		**(161.0)**	(35.3)	207.6
Opening cash and cash equivalents		**1,055.3**	847.7	847.7
Closing cash and cash equivalents		**894.3**	812.4	1,055.3
Represented by balances within				
Cash and cash equivalents	*19*	**895.3**	812.6	1,056.0
Financial liabilities		**(1.0)**	(0.2)	(0.7)
		894.3	812.4	1,055.3

Consolidated Statement of Movements in Equity

Six months ended 31 March 2016 (Unaudited)

	Note	**Six months to 31 Mar 2016 £m**	Six months to 31 Mar 2015 £m	Year to 30 Sep 2015 £m
Total comprehensive income for the period		**54.9**	40.8	101.2
Dividends paid	*22*	**(21.7)**	(18.3)	(29.1)
Net movement in own shares		**(38.6)**	(17.2)	(51.8)
Deficit on transactions in own shares		**(1.3)**	(3.9)	(3.6)
Charge for share based remuneration		**2.1**	2.6	4.5
Tax on share based remuneration		**(0.5)**	1.4	1.2
Total movements in equity in the period		**(5.1)**	5.4	22.4
Opening equity		**969.5**	947.1	947.1
Closing equity		**964.4**	952.5	969.5

Selected Notes to the Accounts

For the six months ended 31 March 2016 (Unaudited)

1. General Information

The condensed financial statements are prepared for The Paragon Group of Companies PLC and its subsidiary companies ('the Group') on a consolidated basis.

The condensed financial statements for the six months ended 31 March 2016 and for the six months ended 31 March 2015 have not been audited, as defined in section 434 of the Companies Act 2006.

The figures shown above for the years ended 30 September 2015 and 30 September 2014 are not statutory accounts. A copy of the statutory accounts for each year has been delivered to the Registrar of Companies. The auditors reported on those statutory accounts and their reports were unqualified, did not draw attention to any matters by way of emphasis and did not contain an adverse statement under sections 498 (2) or 498 (3) of the Companies Act 2006.

A copy of the half-yearly financial report will be posted to those shareholders who have requested to receive one and additional copies can be obtained from the Company Secretary, The Paragon Group of Companies PLC, 51 Homer Road, Solihull, West Midlands, B91 3QJ.

This half-yearly financial report is also available on the Group's website at www.paragon-group.co.uk.

2. Accounting Policies

The condensed financial statements are presented in accordance with the requirements of International Accounting Standard 34 – 'Interim Financial Reporting'.

The Group prepares its annual financial statements in accordance with International Financial Reporting Standards as endorsed by the European Union. The condensed financial statements have been prepared on the basis of the accounting policies set out in the Annual Report and Accounts of the Group for the year ended 30 September 2015, which are expected to be used in the preparation of the financial statements of the Group for the year ending 30 September 2016.

Going concern basis

The business activities of the Group, its current operations and those factors likely to affect its future results and development, together with a description of its financial position and funding position, are described in the Interim Management Report on pages 7 to 28. The principal risks and uncertainties affecting the Group in the forthcoming six months are described on page 70.

Note 6 to the accounts for the year ended 30 September 2015 includes an analysis of the Group's working capital position and policies, while note 7 includes a detailed description of its funding structures, its use of financial instruments, its financial risk management objectives and policies and its exposure to credit, interest rate and liquidity risk. Note 5 to those accounts discusses critical accounting estimates affecting the results and financial position disclosed therein. The position and policies described in these notes remain materially unchanged to the date of this half-yearly report, except for the acquisition of PBAF, described in note 5 and the changes in funding described in note 26.

The Group has a formalised process of budgeting, reporting and review. The Group's planning procedures forecast its profitability, capital position, funding requirement and cash flows. Detailed plans are produced for a rolling 24 month period with longer term forecasts covering a 5 year period. These plans provide information to the directors which is used to ensure the adequacy of resources available for the Group to meet its business objectives, both on a short term and strategic basis.

The Group's securitisation funding structures ensure that both a substantial proportion of its originated loan portfolio and a significant amount of its acquired Idem Capital assets are match-funded. Repayment of the securitisation borrowings is restricted to funds generated by the underlying assets and there is limited recourse to the Group's general funds. Recent and current loan originations utilising the Group's available warehouse facilities are refinanced through securitisation from time to time.

The Group's retail deposits of £1,426.4m (note 25), accepted through Paragon Bank are repayable within five years, with 56.7% of this balance (£808.5m) payable within twelve months of the balance sheet date. The liquidity exposure represented by these deposits is monitored; a process supervised by the Asset and Liability Committees of the Group and Paragon Bank. The Group is required to hold liquid assets in Paragon Bank to mitigate this liquidity risk. At 31 March 2016 Paragon Bank held £121.4m in liquid assets, £17.3m of short term investments (note 18) and £104.1m of cash (note 19).

Paragon Bank manages its liquidity in line with the Board's risk appetite and the requirements of the PRA, which are formally documented in the Board's approved Individual Liquidity Adequacy Assessment Process ('ILAAP'). The Bank maintains a liquidity framework that includes a short to medium term cash flow requirement analysis, a longer term funding plan and access to the Bank of England's liquidity insurance facilities.

The earliest maturity of any of the Group's working capital debt is in April 2017, when the £110.0m corporate bond is repayable. The outstanding principal balance of the Group's retail bonds at 31 March 2016 was £297.5m, none of which is repayable before December 2020.

The Group has concluded, based on its cash forecasts described above, that it will be able to refinance the £110.0m borrowing on its due date. This analysis was based on the current strong free cash balances, the levels of cash flows being generated by its securitisation investments, the Group's ability to raise retail bond debt under the programme renewed in January 2016, and its history of raising new corporate debt when required through this and other programmes. It also noted that the cash forecast contained significant major discretionary cash flows.

At 31 March 2016 the Group had free cash balances of £152.7m immediately available for use (note 19).

As described in note 4 the Group's capital base is subject to consolidated supervision by the PRA. Its capital at 31 March 2016 was in excess of regulatory requirements and its forecasts show this continuing to be the case.

Accounting standards require the directors to assess the Group's ability to continue to adopt the going concern basis of accounting. In performing this assessment, the directors consider all available information about the future, the possible outcomes of events and changes in conditions and the realistically possible responses to such events and conditions that would be available to them, having regard to those aspects of the 'Guidance on Risk Management, Internal Control and Related Financial and Business Reporting' published by the Financial Reporting Council in September 2014 applicable to half-yearly reporting.

After performing this assessment the directors concluded that it was appropriate for them to continue to adopt the going concern basis in preparing the half-yearly report.

3. Fair Values of Financial Assets and Financial Liabilities

Fair values have been determined for all derivatives, listed securities and any other financial assets and liabilities for which an active and liquid market exists.

Derivative financial instruments are stated at their fair values in the accounts. The Group uses a number of techniques to determine the fair values of its derivative assets and liabilities, for which observable prices in active markets are not available. These are principally present value calculations based on estimated future cash flows arising from the instruments, discounted using a risk adjusted interest rate. The principal inputs to these valuation models are LIBOR benchmark interest rates for the currencies in which the instruments are denominated, sterling, euros and dollars. The cross currency basis swaps have a notional principal related to the outstanding currency borrowings and therefore the estimated rate of repayment of these notes also affects the valuation of the swaps. In order to determine the fair values management apply valuation adjustments to observed data where that data would not fully reflect the attributes of the instrument being valued, such as particular contractual features or the identity of the counterparty. Management reviews the models used on an ongoing basis to ensure that the valuations produced are reasonable and reflect all relevant factors.

For assets and liabilities carried at fair value, IFRS 7 requires that the measurements should be classified using a fair value hierarchy reflecting the inputs used, and defines three levels. Level 1 measurements are unadjusted market prices, level 2 measurements are derived from observable data, such as market prices or rates, while level 3 measurements rely on significant inputs which are not derived from observable data. As described above the valuations of the Group's derivatives are based on market information and they are therefore classified as level 2 measurements. Details of these assets are given in note 17. The short term investments described in note 18 are freely traded securities for which a market price quotation is available and are classified as level 1 measurements. The Group had no financial assets or liabilities in the six months ended 31 March 2016 or the year ended 30 September 2015 valued using level 3 measurements.

The fair values of cash and cash equivalents, bank loans and overdrafts and asset backed loan notes, which are carried at amortised cost are considered to be not materially different from their book values. In arriving at that conclusion market inputs have been considered but because all the assets mature within three months of the period end and the interest rates charged on financial liabilities reset to market rates on a quarterly basis, little difference arises. While the Group's asset backed loan notes are listed, the quoted prices for an individual note may not be indicative of the fair value of the issue as a whole, due to the specialised nature of the market in such instruments and the limited number of investors participating in it and an adjustment is required. As these valuation exercises are not wholly market based they are considered to be level 2 measurements.

To assess the likely fair value of the Group's retail deposit liabilities, the directors have considered the estimated cash flows expected to arise based on a mixture of market based inputs, such as rates and pricing and non-market based inputs such as redemption rates. On this basis they have concluded that the carrying value of these liabilities, determined on the amortised cost basis, is not significantly different from their fair value derived on a discounted cash flow basis. Given the mixture of observable and non-observable inputs, these are considered to be level 2 measurements as the observable inputs are the most significant.

To assess the likely fair value of the Group's loan assets in the absence of a liquid market, the directors have considered the estimated cash flows expected to arise from the Group's investments in its loans to customers based on a mixture of market based inputs, such as rates and pricing and non-market based inputs such as redemption rates. On this basis they have concluded that the carrying value of these assets, determined on the amortised cost basis, is not significantly different from the fair value of the assets derived on a discounted cash flow basis. Given the mixture of observable and non-observable inputs these are considered to be level 2 measurements as the observable inputs are the most significant.

4. Capital Management

The Group's objectives in managing capital are:

- To ensure that the Group has sufficient capital to meet its operational requirements and strategic objectives;
- To safeguard the Group's ability to continue as a going concern, so that it can continue to provide returns to shareholders and benefits for other stakeholders;
- To provide an adequate return to shareholders by pricing products and services commensurately with the level of risk; and
- To ensure that sufficient regulatory capital is available to meet any externally imposed requirements

The Group sets the amount of capital in proportion to risk, availability and cost. The Group manages the capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying assets, having particular regard to the relative costs and availability of debt and equity finance at any given time. In order to maintain or adjust the capital structure the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares, issue or redeem other capital instruments, such as retail or corporate bonds, or sell assets to reduce debt.

The Group is subject to regulatory capital rules imposed by the Prudential Regulation Authority ('PRA') on a consolidated basis as a group containing an authorised bank. This is discussed further below.

(a) Dividend policy

The Group's dividend policy, announced in 2012 has been to target a dividend cover ratio of between 3.0 and 3.5 times by the end of this financial year. The dividend cover ratio had reached 3.2 times in respect of the year ended 30 September 2015 and the Group stated its aim to reach the bottom of the target range at the end of the current year. The Group considers that it has sufficient cash resources available to pay dividends at this level, and that the parent company has abundant distributable reserves for this purpose.

The Group's intention is that this policy should apply in the medium term, subject to any changes in the Group's capital position caused by regulatory changes or through major corporate transactions, when the policy would be amended. Before the payment of any dividend the continuing appropriateness of the policy, the availability of free cash resources and the distributable reserves position of the parent company are reviewed.

(b) Return on tangible equity

Return on tangible equity ('RoTE') is a measure of an entity's profitability used by investors. RoTE is defined by the Group by comparing the profit after tax for the period, adjusted for amortisation charged on intangible assets, to the average of the opening and closing equity positions, excluding intangible assets and goodwill. The Groups consolidated annualised RoTE for the six months ended 31 March 2016 is derived as follows:

	31 Mar 2016	31 Mar 2015	30 Sep 2015	30 Sep 2014
	£m	£m	£m	£m
Profit for the period	**55.9**	49.8	107.1	97.2
Amortisation of intangible assets	**0.7**	0.7	1.4	1.3
Adjusted profit	**56.6**	50.5	108.5	98.5
Divided by				
Opening equity	**969.5**	947.1	947.1	873.3
Opening intangible assets	**(7.7)**	(7.9)	(7.9)	(8.5)
Opening tangible equity	**961.8**	939.2	939.2	864.8
Closing equity	**964.4**	952.5	969.5	947.1
Closing intangible assets	**(87.0)**	(7.6)	(7.7)	(7.9)
Closing tangible equity	**877.4**	944.9	961.8	939.2
Average tangible equity	**919.6**	942.0	950.5	902.0
Return on tangible equity	**12.7%**	11.0%	11.4%	10.9%

(c) Gearing

The Board of Directors regularly review the proportion of working capital represented by debt and equity. Net debt is calculated as total debt, other than securitised and warehouse debt, valued at principal value, less free cash up to a maximum of the total debt. Adjusted equity comprises all components of equity (i.e. share capital, share premium, minority interest, retained earnings, and revaluation surplus) other than amounts recognised in equity relating to cash flow hedges.

The debt and equity amounts at 31 March 2016 were as follows:

	Note	**31 Mar 2016**	31 Mar 2015	30 Sep 2015	30 Sep 2014
		£m	£m	£m	£m
Debt					
Corporate bond		**110.0**	110.0	110.0	110.0
Retail bonds		**297.5**	185.0	297.5	185.0
Bank overdraft		**1.0**	0.2	0.7	1.1
Less: Applicable free cash	19	**(152.7)**	(206.7)	(199.9)	(177.3)
Net debt		**255.8**	88.5	208.3	118.8
Equity					
Total equity		**964.4**	952.5	969.5	947.1
Less: cash flow hedging reserve	21	**0.7**	1.4	1.9	(0.6)
Adjusted equity		**965.1**	953.9	971.4	946.5
Total working capital		**1,220.9**	1,042.4	1,179.7	1,065.3
Debt		**21.0%**	8.5%	17.7%	11.2%
Equity		**79.0%**	91.5%	82.3%	88.8%
Total working capital		**100.0%**	100.0%	100.0%	100.0%

The movements in the proportion of working capital represented by debt and equity during the period resulted primarily from the operation of the policy described above.

(d) Regulatory capital

The Group is subject to supervision by the PRA on a consolidated basis, as a group containing an authorised bank. As part of this supervision the regulator issues individual capital guidance setting an amount of regulatory capital, defined under the international Basel III rules, implemented through the Capital Requirements Regulation and Directive ('CRD IV'), which the Group is required to hold relative to its risk weighted assets in order to safeguard depositors against the risk of losses being incurred by the Group.

The Group's regulatory capital is monitored by the Board of Directors, its Risk and Compliance Committee and the Asset and Liability Committee, who ensure that appropriate action is taken to ensure compliance with the regulator's requirements. The future regulatory capital requirement is also considered as part of the Group's forecasting and strategic planning process.

At 31 March 2016 the Group's regulatory capital of £891.9m (31 March 2015: £981.9m, 30 September 2015: £976.3m) was comfortably in excess of that required by the regulator.

The Group's regulatory capital differs from its equity as certain adjustments are required by the regulator. A reconciliation of the Group's equity to its regulatory capital determined in accordance with CRD IV at 31 March 2016 is set out below.

	Note	**31 Mar 2016**	31 Mar 2015	30 Sep 2015	30 Sep 2014
		£m	£m	£m	£m
Total equity		**964.4**	952.5	969.5	947.1
Deductions					
Proposed dividend	22	**(12.2)**	(10.9)	(21.8)	(18.3)
Intangible assets	14	**(87.0)**	(7.6)	(7.7)	(7.9)
Deferred tax adjustment	*	**-**	(0.5)	(0.3)	(0.5)
Common Equity Tier 1 ('CET1') capital		**865.2**	933.5	939.7	920.4
Other tier 1 capital		**-**	-	-	-
Total Tier 1 capital		**865.2**	933.5	939.7	920.4
Corporate bond	24	**110.0**	110.0	110.0	110.0
Less: amortisation adjustment	†	**(86.8)**	(64.8)	(75.8)	(53.8)
		23.2	45.2	34.2	56.2
Collectively assessed credit impairment allowances		**3.5**	3.2	2.4	4.5
Total Tier 2 capital		**26.7**	48.4	36.6	60.7
Total regulatory capital		**891.9**	981.9	976.3	981.1

* Deferred tax assets in subsidiary companies are required to be deducted from regulatory capital. This balance is offset against the deferred tax liability in the consolidated accounts.

† When tier 2 capital instruments have less than five years to maturity the amount eligible as regulatory capital reduces by 20% per annum on a straight line basis. The Group's £110.0m Corporate Bond matures in 2017 and therefore such an amortisation adjustment is required.

The total risk exposure calculated under the CRD IV framework, against which this capital is held, and the proportion of this exposure it represents, are calculated as shown below.

	31 Mar 2016	31 Mar 2015	30 Sep 2015
	£m	£m	£m
Credit risk			
Balance sheet assets	**4,860.9**	4,231.8	4,426.8
Off balance sheet	**65.7**	110.3	88.7
Total credit risk	**4,926.6**	4,342.1	4,515.5
Operational risk	**409.7**	337.1	363.6
Market risk	-	-	-
Other	**53.6**	104.8	50.2
Total risk exposure	**5,389.9**	4,784.0	4,929.3
Solvency ratios	**%**	%	%
CET1	**16.1%**	19.5%	19.1%
Total regulatory capital	**16.5%**	20.5%	19.8%

This table not covered by the Independent Review Report

The CRD IV risk weightings for credit risk exposures are calculated using the Standardised Approach. Operational risk is calculated using the Basic Indicator Approach.

The table below shows the calculation of the leverage ratio, based on the consolidated balance sheet assets adjusted as shown below:

	Note	31 Mar 2016	31 Mar 2015	30 Sep 2015
		£m	£m	£m
Total balance sheet assets		**12,846.1**	11,197.8	11,878.9
Less: Derivative assets	*17*	**(939.9)**	(810.9)	(660.1)
On-balance sheet items		**11,906.2**	10,386.9	11,218.8
Less: Intangible assets	*14*	**(87.0)**	(7.6)	(7.7)
Total on balance sheet exposures		**11,819.2**	10,379.3	11,211.1
Derivative assets	*17*	**939.9**	810.9	660.1
Potential future exposure on derivatives		**71.2**	73.0	69.1
Total derivative exposures		**1,011.1**	883.9	729.2
Post offer pipeline at gross notional amount		**292.9**	617.0	482.3
Adjustment to convert to credit equivalent amounts		**(146.4)**	(308.5)	(241.1)
Off balance sheet items		**146.5**	308.5	241.2
Tier 1 capital		**865.2**	933.5	939.7
Total leverage exposure		**12,976.8**	11,571.7	12,181.5
Basel III leverage ratio		**6.7%**	8.1%	7.7%

This table not covered by the Independent Review Report

The regulatory capital disclosures in these financial statements relate only to the consolidated position for the Group. Individual entities within the Group are also subject to supervision on a standalone basis. All such entities complied with the requirements to which they were subject during the period.

5. Acquisition

On 3 November 2015 the Group acquired the entire share capital of Paragon Bank Asset Finance Limited ('PBAF') (formerly Five Arrows Leasing Group Limited) from Rothschild & Co. PBAF is the parent company of a group of companies ('PBAF Group') providing a range of asset finance products to UK SMEs, including equipment, vehicle and construction equipment finance and is also a provider of lease servicing. The acquisition allows the Group to diversify its range of both products and the markets it serves within the financial services sector.

The Group acquired 100% of the voting equity interests in PBAF and the consideration was satisfied entirely in cash. Cash transferred on completion was £308.2m, £117.0m in respect of equity and £191.2m to settle existing debt owed by PBAF Group to the vendor. There are no contingent consideration arrangements. Transaction costs of £1.7m have been included in operating expenses for the six months ended 31 March 2016.

The principal operating companies of the PBAF Group are listed below.

Company	Principal Activity
Paragon Bank Asset Finance Limited *(Five Arrows Leasing Group Limited at acquisition)*	Holding company and portfolio administration
Dash Commercial Finance Limited	Asset finance
Paragon Bank Business Finance PLC *(Five Arrows Business Finance PLC at acquisition)*	Asset finance
Paragon Bank Technology Finance *(Five Arrows Media Finance Limited at acquisition)*	Asset finance
Specialist Fleet Services Limited	Asset finance and contract hire

CONDENSED FINANCIAL STATEMENTS

The contribution of PBAF Group to consolidated revenue for the six months ended 31 March 2016 was £18.2m and its contribution to consolidated profit before tax for the period is set out below.

	£m	£m
Contribution to consolidated profit excluding costs of acquisition		5.1
Transaction costs	(1.7)	
Other acquisition related expenses	(0.8)	
		(2.5)
Contribution to consolidated profit after costs of acquisition		2.6

Had the acquisition taken place on 1 October 2015, the consolidated revenue of the Group for the six months ended 31 March 2016 would have been £221.9m and its consolidated profit before tax for the period would have been £70.4m.

The amounts recognised in the consolidated accounts on acquisition in respect of the identifiable assets acquired and liabilities assumed are set out below. The amounts presented are considered to be materially consistent with the existing accounting policies of the Group.

The Group has yet to finalise its exercise to determine these balances and therefore the amounts presented in this note should be considered as provisional. Final amounts will be presented with the Group's annual results for the year ending 30 September 2016.

	Note	£m	£m
Non-current assets			
Operating lease assets		10.8	
Other property, plant and equipment		1.6	
Property, plant and equipment		12.4	
Intangible assets	*a*	1.0	
Loans to customers	*b*	221.7	
Deferred tax		3.7	
			238.8
Current assets			
Other receivables		5.2	
Cash		3.4	
			8.6
			247.4
Current liabilities			
Financial liabilities- bank overdraft	*c*	0.5	
Current tax liabilities		0.5	
Other liabilities		16.5	
			17.5
Total liabilities			17.5
Total net identifiable assets			229.9
Goodwill	*d*		78.3
Consideration	*c*		308.2

a) Intangible assets

Identifiable intangible assets acquired represent broker networks and trading arrangements. They will be amortised over a ten year period.

b) Loans to customers

The financial assets acquired at 3 November 2015 comprised:

	Fair value	Gross Contractual Value	Contractual flows not to be collected
	£m	£m	£m
Asset finance leases	209.1	213.2	2.2
Commercial mortgages	3.6	4.2	0.5
Factoring	8.6	8.6	-
Other loans	0.4	0.4	-
Loans to customers	221.7	226.4	2.7

c) Cash flows on acquisition

Net cashflows on acquisition were:

	Note	Total
		£m
Payment for shares		117.0
Settlement of existing vendor balances		191.2
Consideration paid on completion		308.2
Cash		(3.4)
Bank overdraft		0.5
Net cash outflow	*29*	305.3

The fair value and the gross contractual value of the cash balances acquired was equal to their book value, there are no contractual flows which are expected not to be collectable.

d) Goodwill

The goodwill of £78.3m arising from the acquisition consists of the values of the business relationships, market positions and knowledge base inherent in the business which do not qualify for recognition as intangible assets. These will be utilised in the future development of the acquired business and in expanding the Group's asset finance activities. None of the goodwill is expected to be deductible for tax purposes.

While a full review of the goodwill arising in the transaction for the purposes of IAS 36 – 'Impairment of Assets' has yet to be completed, a preliminary exercise has identified no indications of impairment.

6. Credit Risk

The Group's business objectives rely on maintaining a high-quality customer base and place strong emphasis on good credit management, both at the time of acquiring or underwriting a new loan, where strict lending criteria are applied, and throughout the loan's life.

The Group's credit risk is primarily attributable to its loans to customers. There are no significant concentrations of credit risk to individual counterparties due to the large number of customers included in the portfolios.

The Group's loan assets at 31 March 2016 are analysed as follows:

	31 Mar 2016		31 Mar 2015		30 Sep 2015	
	£m	**%**	£m	%	£m	%
Buy-to-let mortgages	**9,736.3**	**89.7%**	8,826.6	93.2%	9,363.2	93.0%
Owner occupied mortgages	**25.0**	**0.2%**	53.6	0.6%	47.6	0.5%
Total first mortgages	**9,761.3**	**89.9%**	8,880.2	93.8%	9,410.8	93.5%
Secured loans	**562.1**	**5.2%**	409.7	4.3%	387.1	3.9%
Loans secured on residential property	**10,323.4**	**95.1%**	9,289.9	98.1%	9,797.9	97.4%
Development finance	**1.0**	**-**	-	-	-	-
Commercial mortgages	**3.4**	**-**	-	-	-	-
Loans secured on property	**10,327.8**	**95.1%**	9,289.9	98.1%	9,797.9	97.4%
Car loans	**73.6**	**0.7%**	20.0	0.2%	43.4	0.4%
Retail finance loans	**0.2**	**-**	0.3	-	0.2	-
Other consumer loans	**216.4**	**2.0%**	158.1	1.7%	220.9	2.2%
Asset finance loans	**224.9**	**2.1%**	-	-	-	-
Factoring balances	**9.8**	**0.1%**	-	-	-	-
Other loans	**0.4**	**-**	-	-	-	-
Total loans to customers	**10,853.1**	**100.0%**	9,468.3	100.0%	10,062.4	100.0%

Other loans include unsecured loans either advanced by Group companies or acquired from their originators at a discount.

An analysis of the indexed loan to value ratio ('LTV') for those loan accounts secured on property by value at 31 March 2016 is set out below. For acquired accounts the effect of any discount on purchase is allowed for.

	31 Mar 2016		31 Mar 2015		30 Sep 2015	
	First Mortgages	**Secured Loans**	First Mortgages	Secured Loans	First Mortgages	Secured Loans
	%	**%**	%	%	%	%
Loan to value ratio						
Less than 70%	**52.0**	**40.3**	47.2	29.0	51.9	33.7
70% to 80%	**28.2**	**18.6**	27.0	14.2	27.6	16.3
80% to 90%	**11.7**	**16.5**	15.3	17.7	12.8	16.7
90% to 100%	**5.4**	**11.9**	7.0	15.6	4.9	13.5
Over 100%	**2.7**	**12.7**	3.5	23.5	2.8	19.8
	100.0	**100.0**	100.0	100.0	100.0	100.0
Average loan to value ratio	**69.3**	**78.2**	71.7	84.3	69.5	80.9
Buy-to-let	**69.5**		72.0		69.7	
Owner-occupied	**28.9**		31.9		28.8	

The regionally indexed LTVs shown above are affected by changes in house prices, with the Nationwide house price index, for the UK as a whole, registering an increase of 3.1% during the six months ended 31 March 2016 and an annual increase of 3.8% in the year ended 30 September 2015.

The number of accounts in arrears by asset class, based on the most commonly quoted definition of arrears for the type of asset, at 31 March 2016, 31 March 2015 and 30 September 2015, compared to the industry averages at those dates published by the Council of Mortgage Lenders ('CML') and the Finance and Leasing Association ('FLA'), was:

	31 Mar 2016	31 Mar 2015	30 Sep 2015
	%	%	%
First mortgages			
Accounts more than three months in arrears			
- Buy-to-Let accounts including receiver of rent cases	**0.14**	0.20	0.19
- Buy-to-Let accounts excluding receiver of rent cases	**0.02**	0.03	0.04
- Owner Occupied accounts	**3.13**	3.24	3.55
CML data for mortgage accounts more than three months in arrears			
- Buy-to-Let accounts including receiver of rent cases	**0.56**	0.74	0.66
- Buy-to-Let accounts excluding receiver of rent cases	**0.51**	0.66	0.60
- Owner Occupied accounts	**1.14**	1.36	1.27
- All mortgages	**1.04**	1.26	1.17
Secured loans			
Accounts more than two months in arrears	**17.01**	19.70	19.56
FLA data for secured loans	**13.40**	16.50	15.80
Car loans			
Accounts more than two months in arrears	**0.43**	2.02	0.67
FLA data for all personal loans	**3.40**	3.50	3.00
Asset finance loans			
Accounts more than two months in arrears	**1.23**	-	-
FLA data for business lease / hire purchase loans	**0.60**	0.70	0.60
Other loans			
Accounts more than two months in arrears	**95.64**	91.27	94.66

No published industry data for asset classes comparable to the Group's other books has been identified. Where revised data at 30 September 2015 has been published by the FLA or CML, the comparative industry figures above have been amended.

The Group calculates its headline arrears measure for buy-to-let mortgages, shown above, based on the numbers of accounts three months or more in arrears, including purchased Idem Capital assets, but excluding those cases in possession and receiver of rent cases designated for sale. This is consistent with the methodology used by the CML in compiling its statistics for the buy-to-let mortgage market as a whole.

The number of accounts in arrears will be higher for closed books such as the owner occupied mortgage book and the retail finance and unsecured loan books than for comparable active ones, as performing accounts pay off their balances, leaving arrears accounts representing a greater proportion of the total.

The improvement in the arrears position for car loans shown above is due to the recommencement of lending in this market, through Paragon Bank, with the new performing cases reducing the overall average.

The figures shown above for secured loans and other loans include purchased portfolios which generally include a high proportion of cases in arrears at the time of purchase and where this level of performance is allowed for in the discount to current balance represented by the purchase price.

The payment status of the carrying balances of the Group's live loan assets, before provision for impairment at 31 March 2016, 31 March 2015 and at 30 September 2015 split between those accounts considered as performing and those included in the population for impairment testing, is shown below. Balances for immaterial asset classes are not shown.

First Mortgages

	31 Mar 2016	31 Mar 2015	30 Sep 2015
	£m	£m	£m
Performing accounts (less than three months arrears)	**9,733.2**	8,838.9	9,374.8
Impairment population	**50.1**	60.0	53.3
	9,783.3	8,898.9	9,428.1

Consumer and Asset Finance

	Secured loans	**Car loans**	**Asset finance loans**	**Total**
	£m	**£m**	**£m**	**£m**
31 Mar 2016				
Performing accounts (less than two months arrears)	479.2	73.9	224.8	777.9
Impairment population	95.0	0.4	4.3	99.7
	574.2	74.3	229.1	877.6
31 Mar 2015				
Performing accounts (less than two months arrears)	305.9	20.1	-	326.0
Impairment population	108.6	0.4	-	109.0
	414.5	20.5	-	435.0
30 Sep 2015				
Performing accounts (less than two months arrears)	325.0	5.8	-	330.8
Impairment population	116.0	0.7	-	116.7
	441.0	6.5	-	447.5

Other Loans

	31 Mar 2016	31 Mar 2015	30 Sep 2015
	£m	£m	£m
Performing accounts (less than one month arrears)	**6.0**	10.4	7.2
Impairment population	**227.4**	166.6	230.6
	233.4	177.0	237.8

Arrears in the tables above are based on the contractual payment status of the customers concerned. Where assets have been purchased by the Idem Capital loan investment business, customers may already have been in arrears at the time of acquisition and an appropriate adjustment made to the consideration paid.

In the debt purchase industry, Estimated Remaining Collections ('ERC') is commonly used as a measure of the value of a portfolio. This is defined as the sum of the undiscounted cash flows expected to be received over a specified future period. In the Group's view, this measure may be suitable for heavily discounted, unsecured, distressed portfolios, but is less applicable for the types of portfolio in which the Group has invested, where cash flows are higher on acquisition, loans may be secured on property and customers may not be in default. In such cases, the IAS 39 amortised cost balance, at which these assets are carried in the Group balance sheet, provides a better indication of value.

However, to aid comparability, the 84 and 120 month ERC values for the Group's purchased assets are set out below, analysed by the balance sheet line on which they appear. These are derived from the same models and assumptions used in the effective interest rate calculations.

	31 Mar 2016	31 Mar 2015	30 Sep 2015	30 Sep 2014
	£m	£m	£m	£m
Carrying value				
Loans to customers	**593.5**	389.2	432.9	407.2
Investments in structured entities	**-**	17.7	18.1	19.3
	593.5	406.9	451.0	426.5
84 month ERC				
Loans to customers	**716.8**	521.7	555.1	554.8
Investments in structured entities	**-**	24.9	25.7	26.6
	716.8	546.6	580.8	581.4
120 month ERC				
Loans to customers	**823.2**	609.3	647.3	649.9
Investments in structured entities	**-**	29.9	30.4	32.3
	823.2	639.2	677.7	682.2

The analysis of these balances between the Idem Capital and Paragon Bank segments is shown in note 15.

Amounts shown as loans to customers above include loans disclosed as first mortgages and other loans (note 15).

7. Segmental Results

The Group analyses its operations, both for internal management reporting and external financial reporting, on the basis of the entities within the Group generating its assets. The segments used are described below.

- Paragon Mortgages includes revenue, in the form of interest and ancillary income, from the Group's first mortgage operations, other than the buy-to-let lending of Paragon Bank, and from assets remaining in other, legacy, portfolios

- Idem Capital includes revenue generated from assets purchased by the Group's debt investment business, Idem Capital Holdings Limited, other than those financed by Paragon Bank and from third party loan administration activity

- Paragon Bank includes revenue, in the form of interest and ancillary income, generated from the Group's regulated banking business, Paragon Bank PLC and its subsidiary companies including the PBAF group

Each of these businesses invests in consumer finance or SME finance assets. An analysis of the Group's financial assets by type is shown in note 15.

Dedicated financing and administration costs of each of these businesses are allocated to the segment and shared costs, and the financing costs of the Group's working capital invested, are allocated based on the segments' use of those resources.

No profit has been recognised in the segmental disclosures below in respect of transfers of loan assets between segments.

The costs arising from the PBAF acquisition in the period of £2.5m are included in the Paragon Bank segmental profit and loss account for the half year.

Financial information about these business segments is shown below.

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Six months ended 31 March 2016

	Paragon Mortgages	Idem Capital	Paragon Bank	Total
	£m	£m	£m	£m
Interest receivable	135.3	42.8	25.3	203.4
Interest payable	(73.9)	(7.3)	(12.4)	(93.6)
Net interest income	61.4	35.5	12.9	109.8
Other operating income	3.9	3.2	5.4	12.5
Total operating income	65.3	38.7	18.3	122.3
Operating expenses	(17.5)	(13.2)	(18.7)	(49.4)
Provisions for losses	(3.1)	-	(0.4)	(3.5)
	44.7	25.5	(0.8)	69.4
Fair value net gain / (loss)	(0.1)	-	0.2	0.1
Operating profit / (loss)	44.6	25.5	(0.6)	69.5
Tax charge				(13.6)
Profit after taxation				**55.9**

Six months ended 31 March 2015

	Paragon Mortgages £m	Idem Capital £m	Paragon Bank £m	Total £m
Interest receivable	128.6	35.0	1.1	164.7
Interest payable	(61.4)	(5.1)	(1.0)	(67.5)
Net interest income	67.2	29.9	0.1	97.2
Other operating income	4.0	2.8	-	6.8
Total operating income	71.2	32.7	0.1	104.0
Operating expenses	(23.0)	(9.1)	(4.5)	(36.6)
Provisions for losses	(3.5)	-	-	(3.5)
	44.7	23.6	(4.4)	63.9
Fair value net gain / (loss)	(1.2)	-	(0.1)	(1.3)
Operating profit / (loss)	43.5	23.6	(4.5)	62.6
Tax charge				(12.8)
Profit after taxation				**49.8**

Year ended 30 September 2015

	Paragon Mortgages £m	Idem Capital £m	Paragon Bank £m	Total £m
Interest receivable	263.2	71.6	6.2	341.0
Interest payable	(128.1)	(9.9)	(5.6)	(143.6)
Net interest income	135.1	61.7	0.6	197.4
Other operating income	8.5	5.3	0.3	14.1
Total operating income	143.6	67.0	0.9	211.5
Operating expenses	(44.0)	(17.7)	(9.5)	(71.2)
Provisions for losses	(5.6)	-	-	(5.6)
	94.0	49.3	(8.6)	134.7
Fair value net gain / (loss)	(0.4)	-	(0.1)	(0.5)
Operating profit / (loss)	93.6	49.3	(8.7)	134.2
Tax charge				(27.1)
Profit after taxation				**107.1**

The assets of the segments listed above are:

	31 Mar 2016 £m	31 Mar 2015 £m	30 Sep 2015 £m	30 Sep 2014 £m
Paragon Mortgages	**10,844.1**	10,559.4	10,622.9	10,343.3
Idem Capital	**338.0**	429.3	481.2	445.8
Paragon Bank	**1,664.0**	209.1	774.8	106.0
Total assets	**12,846.1**	11,197.8	11,878.9	10,895.1

8. Other Operating Income

	31 Mar 2016	31 Mar 2015	30 Sep 2015
	£m	£m	£m
Loan account fee income	**3.6**	3.1	6.7
Operating lease income	**3.1**	-	-
Insurance income	**0.6**	0.5	1.2
Third party servicing	**4.6**	2.6	4.9
Other income	**0.6**	0.6	1.3
	12.5	6.8	14.1

9. Cost:income Ratio

Cost:income ratio is derived as follows:

	31 Mar 2016	31 Mar 2015	30 Sep 2015
	£m	£m	£m
Operating expenses (£m)	49.4	36.6	71.2
Total operating income (£m)	122.3	104.0	211.5
Cost ÷ Income	**40.4%**	35.2%	33.7%

Cost:income ratio excluding the impact of the acquired business is derived as follows:

	31 Mar 2016	31 Mar 2015	30 Sep 2015
	£m	£m	£m
Operating expenses (£m)	**49.4**	36.6	71.2
Operating expenses of PBAF (£m)	**(10.4)**	-	-
Operating expenses excluding PBAF (£m)	**39.0**	36.6	71.2
Operating income (£m)	**122.3**	104.0	211.5
Operating income of PBAF (£m)	**(13.3)**	-	-
Operating income excluding PBAF (£m)	**109.0**	104.0	211.5
Cost ÷ Income	**35.8%**	35.2%	33.7%

10. Fair Value Net Gains / (Losses)

The fair value net gain / (loss) represents the accounting volatility on derivative instruments which are matching risk exposure on an economic basis generated by the requirements of IAS 39. Some accounting volatility arises on these items due to accounting ineffectiveness on designated hedges, or because hedge accounting has not been adopted or is not achievable on certain items. The losses are primarily due to timing differences in income recognition between the derivative instruments and the economically hedged assets and liabilities. Such differences will reverse over time and have no impact on the cash flows of the Group.

11. Underlying Profit

Underlying profit is determined by excluding from the operating result one off costs relating to the acquisition of PBAF (note 5) and fair value accounting adjustments arising from the Group's hedging arrangements.

	Note	**31 Mar 2016**	31 Mar 2015	30 Sep 2015
		£m	£m	£m
Paragon Mortgages				
Profit before tax for the period	*7*	**44.6**	43.5	93.6
Exclude: Acquisition related costs		**-**	-	-
Exclude: Fair value losses / (gains)		**0.1**	1.2	0.4
		44.7	44.7	94.0
Idem Capital				
Profit before tax for the period	*7*	**25.5**	23.6	49.3
Exclude: Acquisition related costs		**-**	-	-
Exclude: Fair value losses / (gains)		**-**	-	-
		25.5	23.6	49.3
Paragon Bank				
(Loss) before tax for the period	*7*	**(0.6)**	(4.5)	(8.7)
Exclude: Acquisition related costs	*5*	**2.5**	-	-
Exclude: Fair value losses / (gains)		**(0.2)**	0.1	0.1
		1.7	(4.4)	(8.6)
Total				
Profit before tax for the period		**69.5**	62.6	134.2
Exclude: Acquisition related costs		**2.5**	-	-
Exclude: Fair value losses / (gains)		**(0.1)**	1.3	0.5
Underlying profit before tax		**71.9**	63.9	134.7

12. Tax Charge on Profit on Ordinary Activities

Income tax for the six months ended 31 March 2016 is charged at 19.6% (six months ended 31 March 2015: 20.4%, year ended 30 September 2015: 20.2%), representing the best estimate of the annual effective rate of income tax expected for the full year, applied to the pre-tax income of the period.

13. Earnings Per Share

Earnings per ordinary share is calculated as follows:

	31 Mar 2016	31 Mar 2015	30 Sep 2015
Profit for the period (£m)	**55.9**	49.8	107.1
Basic weighted average number of ordinary shares ranking for dividend during the period (£m)	**291.8**	304.9	301.9
Dilutive effect of the weighted average number of share options and incentive plans in issue during the period (£m)	**5.5**	7.1	5.9
Diluted weighted average number of ordinary shares ranking for dividend during the period (£m)	**297.3**	312.0	307.8
Earnings per ordinary share			
- basic	**19.1p**	16.3p	35.5p
- diluted	**18.8p**	16.0p	34.8p

14. Intangible Assets

Intangible assets at net book value comprise:

	31 Mar 2016 £m	31 Mar 2015 £m	30 Sep 2015 £m	30 Sep 2014 £m
Goodwill	**80.0**	1.6	1.6	1.6
Computer software	**1.9**	1.3	1.6	1.3
Other intangibles	**5.1**	4.7	4.5	5.0
Total assets	**87.0**	7.6	7.7	7.9

The increase in goodwill and intangible assets in the period is principally due to the acquisition described in note 5.

15. Financial Assets

	Note	31 Mar 2016 £m	31 Mar 2015 £m	30 Sep 2015 £m	30 Sep 2014 £m
Loans to customers		**10,853.1**	9,468.3	10,062.4	9,255.9
Fair value adjustments from portfolio hedging		**7.3**	3.3	5.2	0.5
Investments in structured entities		**-**	17.7	18.1	19.3
Derivative financial assets	*17*	**939.9**	810.9	660.1	693.9
Total assets		**11,800.3**	10,300.2	10,745.8	9,969.6

During the period the structured entities in which the Group had invested sold their loan assets to the Group and the investments of the participants, including the Group, were repaid.

The Group's loans to customers and investments in structured entities at 31 March 2016, analysed between the segments described in note 7, were as follows:

	31 Mar 2016	31 Mar 2015	30 Sep 2015	30 Sep 2014
	£m	£m	£m	£m
Paragon Mortgages				
First mortgage loans	**8,945.2**	8,802.8	9,046.7	8,635.2
Consumer loans	**160.1**	190.7	175.0	207.7
Asset finance	**-**	-	-	-
Other loans	**-**	-	-	-
Loans to customers	**9,105.3**	8,993.5	9,221.7	8,842.9
Investments in structured entities	**-**	-	-	-
Total investment in loans	**9,105.3**	8,993.5	9,221.7	8,842.9
Idem Capital				
First mortgage loans	**13.9**	15.3	14.5	16.0
Consumer loans	**292.9**	373.9	418.4	391.2
Asset finance	**-**	-	-	-
Other loans	**-**	-	-	-
Loans to customers	**306.8**	389.2	432.9	407.2
Investments in structured entities	**-**	17.7	18.1	19.3
Total investment in loans	**306.8**	406.9	451.0	426.5
Paragon Bank				
First mortgage loans	**802.2**	62.1	349.6	0.5
Consumer loans	**399.3**	23.5	58.2	5.3
Asset finance	**224.9**	-	-	-
Other loans	**14.6**	-	-	-
Loans to customers	**1,441.0**	85.6	407.8	5.8
Investments in structured entities	**-**	-	-	-
Total investment in loans	**1,441.0**	85.6	407.8	5.8
Total				
First mortgage loans	**9,761.3**	8,880.2	9,410.8	8,651.7
Consumer loans	**852.3**	588.1	651.6	604.2
Asset finance	**224.9**	-	-	-
Other loans	**14.6**	-	-	-
Loans to customers	**10,853.1**	9,468.3	10,062.4	9,255.9
Investments in structured entities	**-**	17.7	18.1	19.3
Total investment in loans	**10,853.1**	9,486.0	10,080.5	9,275.2

Of the assets shown above, the balances acquired through the Group's Idem Capital debt purchase operation were as follows:

	31 Mar 2016	31 Mar 2015	30 Sep 2015	30 Sep 2014
	£m	£m	£m	£m
Loans to customers				
Idem Capital	**306.8**	389.2	432.9	407.2
Paragon Bank	**286.7**	-	-	-
	593.5	389.2	432.9	407.2
Investments in structured entities				
Idem Capital	**-**	17.7	18.1	19.3
Paragon Bank	**-**	-	-	-
	-	17.7	18.1	19.3
Total purchased debt interests	**593.5**	406.9	451.0	426.5

16. Impairment Provisions on Loans to Customers

The following amounts in respect of impairment provisions, net of allowances for recoveries of written off assets, have been deducted from the appropriate assets in the balance sheet.

	First mortgages	**Other loans and receivables**	**Finance leases**	**Total**
	£m	**£m**	**£m**	**£m**
At 30 September 2015	86.0	24.4	0.6	111.0
Charge for the period	2.4	0.8	0.3	3.5
Amounts written off	(1.0)	(2.1)	-	(3.1)
Amounts recovered	-	0.4	0.2	0.6
At 31 March 2016	**87.4**	**23.5**	**1.1**	**112.0**
At 30 September 2014	87.0	27.0	0.8	114.8
Charge for the period	2.0	1.7	(0.2)	3.5
Amounts written off	(2.0)	(2.8)	(0.2)	(5.0)
Amounts recovered	0.1	0.6	0.1	0.8
At 31 March 2015	87.1	26.5	0.5	114.1
At 30 September 2014	87.0	27.0	0.8	114.8
Charge for the year	3.6	2.4	(0.4)	5.6
Amounts written off	(4.5)	(3.5)	0.2	(7.8)
Amounts recovered	(0.1)	(1.5)	-	(1.6)
At 30 September 2015	86.0	24.4	0.6	111.0

Of the above balances, the following provisions were held in respect of realised losses not charged off, which remain on the balance sheet and provided for in full.

	First mortgages	Other loans and receivables	Finance leases	Total
	£m	£m	£m	£m
At 31 March 2016	**71.3**	**0.2**	**0.2**	**71.7**
At 31 March 2015	69.1	0.2	0.1	69.4
At 30 September 2015	70.7	0.3	0.1	71.1

17. Derivative Financial Assets and Liabilities

	Note	**31 Mar 2016**	31 Mar 2015	30 Sep 2015	30 Sep 2014
		£m	£m	£m	£m
Derivative financial assets	15	**939.9**	810.9	660.1	693.9
Derivative financial liabilities	24	**(10.2)**	(5.0)	(6.7)	(1.1)
		929.7	805.9	653.4	692.8
Of which:					
Foreign exchange basis swaps		**938.4**	810.6	659.8	693.5
Other derivatives		**(8.7)**	(4.7)	(6.4)	(0.7)
		929.7	805.9	653.4	692.8

The Group's securitisation borrowings are denominated in sterling, euros and US dollars. All currency borrowings are swapped at inception so that they have the effect of sterling borrowings. These swaps provide an effective hedge against exchange rate movements, but the requirement to carry them at fair value leads, when exchange rates have moved significantly since the issue of the notes, to large balances for the swaps being carried in the balance sheet. This is currently the case with both euro and US dollar swaps, although the debit balance is compensated for by retranslating the borrowings at the current exchange rate.

18. Short Term Investments

This amount represents treasury bills and other liquid securities held as part of the liquidity requirement of Paragon Bank PLC. As such they are designated as 'Available for Sale', as defined by IAS 39 - 'Financial Instruments: Recognition and Measurement' and are consequently shown at market value.

19. Cash and Cash Equivalents

	31 Mar 2016	31 Mar 2015	30 Sep 2015	30 Sep 2014
	£m	£m	£m	£m
Balances with central banks	**81.5**	59.0	286.0	-
Balances with other banks	**813.8**	753.6	770.0	848.8
	895.3	812.6	1,056.0	848.8

Only 'Free Cash' is unrestrictedly available for the Group's general purposes. Cash received in respect of loan assets is not immediately available, due to the terms of the warehouse facilities and the securitisations. Cash held in the Group's banking entity, Paragon Bank, and its subsidiaries is subject to regulatory rules covering liquidity and capital adequacy, and is shown as 'Bank Cash' below.

'Cash and Cash Equivalents' also includes balances held by the Trustees of the Paragon Employee Share Ownership Plans which may only be used to invest in the shares of the Company, pursuant to the aims of those plans.

The total 'Cash and Cash Equivalents' balance may be analysed as shown below:

	31 Mar 2016	31 Mar 2015	30 Sep 2015	30 Sep 2014
	£m	£m	£m	£m
Free cash	**152.7**	206.7	199.9	177.3
Securitisation cash	**636.1**	531.3	530.9	609.0
Bank cash	**104.1**	72.7	323.3	60.6
ESOP cash	**2.4**	1.9	1.9	1.9
	895.3	812.6	1,056.0	848.8

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20. Called-Up Share Capital

Movements in the issued share capital in the period were:

	Six months to 31 Mar 2016	Six months to 31 Mar 2015	Year to 30 Sep 2015
	Number	Number	Number
Ordinary shares of £1 each			
At 1 October 2015	**309,349,316**	307,308,283	307,308,283
Shares issued	**213,425**	1,637,402	2,041,033
At 31 March 2016	**309,562,741**	308,945,685	309,349,316

During the period the Company issued 163,045 shares at par (six months ended 31 March 2015: 800,000; year ended 30 September 2015: 1,050,000) to the trustees of its ESOP Trusts in order that they could fulfil their obligations under the Group's share based award arrangements. It also issued 50,380 shares (six months ended 31 March 2015: 837,402; year ended 30 September 2015: 991,033) to satisfy options granted under sharesave schemes for a consideration of £55,730 (six months ended 31 March 2015: £1,193,801; year ended 30 September 2015: £1,365,944).

21. Reserves

	31 Mar 2016	31 Mar 2015	30 Sep 2015	30 Sep 2014
	£m	£m	£m	£m
Share premium account	**64.6**	64.5	64.6	64.1
Merger reserve	**(70.2)**	(70.2)	(70.2)	(70.2)
Cash flow hedging reserve	**(0.7)**	(1.4)	(1.9)	0.6
Profit and loss account	**799.7**	716.1	767.7	693.5
	793.4	709.0	760.2	688.0

22. Equity Dividend

Amounts recognised as distributions to equity shareholders in the period:

	Six months to 31 Mar 2016	Six months to 31 Mar 2015	Year to 30 Sep 2015
	£m	£m	£m
Final dividend for the year ended 30 September 2015 of 7.4p per share	**21.7**	-	-
Final dividend for the year ended 30 September 2014 of 6.0p per share	**-**	18.3	18.3
Interim dividend for the year ended 30 September 2015 of 3.6p per share	**-**	-	10.8
	21.7	18.3	29.1

An interim dividend of 4.3p per share is proposed (2015: 3.6p per share), payable on 22 July 2016 with a record date of 1 July 2016. The amount expected to be absorbed by this dividend, based on the number of shares in issue at the balance sheet date is £12.2m (2015: £10.9m). The interim dividend will be recognised in the accounts when it is paid.

23. Own Shares

	31 Mar 2016	31 Mar 2015	30 Sep 2015
	£m	£m	£m
Treasury shares			
At 1 October 2015	**89.2**	39.5	39.5
Shares purchased	**33.8**	17.2	49.7
At 31 March 2016	**123.0**	56.7	89.2
ESOP shares			
At 1 October 2015	**10.8**	8.7	8.7
Shares purchased	**6.2**	5.1	7.2
Shares subscribed for	**0.2**	0.8	1.0
Options exercised	**(1.6)**	(5.9)	(6.1)
At 31 March 2016	**15.6**	8.7	10.8
Total at 31 March 2016	**138.6**	65.4	100.0
Total at 1 October 2015	**100.0**	48.2	48.2
Number of shares held			
Treasury	**22,941,909**	4,763,900	12,401,400
ESOP	**3,224,335**	879,075	1,562,571
Balance at 31 March 2016	**26,166,244**	5,642,975	13,963,971

CONDENSED FINANCIAL STATEMENTS

24. Financial Liabilities

	Note	**31 Mar 2016**	31 Mar 2015	30 Sep 2015	30 Sep 2014
		£m	£m	£m	£m
Current liabilities					
Retail deposits	25	**808.5**	101.1	338.9	53.3
Bank loans and overdrafts		**1.0**	0.2	0.7	1.1
		809.5	101.3	339.6	54.4
Non-current liabilities					
Asset backed loan notes		**8,414.7**	8,461.7	8,274.6	8,115.0
Corporate bond		**110.0**	110.0	110.0	110.0
Retail bonds		**295.0**	183.2	294.9	183.2
Retail deposits	**25**	**617.9**	63.9	369.8	6.8
Bank loans and overdrafts		**1,510.6**	1,237.7	1,425.4	1,397.9
Derivative financial liabilities	**17**	**10.2**	5.0	6.7	1.1
		10,958.4	10,061.5	10,481.4	9,814.0

Details of changes in the Group's borrowings since the year end are given in note 26 below.

25. Retail Deposits

The Group's retail deposits, held by Paragon Bank PLC, were received from customers in the United Kingdom and are denominated in sterling. The deposits comprise principally term deposits and 120 day notice accounts. The method of interest calculation on these deposits is analysed as follows:

	31 Mar 2016	31 Mar 2015	30 Sep 2015	30 Sep 2014
	£m	£m	£m	£m
Fixed rate	**891.3**	116.1	508.3	39.8
Variable rates	**535.1**	48.9	200.4	20.3
	1,426.4	165.0	708.7	60.1

The weighted average interest rate on retail deposits, analysed by charging method, was:

	31 Mar 2016	31 Mar 2015	30 Sep 2015	30 Sep 2014
	%	%	%	%
Fixed rate	**2.31**	2.08	2.33	1.90
Variable rates	**1.67**	1.70	1.62	1.85

The contractual maturity of these deposits is analysed below.

	Note	31 Mar 2016	31 Mar 2015	30 Sep 2015	30 Sep 2014
		£m	£m	£m	£m
Amounts repayable					
In less than three months		**13.4**	1.9	9.1	-
In more than three months but not more than one year		**532.2**	98.4	242.6	52.8
In more than one year, but not more than two years		**381.5**	31.0	181.7	6.8
In more than two years, but not more than five years		**236.4**	32.9	188.1	-
Total term deposits		**1,163.5**	164.2	621.5	59.6
Repayable on demand		**262.9**	0.8	87.2	0.5
		1,426.4	165.0	708.7	60.1
Total falling due in less than one year	*24*	**808.5**	101.1	338.9	53.3
Total falling due in more than one year	*24*	**617.9**	63.9	369.8	6.8
		1,426.4	165.0	708.7	60.1

26. Borrowings

All borrowings described in the Group Accounts for the year ended 30 September 2015 remained in place throughout the period, except as noted below.

On 20 October 2015, a Group company, Idem Luxembourg (No. 8) entered into an agreement under which £117.3m of sterling floating rate notes have been issued to Citibank NA on a limited recourse basis. These notes bear interest at a rate of one month LIBOR plus 3.50%. The Group investment in this company to support these notes was £84.9m. The facility was used to refinance existing Idem Capital borrowings and to refinance further existing Idem Capital unsecured loan assets and is secured on those assets. During the period a further £4.1m of notes were issued and a further £70.8m of notes was issued under the facility after the end of the period. Both of these issues were used to fund the purchase of loan balances from third parties.

On 19 November 2015, a Group company, Paragon Mortgages (No. 24) PLC, issued €125.0m of euro mortgage backed floating rate notes and £253.0m of sterling mortgage backed floating rate notes to external investors at par. The euro notes were class A1 notes, rated AAA by Fitch and Aaa by Moody's and bearing interest at 1.10% above EURIBOR. £208.3m of the sterling notes were class A2 notes, rated AAA by Fitch and Aaa by Moody's, £19.3m were class B notes, rated AA by Fitch and Aa2 by Moody's and £25.4m were class C notes rated A by Fitch and A1 by Moody's. The interest margins above LIBOR on the sterling notes were 1.50% on the A2 notes, 2.45% on the B notes and 3.20% on the C notes. Cross-currency basis swaps were entered into at the time of the transaction, effectively translating the euro notes into a LIBOR linked sterling liability. The average interest margin on the transaction, taking swap costs into account was 1.75% and the proceeds were used to pay down existing warehouse debt. The Group retained £8.8m of class Z notes and also invested £8.7m in the first loss fund, bringing its total investment to £17.5m, or 5.0% of the issued notes.

During the period the £100.0m warehouse facility provided to Paragon Sixth Funding Limited by Natixis was terminated.

Of the Group's borrowings at 30 September 2015, the notes issued by Idem First Finance Limited were repaid in October 2015 while those issued by Idem Capital Securities (No. 1) were repaid in January 2016. The assets financed by these borrowings were refinanced through Idem Luxembourg (No. 8) or through Paragon Bank retail deposits.

The mortgage backed floating rate notes issued by Paragon Mortgages (No. 17) PLC were repaid in January 2016, following the purchase of its mortgage assets by Paragon Bank.

On 11 February 2013 the Company inaugurated a £1,000.0m Euro Medium Term Note Programme under which it may issue retail bonds, or other notes, within a 12 month period. The prospectus was updated, renewing the programme for a further 12 month period on 22 January 2016.

Repayments made in respect of the Group's borrowings are shown in note 30.

27. Retirement Benefit Obligations

The defined benefit obligation at 31 March 2016 has been calculated on a year-to-date basis, using the latest actuarial valuation for IAS 19 purposes at 30 September 2015. There have been movements in financial market conditions since that date, requiring an adjustment to the actuarial assumptions underlying the calculation of the defined benefit obligation a 31 March 2016. In particular, over the period since the 30 September 2015 actuarial valuation, the discount rate has decreased by 0.3% per annum, whereas expectations of long term inflation have decreased by 0.15% per annum. The net effect of these changes has resulted in an increase in the value of the defined benefit obligation at 31 March 2016. The impact of the change in actuarial assumptions has been recognised as an actuarial loss in other comprehensive income.

The defined benefit plan assets have been updated to reflect their market value at 31 March 2016. In particular, over the period since 30 September 2015 the Plan assets have achieved returns in excess of the assumptions made at 30 September 2015. The difference between the expected and actual return on assets has been recognised as an actuarial gain in other comprehensive income.

The movements in the deficit on the defined benefit plan during the six month period ended 31 March 2016 are summarised below.

	Six months to 31 Mar 2016	Six months to 31 Mar 2015	Year to 30 Sep 2015
	£m	£m	£m
Opening pension deficit	**21.5**	17.3	17.3
Service cost	**0.8**	0.8	1.7
Net funding cost	**0.4**	0.4	0.7
Administrative expenses	**0.2**	0.3	0.7
Employer contributions	**(1.6)**	(1.6)	(3.2)
Amounts posted to other comprehensive income			
Return on plan assets not included in interest	**(2.0)**	(5.8)	1.8
Actuarial loss from changes in financial assumptions	**4.7**	14.6	2.5
Closing pension deficit	**24.0**	26.0	21.5

28. Net Cash Flow from Operating Activities

	Six months to 31 Mar 2016 £m	Six months to 31 Mar 2015 £m	Year to 30 Sep 2015 £m
Profit before tax	**69.5**	62.6	134.2
Non-cash items included in profit and other adjustments			
- Depreciation of property, plant and equipment	**2.2**	0.8	1.5
- Profit on disposal of property, plant and equipment	**(0.7)**	-	-
- Amortisation of intangible assets	**0.7**	0.7	1.4
- Foreign exchange movements on borrowings	**277.2**	119.6	(30.8)
- Other non-cash movements on borrowings	**7.3**	2.3	4.8
- Impairment losses on loans to customers	**3.5**	3.5	5.6
- Charge for share based remuneration	**2.1**	2.6	4.5
Net (increase) / decrease in operating assets			
- Loans to customers	**(554.4)**	(214.3)	(810.9)
- Derivative financial instruments	**(279.8)**	(117.0)	33.8
- Fair value of portfolio hedges	**(2.1)**	(2.8)	(4.7)
- Other receivables	**0.9**	0.8	0.4
Net (decrease) / increase in operating liabilities			
- Retail deposits	**717.7**	104.8	648.6
- Derivative financial instruments	**3.5**	3.9	5.6
- Other liabilities	**5.2**	(4.0)	2.7
Cash generated / (utilised) by operations	**252.8**	(36.5)	(3.3)
Income taxes (paid)	**(9.7)**	(11.0)	(22.6)
Net cash flow generated / (utilised) by operating activities	**243.1**	(47.5)	(25.9)

29. Net Cash Flow Used in Investing Activities

	Note	Six months to 31 Mar 2016 £m	Six months to 31 Mar 2015 £m	Year to 30 Sep 2015 £m
Proceeds from sales of property, plant and equipment		**0.9**	-	-
Purchases of property, plant and equipment		**(4.6)**	(0.7)	(0.7)
Purchases of intangible assets		**(0.7)**	(0.4)	(1.2)
Decrease / (increase) in short term investments		**23.8**	(9.1)	(1.7)
Acquisition of subsidiary	*5*	**(305.3)**	-	-
Net cash (utilised) by investing activities		**(285.9)**	(10.2)	(3.6)

CONDENSED FINANCIAL STATEMENTS

30. Net Cash Flow from Financing Activities

	Note	**Six months to 31 Mar 2016**	Six months to 31 Mar 2015	Year to 30 Sep 2015
		£m	£m	£m
Shares issued		**0.1**	1.2	1.5
Dividends paid	*22*	**(21.7)**	(18.3)	(29.1)
Issue of asset backed floating rate notes		**460.3**	533.4	823.8
Repayment of asset backed floating rate notes		**(601.3)**	(308.7)	(638.3)
Issue of retail bonds		**-**	-	111.3
Movement on bank facilities		**84.4**	(162.9)	24.8
Purchase of shares	*23*	**(40.0)**	(22.3)	(56.9)
Net cash (utilised) / generated by financing activities		**(118.2)**	22.4	237.1

31. Related Party Transactions

CONDENSED FINANCIAL STATEMENTS

In the six months ended 31 March 2016, the Group has continued the related party relationships described in note 62 on page 229 of the Annual Report and Accounts of the Group for the financial year ended 30 September 2015. Related party transactions in the period comprise the compensation of the Group's key management personnel, transactions with the Group Pension Plan and fees paid to a non-executive director in respect of his appointment as a director of the Corporate Trustee of the Group Pension Plan. There have been no changes in these relationships which could have a material effect on the financial position or performance of the Group in the period.

Save for the transactions referred to above, there have been no related party transactions in the six months ended 31 March 2016.

32. Income Statement Ratios

The average net interest margin is calculated as follows:

	Note	Six months to 31 Mar 2016 £m	Six months to 31 Mar 2015 £m	Year to 30 Sep 2015 £m
Opening loans to customers	*15*	**10,062.4**	9,255.9	9,255.9
Closing loans to customers	*15*	**10,853.1**	9,468.3	10,062.4
Average loans to customers		**10,457.8**	9,362.1	9,659.2
Net interest		**109.8**	97.2	197.4
Annualised net interest margin		**2.11%**	2.09%	2.04%
Impairment provision		**3.5**	3.5	5.6
Impairment as a percentage of average loan balance (annualised)		**0.07%**	0.07%	0.06%

33. Contingent Liabilities

Over recent years, in common with other financial services firms, the Group has followed guidance issued by the FCA in respect of redress to customers in respect of the misselling of payment protection insurance ('PPI'), though the sums involved have not been material.

In November 2014 the UK Supreme Court handed down its decision in Plevin v Paragon Personal Finance Limited ('Plevin'), which addressed potential liability in respect of PPI claims under section 140 of the Consumer Credit Act 1974, where commission charged to the customer was particularly high. On 2 October 2015 the FCA published a statement outlining proposed rules addressing the handling of PPI cases in the light of the Plevin decision and including a deadline beyond which no further new PPI claims would be required to be considered.

The Group has reviewed its current exposure to PPI and related claims in the light of the Court's judgement in Plevin and the FCA proposals and its current expectation is that it will suffer no material additional costs from such claims. However, this assessment is based on our current interpretation of both the Plevin judgement and the draft rules, which may be revised before finalisation, while interpretations may develop as both the judgement and the rules are implemented. Therefore, it is possible that the maximum liability may be greater, but it is impracticable to evaluate the potential impact at this stage.

INDEPENDENT REVIEW REPORT

to The Paragon Group of Companies PLC

Introduction

We have been engaged by the Company to review the condensed set of financial statements in the half-yearly financial report for the six months ended 31 March 2016 which comprises the income statement, the statement of comprehensive income, the balance sheet, the cash flow statement, the statement of movements in equity and related notes 1 to 33. We have read the other information contained in the half-yearly financial report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

This report is made solely to the Company in accordance with the terms of our engagement to assist the company in meeting the requirements of the Disclosure and Transparency Rules ('the DTR') of the UK's Financial Conduct Authority ('the UK FCA'). Our review has been undertaken so that we might state to the company those matters we are required to state to it in this report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company for our review work, for this report, or for the conclusions we have reached.

Directors' Responsibilities

The half-yearly financial report is the responsibility of, and has been approved by, the directors. The directors are responsible for preparing the half-yearly financial report in accordance with the DTR of the UK FCA.

As disclosed in note 2, the annual financial statements of the group are prepared in accordance with IFRSs as adopted by the EU. The condensed set of financial statements included in this half-yearly financial report has been prepared in accordance with IAS 34 Interim Financial Reporting as adopted by the EU.

Our Responsibility

Our responsibility is to express to the Company a conclusion on the condensed set of financial statements in the half-yearly financial report based on our review.

Scope of Review

We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410 'Review of Interim Financial Information Performed by the Independent Auditor of the Entity' issued by the Auditing Practices Board for use in the UK. A review of interim financial information consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK and Ireland) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements in the half-yearly financial report for the six months ended 31 March 2016 is not prepared, in all material respects, in accordance with IAS 34 as adopted by the EU and the DTR of the UK FCA.

Andrew Walker
for and on behalf of KPMG LLP

Chartered Accountants
One Snowhill
Snow Hill Queensway
Birmingham
B4 6GH

24 May 2016

PRINCIPAL RISKS AND UNCERTAINTIES

There are a number of potential risks and uncertainties which could have a material impact on the Group's performance over the remaining six months of the financial year and could cause actual results to differ materially from expected and historical results. In the opinion of the directors these have not changed materially from those described in section A2.2 of the last annual report and accounts of the Company for the year ended 30 September 2015. These are summarised below.

Category	Risk	Description
Business	Economic	A severe downturn in the UK would impact on demand for loans, customer ability to pay and security values
	Concentration	The Group is particularly exposed to the performance of the UK private rented sector, through its buy-to-let activities
	Competition	Operating in actively competitive markets, profitability or market share could be eroded by competitor activity
Credit	Customer	Lending may be incorrectly targeted or customers may become less able to service debt, exposing the Group to loss
	Counterparty	Failure of an institution holding the Group's cash deposits or providing hedging facilities for risk mitigation could expose the Group to loss or liquidity issues
Conduct	Fair outcomes	Failure to deliver appropriate customer outcomes would impact on the Group's reputation and its financial performance
Operational	People	Failure to retain appropriately skilled employees would impact upon the Group's ability to deliver its business plans
	Systems	Substantial IT systems are required to support the operations of the Group and guard against cyber risks. Failure in these systems might result in loss
	Regulation	The Group operates in sectors which are highly regulated and are becoming more so. Compliance failures would risk financial and reputational damage
Liquidity and Capital	Funding	Inability to raise new funds could restrict lending, while changes in the retail savings market could impact the liquidity of Paragon Bank
Market	Interest rates	Reduction in margins between market lending and borrowing rates or mismatches in the Group balance sheet would impact profit
Pension Obligation	Pensions	The obligation to support the Group's defined benefit pension plan might deplete resources

The Group has considered and responded to all of these risks, mitigating the exposure as far as practicable.

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