Paragon Banking Group PLC

Financial Results for twelve months ended 30 September 2018

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2018 results highlights

Strong financial performance and further strategic progress

Strong operational performance	Enhancing returns with strong capital base	Strategy
• New lending £2.3 billion (+25.9%) • Mortgages £1.6 billion (+10.8%) • Buy-to-let pipeline of £779 billion providing strong momentum into H1 2019 • Commercial Lending £710 million (+82.6%) with further products added • Retail deposit funding £5.3 billion (+46.5%) • NIM +8bp to 221bp • Continued exemplary credit record	• Underlying operating profits up 7.8% • Underlying EPS +11.3% and RoTE at 14.0% • Increase in DPS +23.6%, 2.5x cover target achieved • £28.0 million exceptional gain on Idem portfolio sale • CET1 strong at 13.8% • Total capital at 16.2%	• Diversified model and product range • Increasingly specialist • M&A • December 2017 – acquisition of Iceberg • July 2018 – acquisition of Titlestone • September 2018 – disposal of Idem Capital portfolio • Focus on building future shareholder returns through: • Strong organic growth • Potential to augment proposition if attractive • Disciplined capital allocation

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Section 1

Financial Results

For twelve months ended 30 September 2018

Richard Woodman
Chief Financial Officer

Profit performance

Underlying profits up 7.8% at £156.5 million

- Statutory profits of £181.5 million include fair value movements and one-off items relating to acquisitions and portfolio disposals
- Exceptional items summarised as:
  - Gross gain on Idem Capital portfolio disposal £28.0 million
  - Net liquidity costs from acquisition funding and costs associated with Idem Capital disposal (funding and accelerated fee amortisation) £1.9 million
  - Deal related costs and restructuring related overhead £2.3 million

£'m	Statutory	Adjustments	Underlying
Interest Receivable	**451.8**	**0.3**	**451.5**
Interest Payable	(197.2)	(2.2)	(195.0)
Net Interest Income	**254.6**	**(1.9)**	**256.5**
Gain on Disposal of Financial Assets	28.0	28.0	0.0
Other Income	19.3	0.0	19.3
Total Income	**301.9**	**26.1**	**275.8**
Operating Expenses	(114.2)	(2.3)	(111.9)
Bad debt provisions	(7.4)	0.0	(7.4)
Operating Profit	**180.3**	**23.8**	**156.5**
Fair value net gains / (losses)	1.2	0.0	1.2
Exceptional Items	0.0	(23.8)	23.8
Profit Before Tax	**181.5**	**0.0**	**181.5**

Remaining presentation focused on underlying results

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Income statement

Income growth underpinning stronger profits

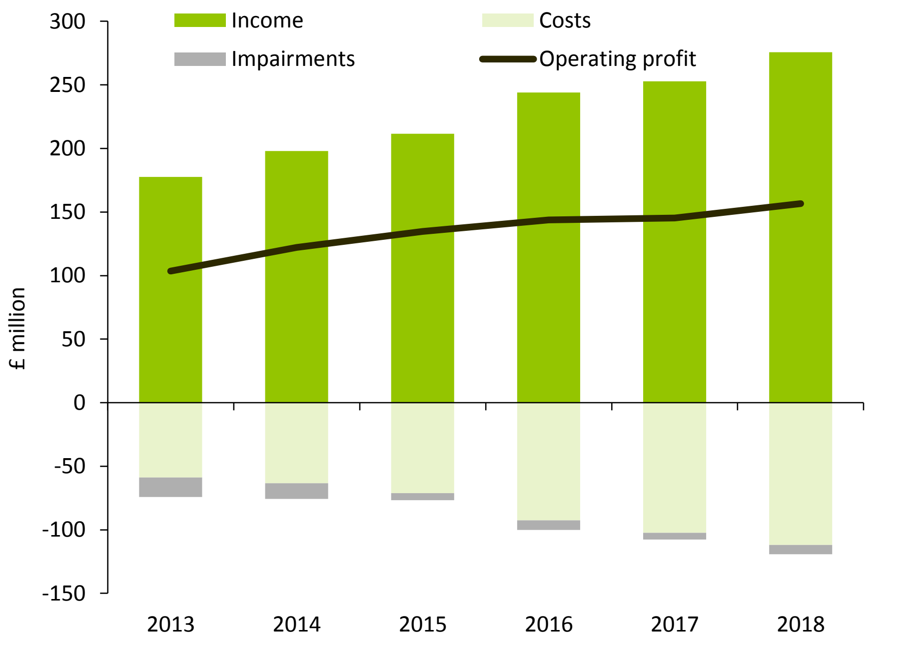
- Total income increased by 9.1% year-on-year to £275.8 million
- Net interest margin +8bp to 2.21%
- Average loan book up 6.4% to £11.6 billion

- Operating costs increased by 9.4% to £111.9 million
- Cost:income ratio stable at 40.6%

- Operating profit CAGR of 8.6% per annum since 2013

- Cost of risk remains low at 6bp – reflecting conservative risk appetite

Underlying operating profits



Underlying operating profits					
2013	**2014**	**2015**	**2016**	**2017**	**2018**
£103.5m	£122.2m	£134.7m	£143.8m	£145.2m	£156.5m

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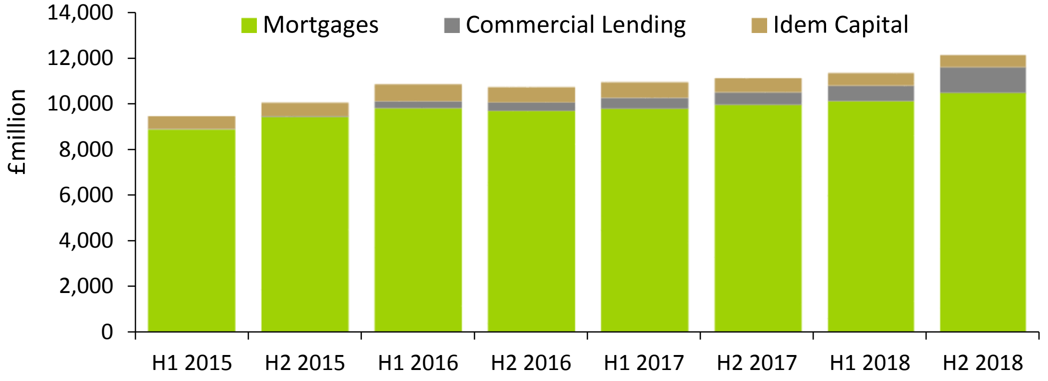
Loan book

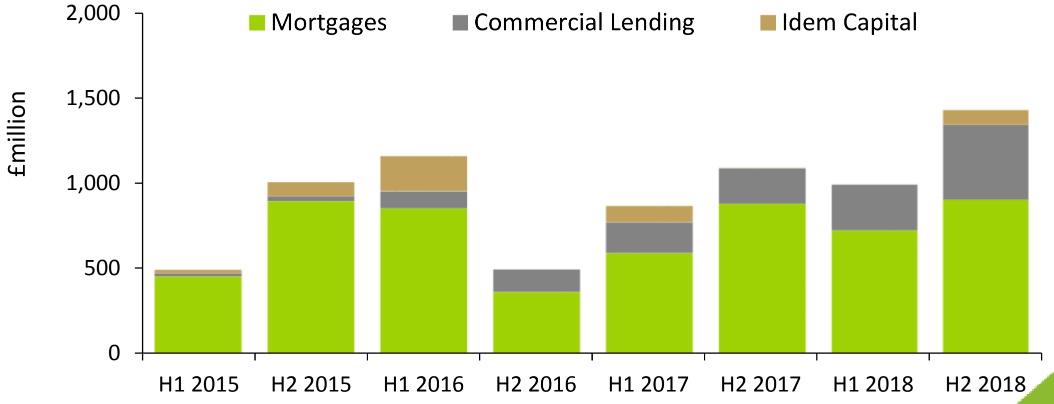
Organic advances and acquisitions accelerate loan book growth

- Like-for-like lending up 18.1% at £2.19 billion
- All lending up 25.9% to £2.33 billion
- Fastest growth achieved in Commercial Lending advances
- Balance sheet to remain dominated by buy-to-let portfolio
- Change in business mix supporting margin growth

Loans and advances to customers



Originations and investments



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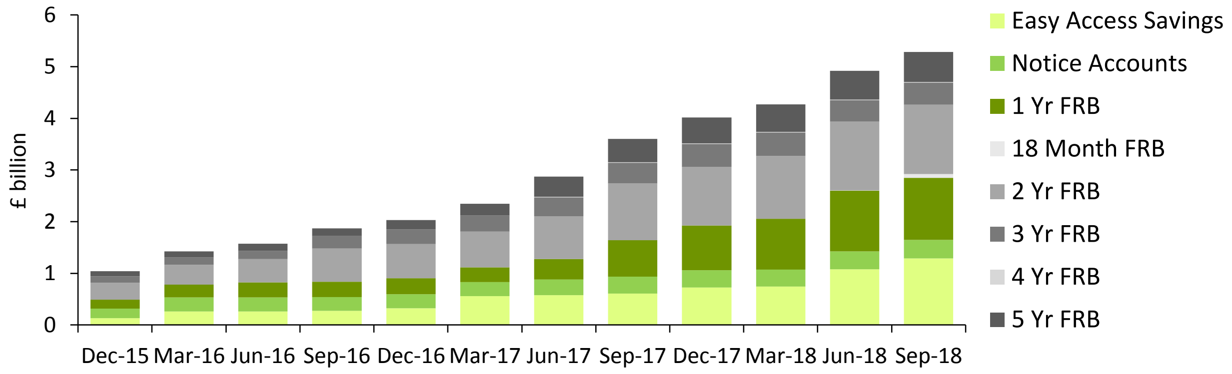
Deposit funding

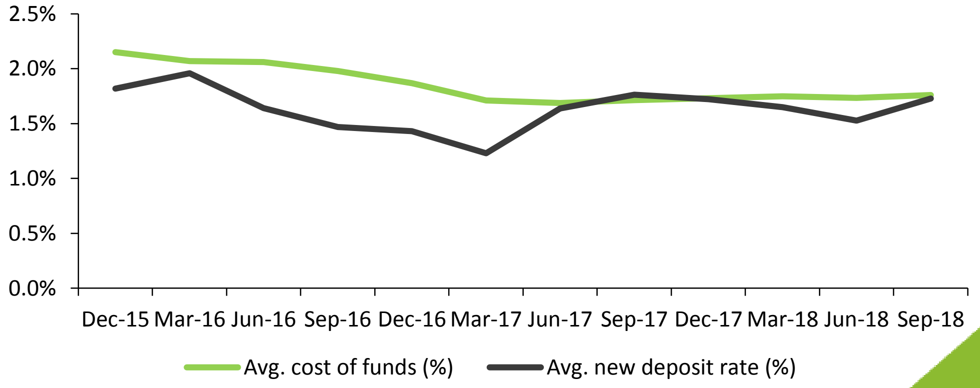
Continued strong growth in retail savings deposits

- Total deposit balances increased by £1.7 billion during 2018 to £5.3 billion
- Monthly average new deposit costs depend on mix of tenors
- Overall deposit book cost stable year-on-year (1.76% in September 2018 compared to 1.71% in September 2017)

Deposit balances



Cost of funds



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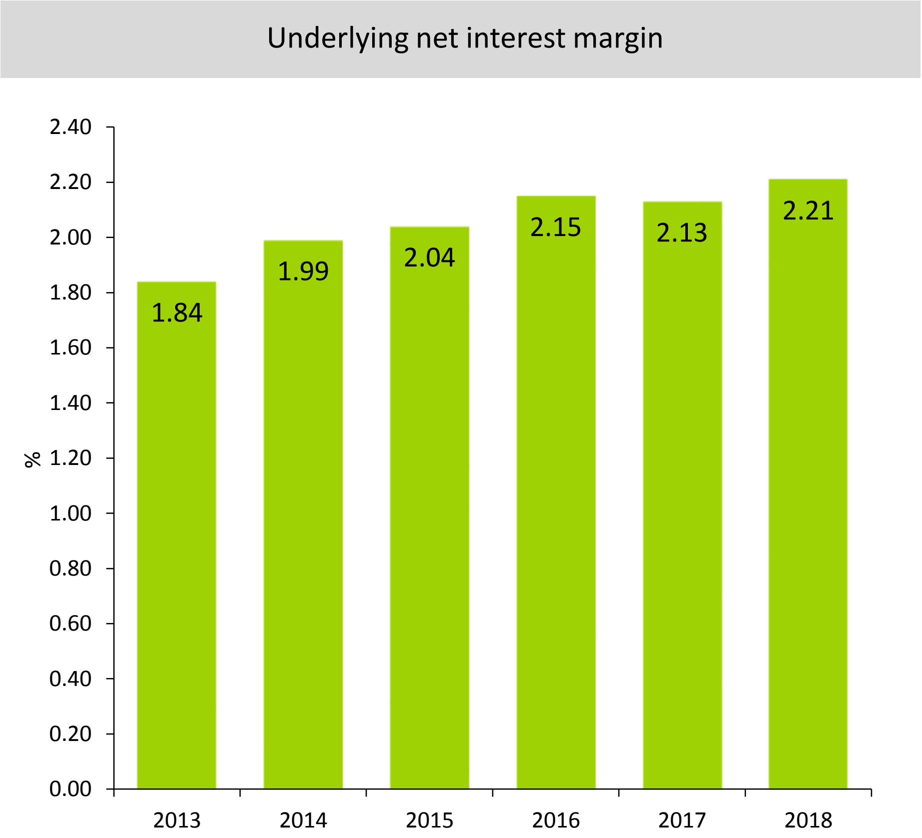
Net interest margin

NIM progress reflects diversification benefits

- NIM increased by 8bp year-on-year
- Mortgages NIM stable with a steadily growing portfolio
- Commercial Lending NIM lower as expected but faster volume growth
- Idem Capital NIM strong, reflecting portfolio cash flows
  - Figures exclude the gain on disposal
  - Disposal accelerated income levels
- Mix led improvement, further widening expected

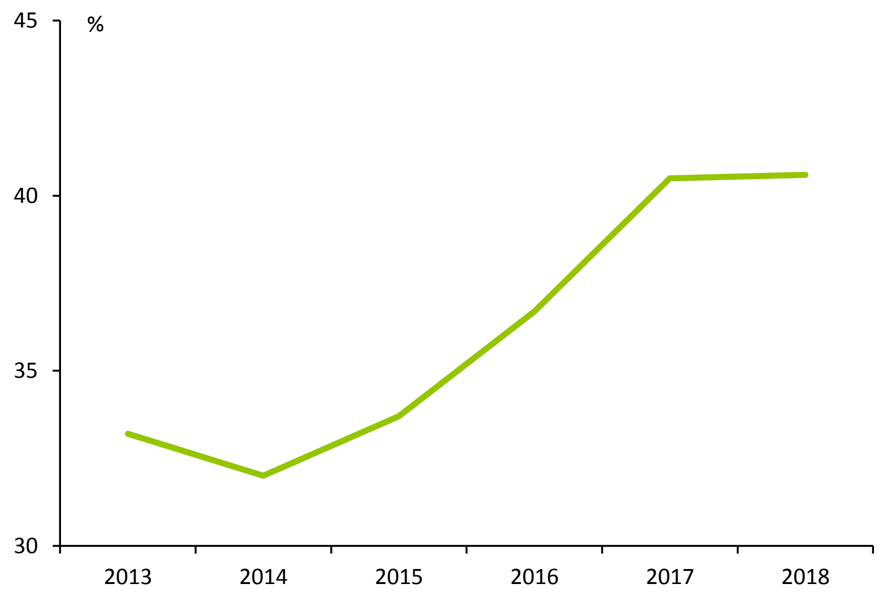


Operating expenses

Further investment in growth platform

- Operating expenses increased £9.6 million to £111.9 million reflecting:
  - New acquisitions
  - GDPR / IFRS9 / IRB and other IT investment
- Further investment planned in 2019 but low 30s% cost:income ratio still targeted in medium term

Cost:income ratio progress



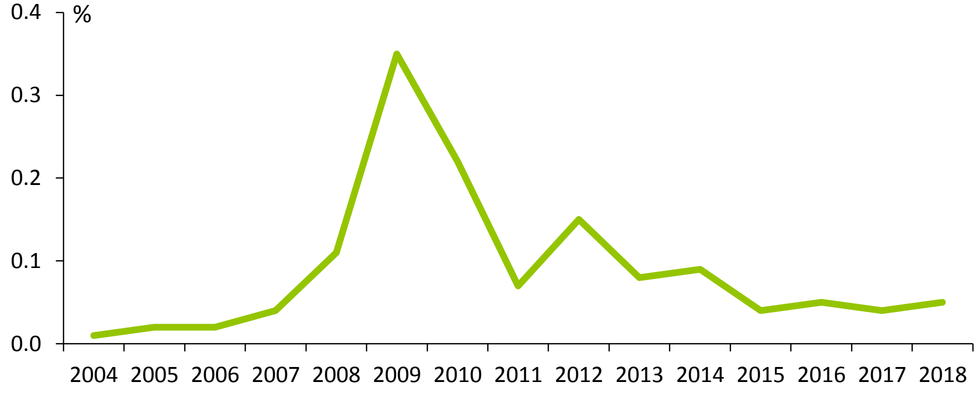
Credit performance

Bad debt levels reflect conservative risk appetite

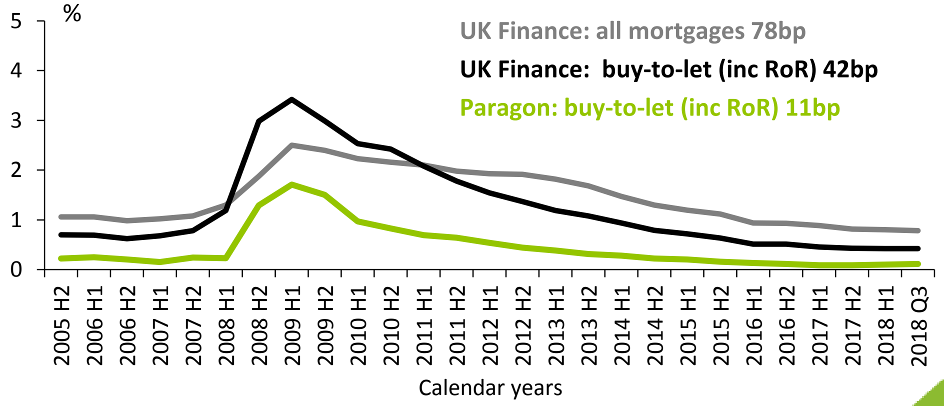
- Cost of credit remains low at 6bp
- 15 year BTL average cost of credit 9bp
- No emerging stress evident in behavioural scores
- Average first mortgage LTV 66.0% – compares favourably to 80.8% in September 2008

Indexed credit behavioural scores by portfolio		
	Sep-17	**Sep-18**
Buy-to-let: New	100.0	101.0
Legacy	100.0	100.4
New second charge mortgages	100.0	99.0
Legacy second charge and Idem Capital assets	100.0	103.0
Motor finance	100.0	100.2

BTL long-term cost of risk



BTL 3 months+ arrears



Source: UK Finance / Paragon

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Group capital

Capital levels remain strong

Group consolidated capital	
Core Equity Tier-1 capital *	£890.8m
Tier-2 capital	£154.9m
Total capital resources	**£1,045.7m**
Credit risk	£5,855.1m
Operational risk	£485.1m
Market risk	-
Other	£105.1m
Total risk exposure	**£6,445.3m**
CET1 ratio *	13.8%
Total capital ratio	16.2%

Group consolidated leverage ratio	
Tier-1 equity *	£890.8m
Leverage exposure **	£13,892.2m
UK leverage ratio *	6.4%

* Adjusted for proposed dividend and subject to verification

** Excludes qualifying central bank claims in accordance with the rule modification applied to the UK Leverage Ratio Framework

Capital ratios

- Growth, M&A and distributions have brought CET1 to more “on-target” level

Risk weightings

- Risk weights still calculated on a standardised basis. IRB application on track for early 2019
- Risk weight density increased following acquisitions in Commercial Lending division, trend to continue

IFRS 9

- Initial estimate of £27 million adjustment on transition
- Transitionary approach being taken for regulatory reporting purposes. IFRS9 impact on CET1 has expected to have immaterial impact on a transitionary basis and 0.3% on a fully loaded basis
- Full disclosure to follow in 2019

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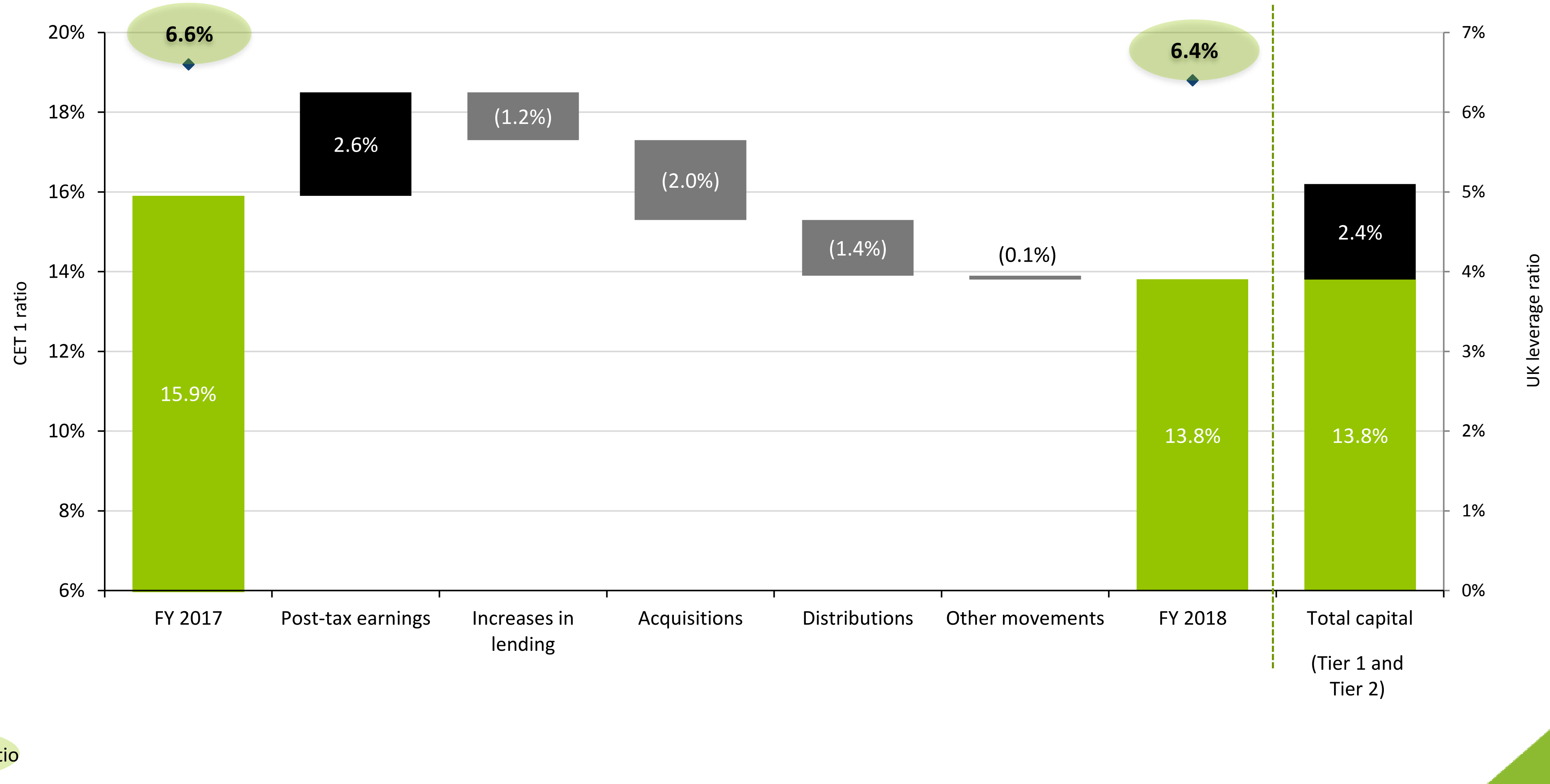
Capital bridge – 2017/2018

Continued strong capital generation employed in growth areas and distributions



Dividends 0.9% and buy-backs 0.5%

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Section 2

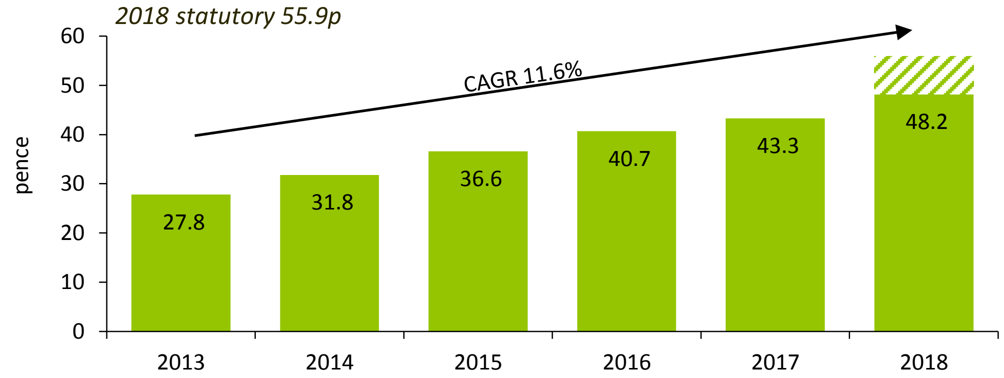
Business Development

Nigel Terrington
Chief Executive

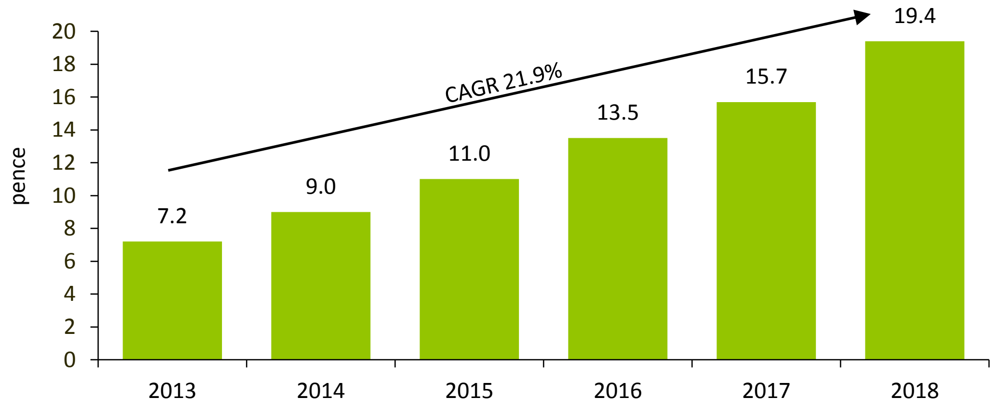
Strong performance alongside strategic transformation

- Total lending over last 5 years £7.7 billion
- Significant start-ups / acquisitions to deliver income diversification
- Bank formed in 2014 – restructured in 2017 to subsume Group
- Majority of growth now retail funded
- All achieved whilst delivering …
  - Strong earnings momentum
  - Cumulative buy-back of £190 million since 2015
  - Improved dividend cover ratio to 2.5 times

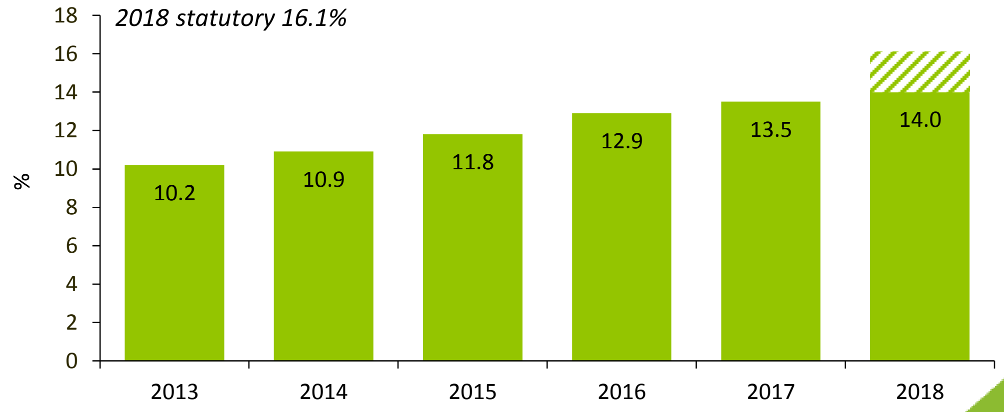
Underlying earnings per share



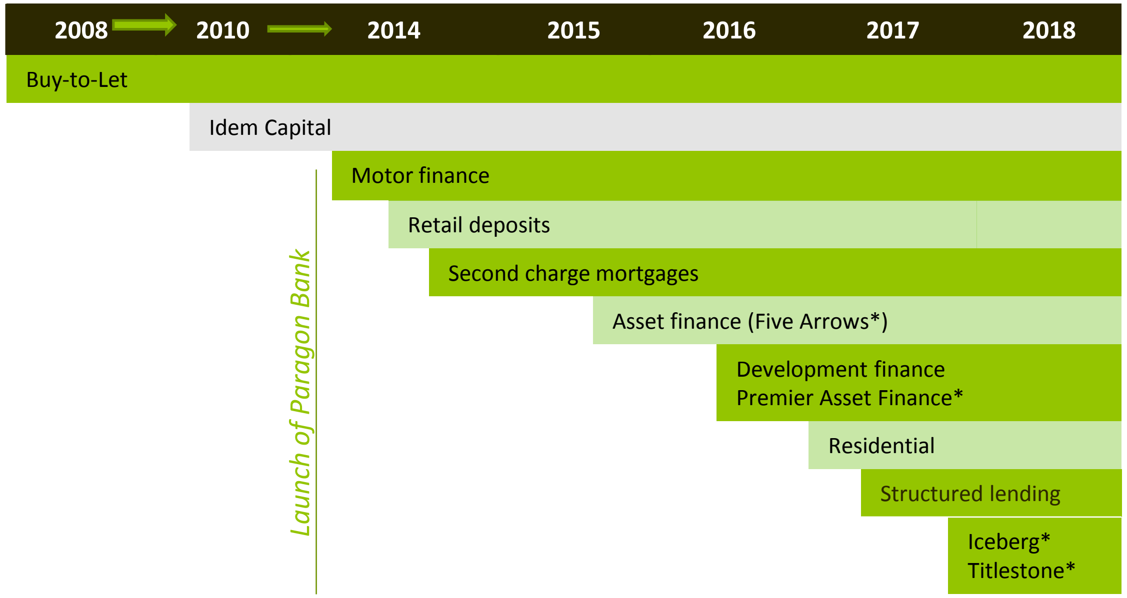
Dividend per share

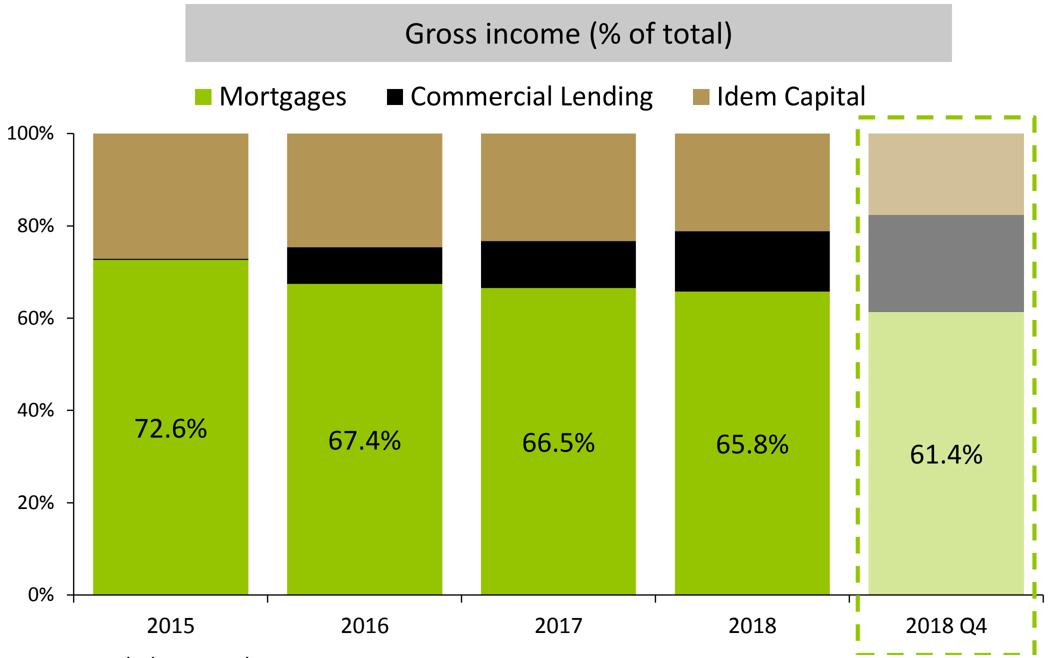


Underlying return on Tangible Equity (%)



Greater optionality around capital deployment





Excludes central segment

- Operating model supports optionality
  - Diversification added portfolio of investment opportunities
  - Centralised operating model supports resources allocation
  - Bank restructuring enhances capital mobility and funding
- Capital allocated and recycled to optimise growth / risk / return
  - Disciplined organic focus adding loan growth at better margins
  - Iceberg acquisition
  - Titlestone acquisition
  - Idem Capital portfolio disposal
  - Share buy-backs

** Acquisitions*

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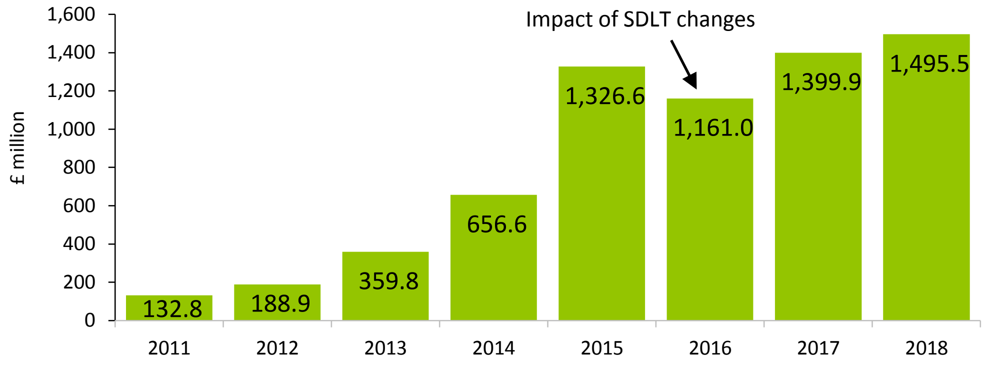
Buy-to-let new lending

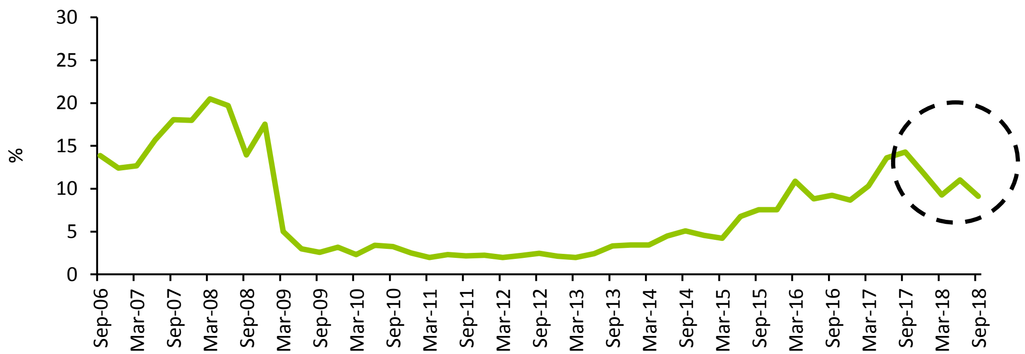
Strong new lending and reducing redemptions driving loan book growth

- BTL new lending up 6.8% to £1,495.5 million
- Growth in complex / professional benefitting from fiscal and regulatory changes
- Lower redemption levels enhance
  - Improved retention strategies
  - Reducing amateur / simple share of total
  - 5 year products extending redemption profile
- Net loan growth +4.3%

Buy-to-let completions



Buy-to-let redemptions (%)



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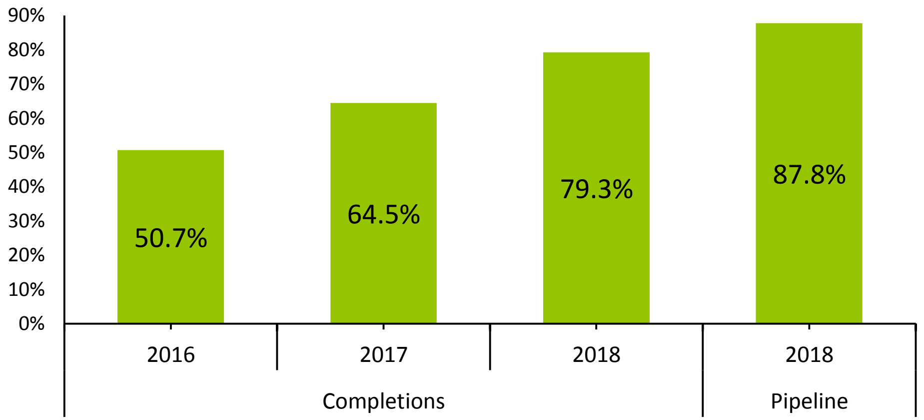
Buy-to-let outlook

Focus on complex / professional

- Continued focus on complex / professional landlords
- Competitive environment
  - Simple / amateur pricing competitive reflecting wider mortgage market
  - Complex / professional pricing more robust
- Pipeline increased to £778.9 million, 28.9% higher than 2017 year end

% of specialist buy-to-let lending



Total specialist buy-to-let lending

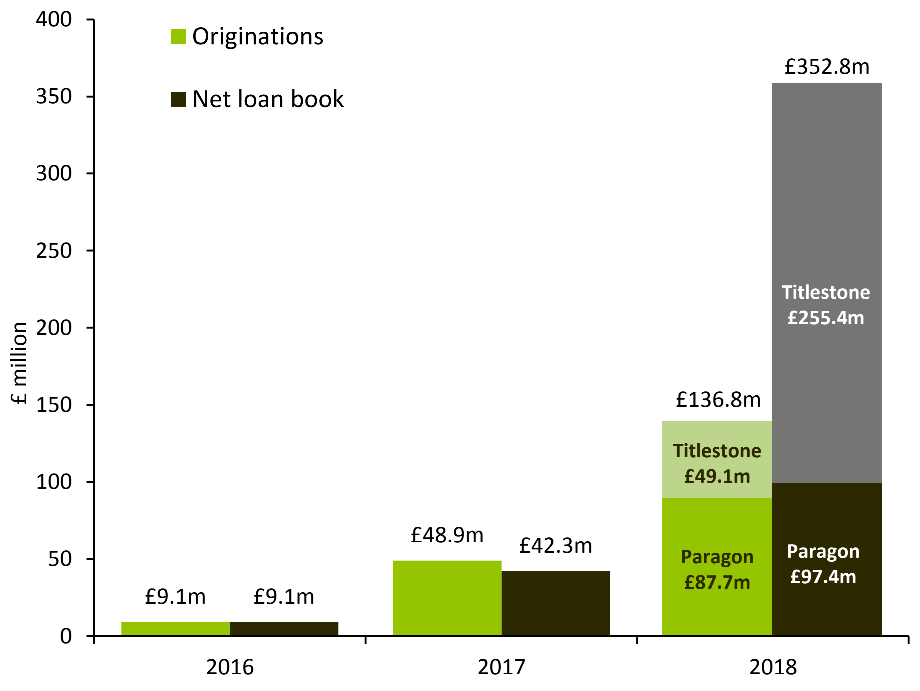
	Completions			Pipeline
	2016 FY	**2017 FY**	**2018 FY**	**2018 FY**
Corporate	£103.4m	£293.5m	£656.7m	£410.7m
Complex	£485.2m	£609.4m	£528.8m	£272.9m
Total	£588.6m	£902.9m	£1,185.5m	£683.6m
% of total	50.7%	64.5%	79.3%	87.8%

Development finance

Significantly enhanced by Titlestone acquisition

- July 2018 – Titlestone acquisition
  - £227.4 million book acquired
  - Significantly strengthens and expands organic business
- Total book size £352.8 million at 30 September 2018
- Service-led proposition
  - Experienced team with 30+ years' market experience
  - Direct, relationship-driven origination
  - c70% of new business sourced through direct channels
- Strong risk discipline
- Average LTGDV across organic and purchased book of 63.2% (2017: 60.6%)
- Integration largely complete
- Combined 2017/18 annualised pre-acquisition originations plus existing flows total £320.8 million
- Highly scalable platform and team with demonstrable track record

Development finance originations and loan book growth

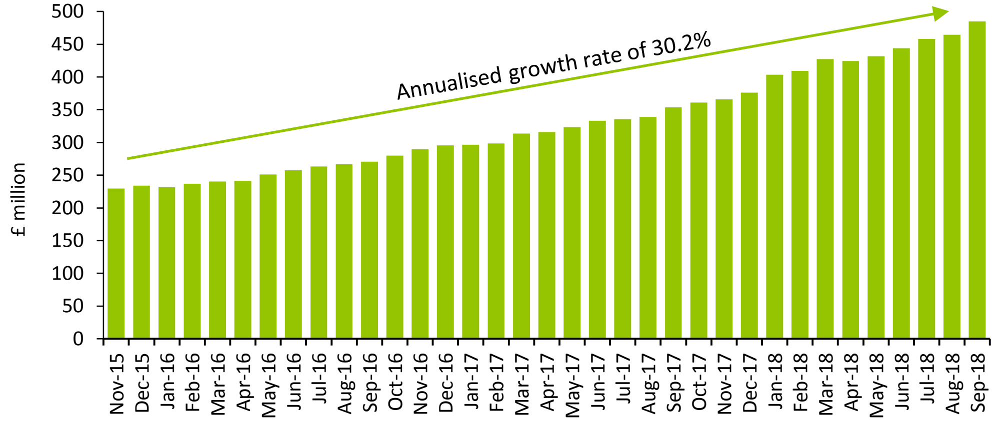


Asset finance

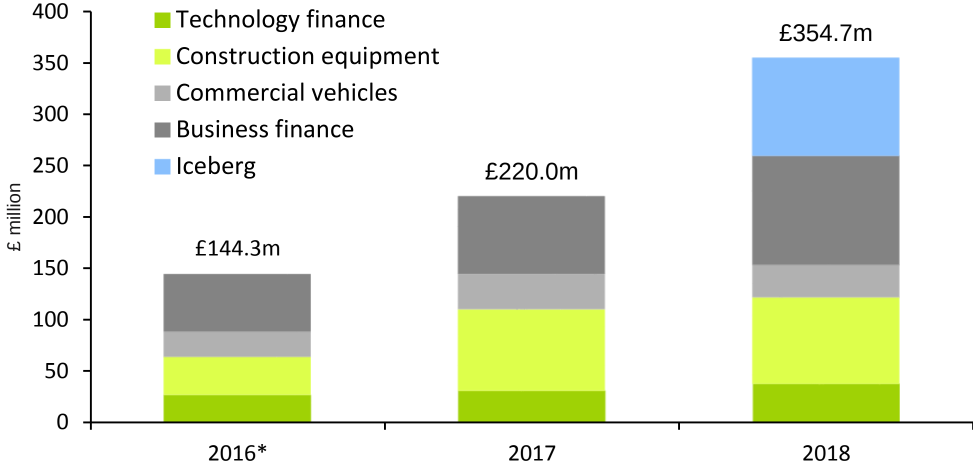
Further distribution and product development delivered

- New business volumes £354.7 million, up 61.2% year-on-year
- Lower margins associated with strategic move towards higher volume, better credit mix
  - Competitive environment, but disciplined stance maintained
  - Additional product range at enhanced margins
- Strong credit standards

Asset finance – portfolio growth



Asset finance – new originations



* 11 months post acquisition

Iceberg acquisition

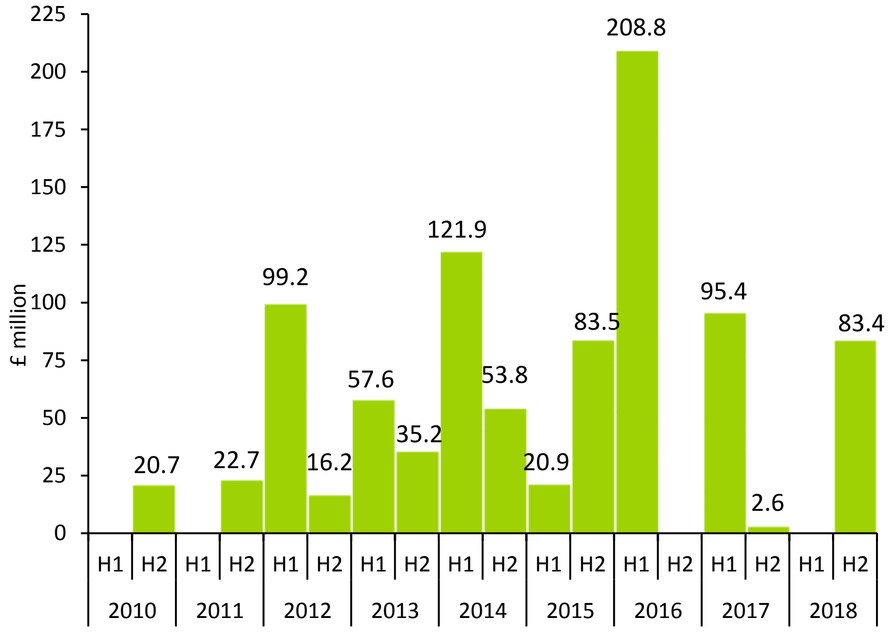
- Specialist lender focused on professions financing
- Fast working capital cycle assets
- 2017/18 new business flow of £95.5 million

Idem Capital

Optimising returns through disciplined capital allocation

- Excellent financial performance
  - Cumulative cash flow now 109.6% of underwriting estimate
- Market remains highly competitive
  - Disciplined risk and pricing stance maintained
- Purchase transaction - £83.4 million
  - Motor and asset finance assets
  - Attractive price in competitive market
- Disposal transaction - £54.7 million
  - Realised profit of £28.0 million against book value
  - Recycled capital to support further growth in Commercial Lending
- £144.5 million sold from Idem Capital to Bank to improve funding costs

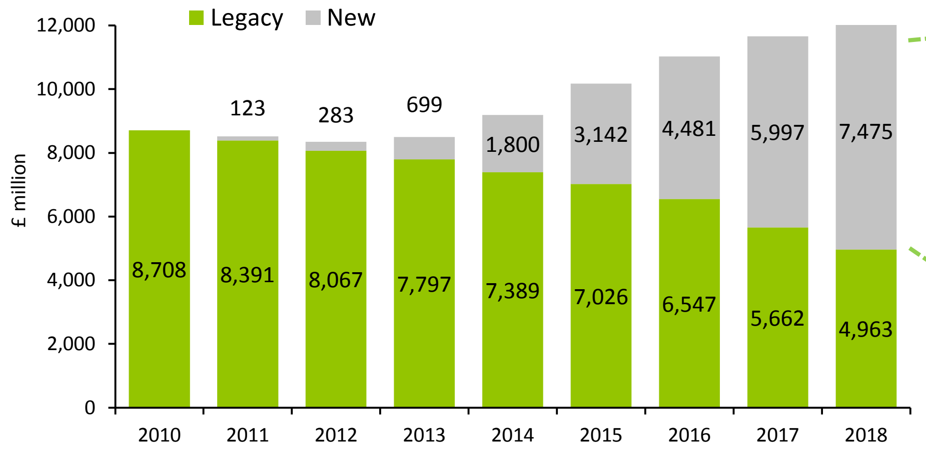
Portfolio purchase investment and disposals



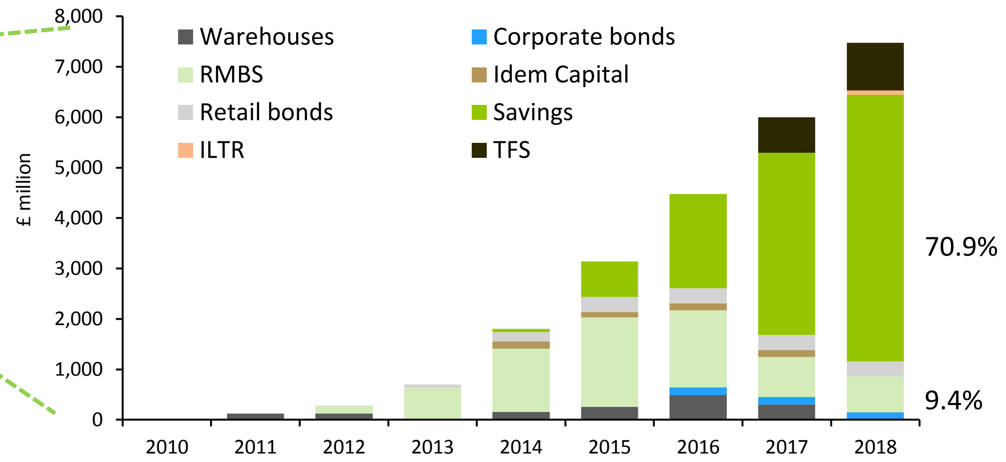
Increasingly diversified funding strategy

Capacity and breadth of funding increasing

Funding mix



Diversification of new funding mix



- Improving deposit franchise – now covers 70.9% post-2010 funding
  - £5,297 million retail deposits outstanding
  - 79.4% retention rate
  - Net Promoter Score +61 (2017 FY: +59)

- Long-term senior debt upgraded to BBB; subordinated debt BBB-
- PM25 April – Paragon's first securitisation as a banking group and a return to market following 2 year absence
  - £725 million securitisation (£289 million retained) – largest since 2008 and at lowest pricing
- TFS drawings increased to £944 million prior to scheme close (2017: £700 million) – only 7.6% of total funding
- New £200 million warehouse facility from BAML will provide cost-effective standby funding

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Brexit risks

A strong starting point

- UK domestic lending only, no notable direct exposures to trade and or currency risks
- Prudent risk appetite
  - Exemplary credit record
  - Operate well inside risk-appetite
  - Risk appetite kept tight at this stage of the cycle and Brexit uncertainty
- Highly experienced with track record of managing through a down-turn
- Operational and liquidity requirements re-reviewed as part of contingency planning and stress testing framework

A resilient balance sheet

- 98.2% of loan book secured
- 91.6% of loan book secured on property
- Average BTL LTV of 66.1%
- 97.9% of deposits covered by FSCS
- 74.5% of deposits are term or notice accounts
- £1.0 billion of HQLA
- 144.0% LCR ratio
- No wholesale funding maturities until 2021
- CET1 of 13.8%

Conclusion

Strong financial and operational progress

- Good financial performance
- Strong loan book growth in specialist segments
- Diversification-led earnings enhancement
- Robust credit record continues
- RoTE now 14%

Strategic delivery supports positive medium term outlook

- Significant strategic change in recent years
- Further growth with continued focus on specialist areas
- Positive structural growth drivers of NIM
- Continued low credit risk appetite
- Increasing capital and funding efficiency
- Disciplined capital allocation
- RoTE target of >15%

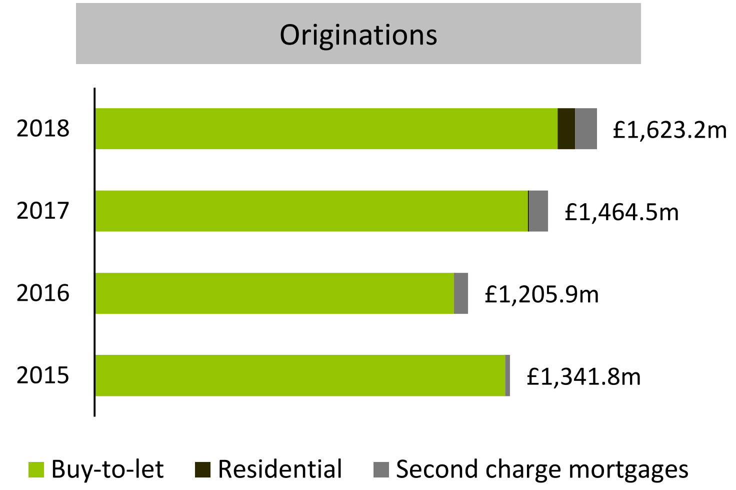
Section 3

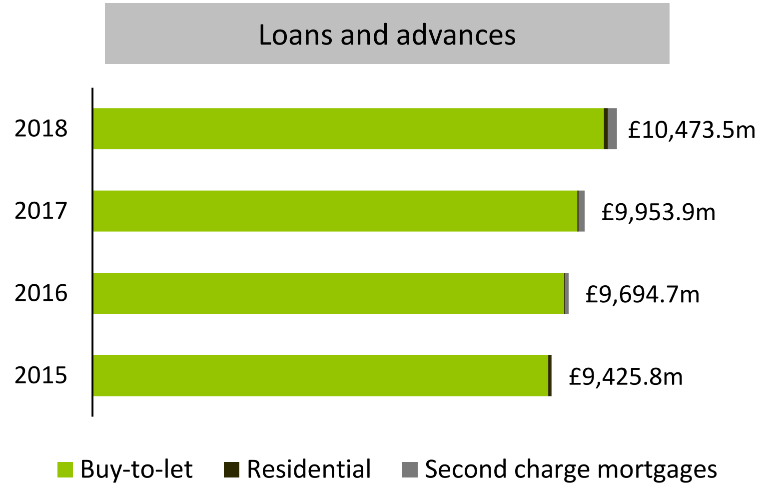
Appendix

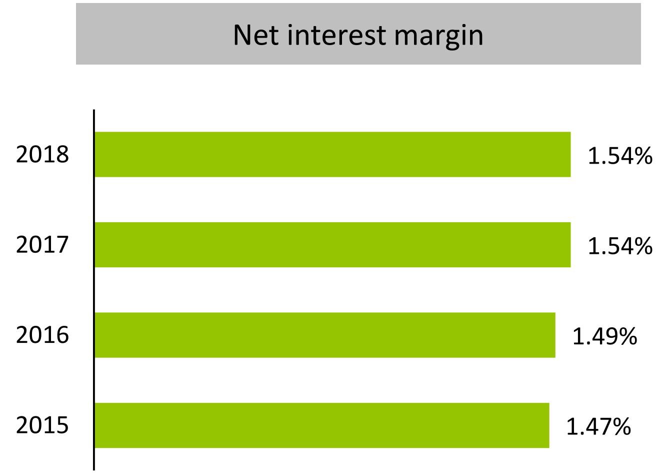
Mortgages

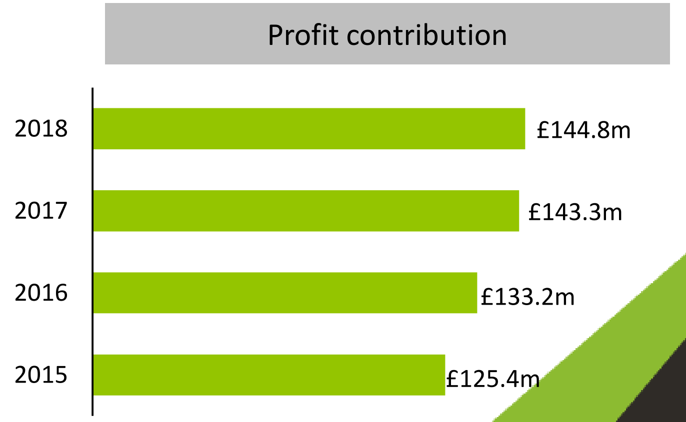
Portfolio growth with stable margins

- Loan book now approaching £10.5 billion
- Originations in line with £1.6 billion guidance
- Segmental profit increased from £143.3 million in 2017 to £144.8 million in 2018
- £6.5 million increase in net interest offset in part by:
  - Greater take-up of fee-free products lowers other income
  - Operating costs higher as volumes increase
  - Modest increase in bad debt back to 2016 levels









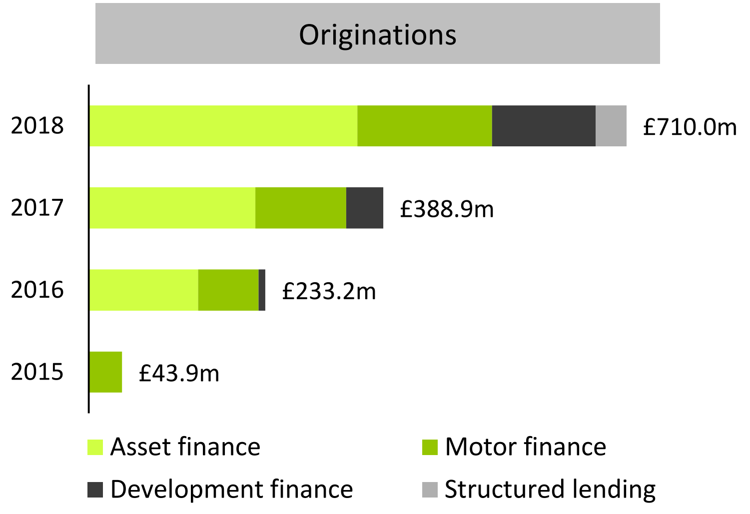
Commercial Lending

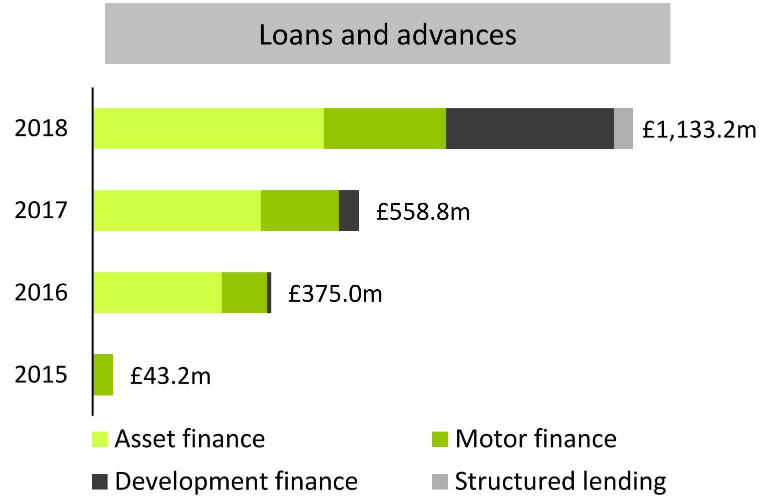
Strong organic and acquisitive growth

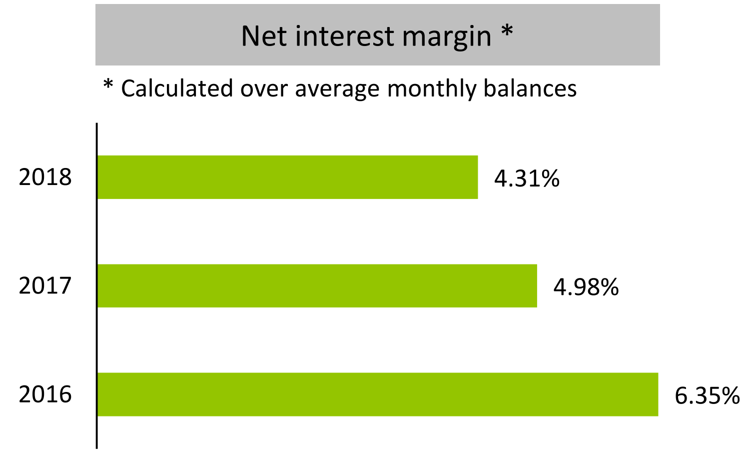
- Total originations increased by 82.6% to £710.0 million. Excluding acquisitions made in the year the increase was 45.4% to £565.4 million

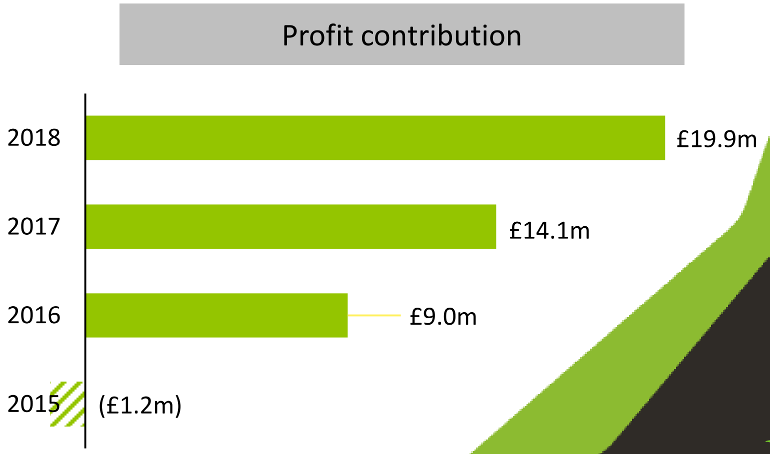
- Segmental profit increased from £14.1 million in 2017 to £19.9 million in 2018

- NIM reduction for the year reflects strategic repositioning of asset finance business, segmental NIM expected to expand in 2019









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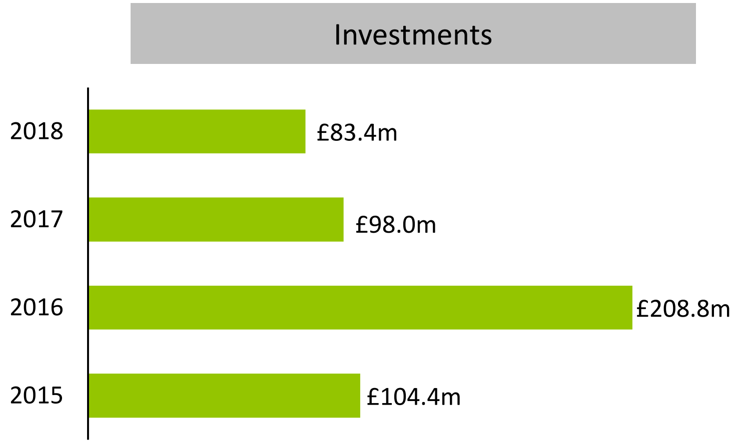
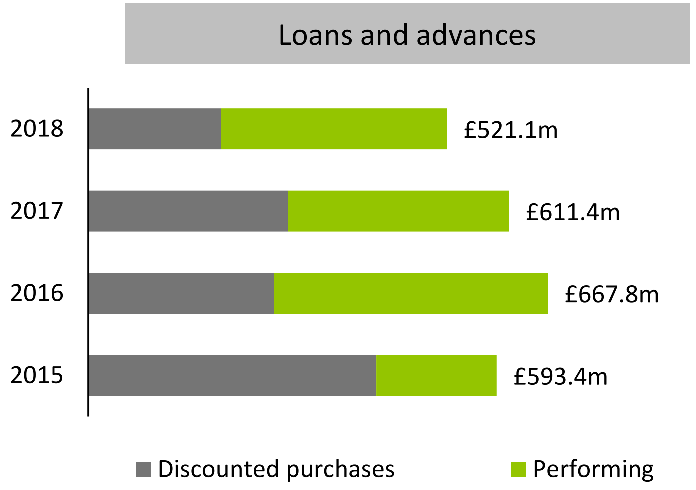
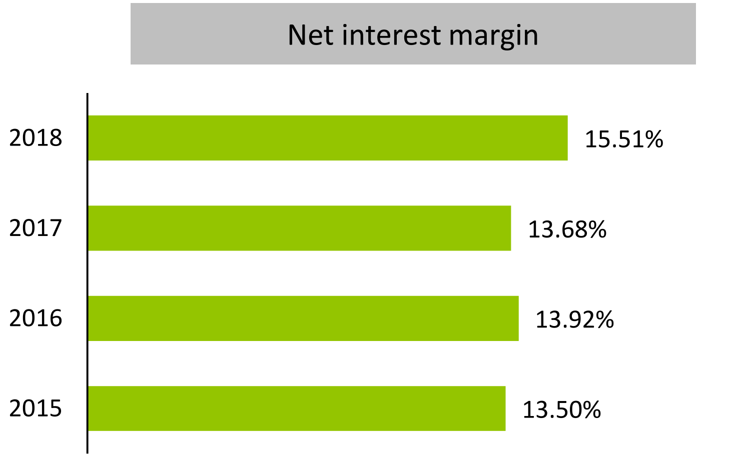
Idem Capital

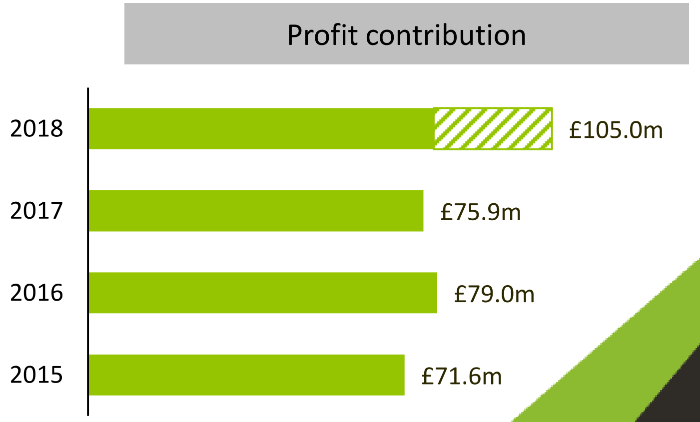
Strong cash flow and partial portfolio disposal

- Idem Capital investments remain lumpy in nature
- New investments augment new product origination rather than purchase of discounted receivables
- Continued strong cash flow underpins earnings growth
  - Underlying profits increased from £75.9 million to £78.2 million
  - Exceptional gain of £26.8 million (net of associated funding costs) on sale of secured portfolio









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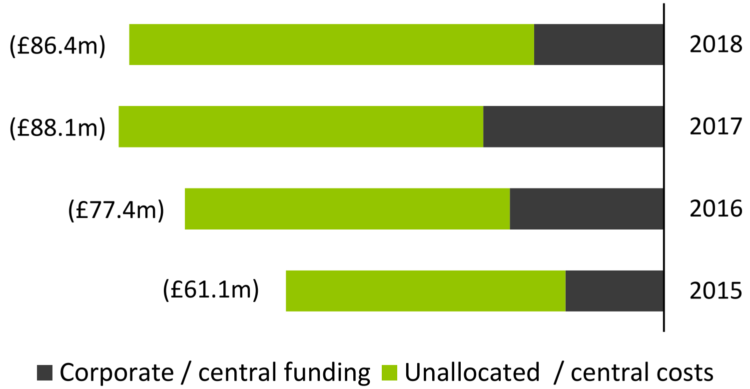
Central

Unallocated costs stable

- Central funding costs reduced year-on-year
- Overheads increased, particularly around technology spend given resilience-based investment and new business system enhancements

Profit / (loss) contribution



Operating leverage *

* Central operating costs as a proportion of total operating costs

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