paragon

The Paragon Group of Companies PLC

Interim Report

Six months ended 31 March 2006

Contents

Financial highlights

16.4%

Increase in profit before tax
on a statutory basis to £39.0 million
(2005 H1: £33.5 million)
and by 13.0% on a proforma basis
(2005 H1 proforma*: £34.5 million)

26.9%

Growth in earnings per share
on a statutory basis to 28.8p
(2005 H1: 22.7p)
and by 23.6% on a proforma basis
(2005 H1 proforma*: 23.3p)

Record mortgage pipeline gives **strong start** to second half year

32.7%

Increase in interim dividend
to 6.9p per share
(2005 H1 : 5.2p)

86.5%

Increase in loan advances to
£1,525.0 million
(2005 H1: £817.9 million)

Pension scheme **deficit** at 30 September 2005 **eliminated** by special contribution

111.4%

Increase in buy-to-let loan
advances to £1,334.5 million
(2005 H1: £631.4 million)

18.8%

Increase in loan assets to
£7,232.9 million on a statutory basis
(2005 H1: £6,087.0 million)
and by 20.7% on a proforma basis
(2005 H1 proforma*: £5,990.5 million)

Share repurchase programme **increased** to **£30 million**

* For all references to proforma numbers see note 10

Chairman's statement

The six months ended 31 March 2006 has been a period of further strong growth in profits, business volumes and loan assets, with buy-to-let mortgages being the principal engine for this growth.

During the period, profit on ordinary activities before taxation increased by 16.4% on a statutory basis to £39.0 million from £33.5 million for the first half of 2005, and by 13.0% from £34.5 million on a proforma basis (see below). Earnings per share increased by 26.9% on a statutory basis to 28.8p (2005 H1: 22.7p) and by 23.6% on a proforma basis (2005 proforma 23.3p).

Total loan advances during the six months to 31 March 2006 were 86.5% higher at £1,525.0 million compared with £817.9 million for the first half of 2005, with most of this growth coming from the buy-to-let business. At 31 March 2006, loan assets were £7,232.9 million (note 6), compared with £6,087.0 million on a statutory basis (£5,990.5 million on a proforma basis) at 31 March 2005, an increase of 20.7% on a proforma basis.

The Board has declared an interim dividend of 6.9p per share, payable on 31 July 2006 to shareholders on the register at 30 June 2006, an increase of 32.7% from last year's interim dividend of 5.2p per share, as we progress towards a market level of dividend cover.

In adopting International Financial Reporting Standards ("IFRS") for the first time, the Group has not applied IAS 32 and IAS 39 in compiling the statutory comparative figures for the six months ended 31 March 2005 shown in this report. In order to aid comparison of the 2006 and 2005 results, additional proforma information has been provided within this statement, showing the results for that period as they would have been stated had the Group applied those provisions of IAS 32 and IAS 39 relating to accounting for the Group's loan assets. Further information is given in note 10. For all references to proforma disclosures refer to this note. A full statement of the effects of the transition to IFRS was issued by the Group on 21 February 2006.

Consolidated income statement

For the six months ended 31 March 2006 (Unaudited)

	Six months to 31 March 2006 £m	Six months to 31 March 2005 Proforma £m	Six months to 31 March 2005 Statutory £m
Interest receivable	**254.9**	240.0	241.6
Interest payable and similar charges	**(183.6)**	(178.6)	(196.5)
Net interest income	**71.3**	61.4	45.1
Other operating income	**15.2**	14.9	18.0
Total operating income	**86.5**	76.3	63.1
Operating expenses	**(24.8)**	(21.1)	(21.1)
Provisions for losses	**(23.6)**	(20.7)	(8.5)
	38.1	34.5	33.5
Fair value net gains / (losses)	**0.9**	-	-
Operating profit being profit on ordinary activities before taxation	**39.0**	34.5	33.5
Tax charge on profit on ordinary activities	**(6.5)**	(7.9)	(7.6)
Profit on ordinary activities after taxation	**32.5**	26.6	25.9
Proposed dividend – Rate per share	**6.9p**	5.2p	5.2p
Basic earnings per share	**28.8p**	23.3p	22.7p
Diluted earnings per share	**27.4p**	22.4p	21.8p

For management purposes the Group is organised into two major operating divisions, Buy-to-Let Mortgages and Consumer Finance, which includes secured lending and car and retail finance. These divisions are the basis on which the Group reports primary segmental information.

Other Operations comprises closed loan books arising from owner-occupied mortgages and unsecured personal lending operations where no further new business is being written and existing assets are being run down.

The adjusted operating results of these business segments are detailed fully in note 3 and are summarised below.

	Six months to 31 March 2006	Six months to 31 March 2005 Proforma	Six months to 31 March 2005 Statutory
	£m	£m	£m
Operating result before fair value adjustments			
Buy-to-Let Mortgages	**23.0**	17.1	14.8
Consumer Finance	**12.1**	9.5	8.1
Other Operations	**3.0**	7.9	10.6
	38.1	34.5	33.5

Net interest income increased by 16.1% to £71.3 million from £61.4 million on a proforma basis for the first half of 2005, as a result of the growth of the loan portfolio. Average margins were similar to the first half of 2005, reflecting the predominance of buy-to-let lending in the Group's business, where improvements in funding costs compensated for more competitive pricing in the buy-to-let book. This, in turn, helped to drive the strong book growth seen over the period.

Other operating income was similar to the first half of 2005 at £15.2 million, compared with £14.9 million on a proforma basis.

Operating expenses increased by 17.5% to £24.8 million from £21.1 million for the first half of 2005. Of this increase, £2.0 million relates to the charge for share based payment and is partially driven by the impact of the increased share price over the period on the value of share based awards. Excluding the charge for share based payment, operating expenses rose 8.8% to £21.1 million from £19.4 million in the first half of 2005. Control over operating costs, through tight financial discipline and by maintaining cost efficiency, continues to be a major focus of the Group's management and is a significant driver for our competitive position in our lending markets.

The charge for impairment provisions of £23.6 million compares with £20.7 million on a proforma basis for the first half of 2005. As a percentage of loans to customers (note 6) the charge remained consistent (on the proforma basis) with that for the first half of 2005 at 0.3%. This charge includes amounts in respect of income which, although accounting standards require it to be charged, is not expected to be received by the Group and hence also increases the charge for loan impairment. Under UK GAAP such income was not recognised. The loan books continue to be carefully managed and the arrears performance remains in line with our expectations, with the buy-to-let book continuing to be exemplary.

Fair value net gains of £0.9 million have arisen from the IFRS requirement that movements in the fair value of hedging instruments attributable to ineffectiveness in the hedging arrangements should be credited or charged to income and expense. Any ineffectiveness arising from differences between the fair value movements of hedging instruments and the fair value movements of the hedged assets or liabilities should trend to zero over time, so any recorded inefficiencies should be excluded when considering the underlying results of any accounting period.

The charge to tax has been reduced by an exceptional credit of £4.3 million as a result of the settlement of a prior year item, reducing the tax charge rate to 16.7% for the period.

Review of operations

Buy-to-Let Mortgages

Buy-to-let mortgage completions were £1,334.5 million for the six months to 31 March 2006, an increase of 111.4% from £631.4 million for the corresponding period last year. At 31 March 2006, the aggregate loans outstanding in the Paragon Mortgages and Mortgage Trust buy-to-let portfolios had increased by 35.6% to £5,964.9 million from £4,400.0 million at 31 March 2005 on the proforma basis (35.6% increase on the statutory basis from £4,398.6 million). A strong pipeline of new business at the end of the period should ensure a strong start to the second half of the year.

The housing market has remained robust over the winter period and activity amongst buy-to-let landlords has been building since mid 2005. This is evidenced by the Council of Mortgage Lenders' buy-to-let survey for the second half of 2005, which showed a net increase of 70,000 outstanding buy-to-let mortgages over the six month period. Buy-to-let advances totalled 9% of gross UK mortgage advances in the six months to December 2005, up from 8% in the previous half year. This accords with the latest surveys by the Royal Institution of Chartered Surveyors, which report a rise in new landlord instructions on the back of very strong tenant demand.

Following the acquisition of Mortgage Trust, the Group's strategy has been to operate on a broad front within the buy-to-let market. The success of the development of the Mortgage Trust proposition, along with developments at Paragon Mortgages has allowed the Group to capitalise on rising tenant demand and on the uplift in landlord activity by competing effectively for the business of a broad range of residential landlords with differing portfolio sizes and investment objectives.

Consumer Finance

Completions by the consumer finance businesses were £189.2 million during the period, an increase of 4.8% from £180.6 million during the corresponding period of the previous year. At 31 March 2006, the total loans outstanding on the consumer finance books were £703.7 million, compared with £711.2 million on the proforma basis at 31 March 2005 (£718.1 million on the statutory basis). This fall reflects the general weakness in the consumer lending markets and our objective of maintaining portfolio quality.

The division continues to focus on writing high quality loans, and bad debt levels within the business remain below the market averages.

Secured Personal Finance

Weaker consumer activity has continued to impact consumer lending. Data published by the Finance & Leasing Association during the period has evidenced lower secured lending volumes against the corresponding period last year. In this environment we remain cautious and have tightened our credit policy to ensure the maintenance of high quality lending. Secured personal finance advances were £117.6 million, a reduction of 6.2% from £125.4 million in the first half of 2005.

Sales Aid Finance

The sales aid finance business, incorporating retail and car finance, saw a 29.7% increase in volumes to £71.6 million during the six months ended 31 March 2006 (2005 H1: £55.2 million). The refocusing of the retail business on expanding the distribution base has led to many new retailer accounts where retailers have been attracted by our technology and service. Our objective is to build on this progress during the second half of the year.

Funding

The Group continued to be an active issuer in the capital markets during the period. In November 2005, a £1.0 billion securitisation was completed by Paragon Mortgages (No. 10) PLC and, in March 2006, a further £1.0 billion securitisation was completed by Paragon Mortgages (No. 11) PLC. Each of these was completed on more favourable terms than the preceding transaction, reflecting the increasingly positive attitude of investors in the capital markets to our buy-to-let mortgage originations.

In order to provide finance for the increased level of loan completions, the Group's committed sterling warehouse facility, provided by a consortium of banks, was increased in April 2006 from £1,425.0 million to £2,325.0 million, on finer terms.

Pension scheme

During the period the Group made a special contribution of £14.6 million to the Paragon Pension Scheme. The amount was equal to the IAS 19 deficit at 30 September 2005 and the special contribution puts the scheme on a more secure financial footing, as well as minimising the Group's ongoing payments to the Pension Protection Fund.

Capital management

Last May we reported, as a consequence of the changing mix of the Group's business, that the Board had identified surplus capital available for distribution to shareholders. As a consequence the dividend was significantly increased and a share repurchase programme of up to £20.0 million was established. During the period the Company bought 429,000 shares from the market at a cost of £3.2 million with the result that by 31 March 2006 a total of 2,219,000 shares had been repurchased, at a total cost of £11.6 million. A further 1,000,000 shares have been repurchased since 31 March 2006 at a cost of £6.8 million.

Over the period we have continued to reduce the risk profile of the Group's loan assets through a disciplined restructuring of the portfolio from unsecured towards less capital demanding secured lending. As a result, the Board will increase the amount set aside to repurchase shares from the market by a further £10.0 million, within the authority granted by shareholders at the 2006 Annual General Meeting. This will make available a further £11.6 million to be invested in the repurchase programme going forward.

Conclusion

The Group has had an excellent first half, with strong growth in profits and business volumes and the credit performance of the loan books remains in line with our expectations. In addition we have continued to develop our buy-to-let product proposition to compete for the business of a broad range of investors. A strong cash position has enabled the Group to make a special contribution to the staff pension scheme, to announce a further substantial increase in dividend and to extend the share buy-back programme.

We enter the second half of the year with the buy-to-let mortgage pipeline significantly higher than last year which, with a continued focus on cost and arrears management, leaves us confident that the Group will meet its business objectives for the year. Strong tenant demand over the period reflects the increasing importance of the private rented sector in today's housing market and the drivers to demand point to a favourable long-term outlook for this business.

Jonathan Perry
Chairman
23 May 2006

Consolidated income statement

For the six months ended 31 March 2006 (Unaudited)

	Note	**Six months to 31 March 2006 £m**	Six months to 31 March 2005 £m	Year to 30 September 2005 £m
Interest receivable		**254.9**	241.6	485.8
Interest payable and similar charges		**(183.6)**	(196.5)	(390.8)
Net interest income		**71.3**	45.1	95.0
Other operating income		**15.2**	18.0	37.9
Total operating income		**86.5**	63.1	132.9
Operating expenses		**(24.8)**	(21.1)	(45.2)
Provisions for losses		**(23.6)**	(8.5)	(15.9)
		38.1	33.5	71.8
Fair value net gains / (losses)		**0.9**	-	-
Operating profit being profit on ordinary activities before taxation		**39.0**	33.5	71.8
Tax charge on profit on ordinary activities		**(6.5)**	(7.6)	(16.0)
Profit on ordinary activities after taxation		**32.5**	25.9	55.8
Dividend – rate per share	5	**6.9p**	5.2p	12.6p
Basic earnings per share	4	**28.8p**	22.7p	48.9p
Diluted earnings per share	4	**27.4p**	21.8p	46.9p

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

Consolidated balance sheet

31 March 2006 (Unaudited)

	Note	**31 March 2006** £m	31 March 2005 £m	30 September 2005 £m
Assets employed				
Non-current assets				
Intangible assets		**0.4**	0.3	0.3
Property, plant and equipment		**19.8**	20.5	19.7
Financial assets	6	**7,276.4**	6,087.0	6,528.7
Deferred tax assets		**36.5**	5.7	5.7
		7,333.1	6,113.5	6,554.4
Current assets				
Other receivables		**4.7**	6.4	6.6
Cash and cash equivalents		**734.5**	549.2	530.4
		739.2	555.6	537.0
Total assets		**8,072.3**	6,669.1	7,091.4
Financed by				
Called-up share capital		**12.1**	12.0	12.1
Share premium account		**70.8**	69.5	70.2
Merger reserve		**(70.2)**	(70.2)	(70.2)
Cash flow hedging reserve		**(1.9)**	-	-
Profit and loss account		**279.7**	297.8	323.5
Share capital and reserves		**290.5**	309.1	335.6
Own shares		**(28.4)**	(13.8)	(22.8)
Equity shareholders' funds		**262.1**	295.3	312.8
Current liabilities				
Financial liabilities		**28.5**	1.0	0.9
Current tax liabilities		**10.8**	13.6	12.9
Other liabilities		**58.8**	59.3	59.9
		98.1	73.9	73.7
Non-current liabilities				
Financial liabilities		**7,705.4**	6,278.1	6,684.8
Deferred tax liabilities		**0.7**	2.1	0.7
Retirement benefit obligations		**0.3**	14.5	14.6
Provisions		**2.1**	2.4	2.1
Other liabilities		**3.6**	2.8	2.7
		7,712.1	6,299.9	6,704.9
Total liabilities		**7,810.2**	6,373.8	6,778.6
		8,072.3	6,669.1	7,091.4

The interim financial information was approved by the Board of Directors on 23 May 2006.

Consolidated cash flow statement

For the six months ended 31 March 2006 (Unaudited)

	Note	**Six months to 31 March 2006 £m**	Six months to 31 March 2005 £m	Year to 30 September 2005 £m
Net cash flow (used in) operating activities	7	**(779.4)**	(94.0)	(500.7)
Net cash (used in)/from investing activities	8	**(2.0)**	1.1	(0.3)
Net cash from financing activities	9	**985.5**	140.8	530.3
Net increase in cash and cash equivalents		**204.1**	47.9	29.3
Opening cash and cash equivalents		**529.9**	500.6	500.6
Closing cash and cash equivalents		**734.0**	548.5	529.9
Represented by balances within				
Cash and cash equivalents		**734.5**	549.2	530.4
Financial liabilities		**(0.5)**	(0.7)	(0.5)
		734.0	548.5	529.9

Consolidated statement of recognised income and expenditure

Six months ended 31 March 2006 (Unaudited)

	31 March 2006 £m	31 March 2005 £m	30 September 2005 £m
Profit for the period	**32.5**	25.9	55.8
Actuarial (loss) on pension deficit	**(0.6)**	-	-
Cash flow hedges			
Gains / (losses) taken to equity	**1.0**	-	-
Tax on items taken directly to equity	**(0.1)**	-	-
Total recognised income and expenditure for the period	**32.8**	25.9	55.8
Adoption of IAS 32 and IAS 39	**(72.5)**	-	-
	(39.7)	25.9	55.8

Reconciliation of movements in consolidated equity

Six months ended 31 March 2006 (Unaudited)

	Note	**31 March 2006 £m**	31 March 2005 £m	30 September 2005 £m
Total recognised income and expenditure for the period		**32.8**	25.9	55.8
Dividends	5	**(8.4)**	(6.5)	(12.4)
Net movement in own shares		**(5.6)**	(1.5)	(10.5)
Surplus on transactions in own shares		**0.8**	1.3	2.3
Charge for share based payments		**2.2**	1.1	2.6
Total movements in equity in the period		**21.8**	20.3	37.8
Equity at 30 September 2005		**312.8**	275.0	275.0
Adoption of IAS 32 and IAS 39		**(72.5)**	-	-
Equity at 1 October 2005		**240.3**	275.0	275.0
Closing equity		**262.1**	295.3	312.8

Notes to the interim financial information

For the six months ended 31 March 2006 (Unaudited)

1. General information

The interim financial information for the six months ended 31 March 2006 and for the six months ended 31 March 2005 has not been audited.

The next annual financial statements of the Group, for the year ending 30 September 2006, will be prepared in accordance with International Financial Reporting Standards as adopted for use in the European Union. Accordingly, the interim report has been prepared in accordance with the recognition and measurement criteria of IFRS.

The figures shown above for the year ended 30 September 2005 are not statutory accounts. A copy of the statutory accounts, which were prepared under UK GAAP, has been delivered to the Registrar of Companies, contained an unqualified audit report and did not contain an adverse statement under sections 237 (2) or 237 (3) of the Companies Act 1985.

This document may contain forward-looking statements with respect to certain of the plans and current goals and expectations relating to the future financial conditions, business performance and results of the Group. 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 including, amongst other things, UK domestic and global economic and business conditions, market related risk such as fluctuation in interest rates and exchange rates, inflation, deflation, the impact of competition, changes in customer preferences, risks concerning borrower credit quality, delays in implementing proposals, the timing, impact and other uncertainties of future acquisitions or other combinations within relevant industries, the policies and actions of regulatory authorities, the impact of tax or other legislation and other regulations in the jurisdictions in which the Group and its affiliates operate. As a result, the Group's actual future financial condition, business performance and results may differ materially from the plans, goals and expectations expressed or implied in these forward looking statements. Nothing in this document should be construed as a profit forecast.

A copy of the Interim Statement will be posted to shareholders and additional copies can be obtained from The Company Secretary, The Paragon Group of Companies PLC, St. Catherine's Court, Herbert Road, Solihull, West Midlands, B91 3QE.

2. Accounting policies

The financial information has been prepared in accordance with International Financial Reporting Standards as endorsed by the European Union expected to be applicable in the preparation of the Group Financial Statements for the year ending 30 September 2006, except that, as permitted by IFRS 1 – 'First Time Adoption of International Financial Reporting Standards' the requirements of IAS 32 – 'Financial Instruments: Disclosure and Presentation' and IAS 39 – 'Financial Instruments: Recognition and Measurement' have not been applied in preparing the comparative amounts for the year ended 30 September 2005. In these disclosures, financial instruments are accounted for using the policies and practices previously adopted under UK GAAP.

The particular policies adopted are described below.

(a) Accounting convention

The financial information is prepared under the historical cost convention, except as required in the valuation of certain financial instruments which are carried at fair value.

(b) Basis of consolidation

The consolidated financial information deals with the accounts of the Company and its subsidiaries made up to 31 March 2006. Subsidiaries comprise all those entities over which the Group has control. The results of businesses acquired are dealt with in the consolidated accounts from the date of acquisition.

In accordance with SIC 12 – 'Consolidation: Special Purpose Entities' companies owned by charitable trusts into which loans originated by Mortgage Trust Limited were sold as part of its securitisation programme where the Group enjoys the benefits of ownership are treated as subsidiaries.

Similarly trusts set up to hold shares in conjunction with the Group's employee share ownership arrangements are also treated as subsidiaries.

(c) Goodwill

Goodwill arising from the purchase of subsidiary undertakings, representing the excess of the fair values of acquired assets over the fair value of the purchase consideration, is held on the balance sheet and annually reviewed to determine whether any impairment has occurred.

Negative goodwill is written off as it arises.

As permitted by IFRS 1, the Group has elected not to apply IFRS 3 – 'Business Combinations' to combinations taking place before its transition date to IFRS (1 October 2004). Therefore any goodwill which was written off to reserves under UK GAAP will not be charged or credited to the profit and loss account on any future disposal of the business to which it relates.

(d) Intangible assets

Intangible assets comprise purchased computer software, which is capitalised where it has a sufficiently enduring nature. This is stated at cost less accumulated amortisation. Amortisation is provided in equal instalments at a rate of 25% per annum.

(e) Leases

Leases are accounted for as operating or finance leases in accordance with IAS 17 – 'Leases'. A finance lease is deemed to be one which transfers substantially all of the risks and rewards of the ownership of the asset concerned. Any other lease is an operating lease.

Rental income and costs under operating leases are credited or charged to the profit and loss account over the period of the leases.

(f) Contract hire

Motor vehicles acquired in connection with contract hire arrangements are sold to finance houses, who lease them to customers for a pre-determined period. The Group has undertaken to repurchase these vehicles at the end of the lease term.

In accordance with the requirements of IAS 17, the assets are not derecognised on the sale to the finance house and remain as the Group's assets and the consideration received is spread over the customer's lease term.

(g) Property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation. Cost for property held under a sale and leaseback transaction represents the sale value.

Depreciation is provided on cost in equal annual instalments over the lives of the assets. The rates of depreciation are as follows:

Short leasehold premises	over the term of the lease
Computer hardware	25% per annum
Furniture, fixtures and office equipment	15% per annum
Company motor vehicles	25% per annum
Motor vehicles subject to contract hire arrangements	over the term of the lease

(h) Loans to customers

In the results for the six months ended 31 March 2006

Loans to customers are considered to be 'loans and receivables' as defined by IAS 39 – 'Financial Instruments: Recognition and Measurement'. They are therefore accounted for on the amortised cost basis.

Such loans are valued at inception at the initial advance amount, which is the fair value at that time, inclusive of procuration fees paid to brokers or other business providers and less initial fees paid by the customer. Thereafter they are valued at this amount less the cumulative amortisation calculated using the Effective Interest Rate ('EIR') method. The loan balances are then reduced where necessary by a provision for balances which are considered to be impaired.

The EIR method spreads the expected net income arising from a loan over its expected life. The EIR is that rate of interest which, at inception, exactly discounts the future cash payments and receipts arising from the loan to the initial carrying amount.

The Group's policy is to hedge against any exposure to fixed rate loan assets.

In the results for the year ended 30 September 2005

Loans are stated at cost, inclusive of brokers' commissions payable on origination, less provision for diminution in value.

Brokers' commissions payable on mortgage loans are amortised over an appropriate period. Unamortised commission balances are included within 'Loans to Customers'.

Brokers' commissions payable on other loans are amortised on a straight-line basis over the period of the loans to which they relate. The balances being amortised are included within 'Loans to Customers'.

Amortisation of brokers' commissions is recognised within interest payable.

Interest arising on loans is recognised in the profit and loss account as it is charged to borrowers, to the extent that is expected to be recoverable. Other fee income arising from borrower accounts is recognised in 'other income' as it is charged.

(i) Finance lease receivables

Finance lease receivables are included within 'Loans to Customers' at the total amount receivable less interest not yet accrued, unamortised commissions and provision for doubtful debts.

Income from finance lease contracts is accounted for on the actuarial basis.

(j) Impairment of loans and receivables

In the results for the six months ended 31 March 2006

Loans and receivables are reviewed for indications of possible impairment throughout the year and at each balance sheet date, in accordance with IAS 39. Where loans exhibit objective evidence of impairment, the carrying value of the loans is reduced to the net present value of their expected future cash flows, including the value of the potential realisation of any security, discounted at the original EIR. Loans are assessed collectively, grouped by risk characteristics and account is taken of any impairment arising due to events which are believed to have taken place but have not been specifically identified at the balance sheet date.

In the results for the year ended 30 September 2005

The amount provided is an estimate of the amount needed to reduce the carrying value of the asset to its expected recoverable amount and is based on the application of formulae which take into account the nature of each portfolio, borrower payment profile and expected losses.

(k) Cash and cash equivalents

Balances shown as cash and cash equivalents in the balance sheet comprise demand deposits and short-term deposits with banks with maturities of not more than 90 days.

(l) Own shares

Shares in The Paragon Group of Companies PLC held in treasury or by the trustees of the Group's employee share ownership plans are shown on the balance sheet as a deduction in arriving at total equity. Own shares are stated at cost.

(m) Taxation

The charge for taxation is based on the profit for the period and takes into account taxation deferred because of temporary differences. Temporary differences arise from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in financial statements.

Tax relating to items taken directly to equity is also taken directly to equity.

(n) Borrowings

In the results for the six months ended 31 March 2006

Borrowings are carried in the balance sheet on the amortised cost basis. The initial value recognised includes the principal amount received less any discount on issue or costs of issuance.

Interest and all other costs of the funding are expensed to the income statement as interest payable over the term of the borrowing on an Effective Interest Rate basis.

In the results for the year ended 30 September 2005

Borrowings are stated at their outstanding value less unamortised issue costs and discounts on issue. Discounts on issue of borrowings and initial costs incurred in arranging funding facilities are amortised over the period of the facility.

(o) Finance lease payables

Balances due on the lease arising from the sale and leaseback of a Group property are recognised in creditors at the total amount payable less interest not yet accrued. Interest is accrued for on the actuarial basis.

The profit which arose on the sale and leaseback transaction is held in accruals and deferred income and is being credited to profit over the lease term on a straight line basis.

(p) Derivative financial instruments

In the results for the six months ended 31 March 2006

Derivative instruments utilised by the Group comprise currency swap, interest rate swap, interest rate option and forward interest rate agreements. All such instruments are used for hedging purposes to alter the risk profile of the existing underlying exposure of the Group in line with the Group's risk management policies.

The Group does not enter into speculative derivative contracts.

All derivatives are carried at fair value in the balance sheet, as assets where the value is positive or as liabilities where the value is negative. Fair value is based on market prices, where a market exists. If there is no active market, fair value is calculated using present value models which incorporate assumptions based on market conditions and are consistent with accepted economic methodologies for pricing financial instruments. Changes in the fair value of derivatives are recognised in the income statement, except where such amounts are permitted to be taken to equity as part of the accounting for a cash flow hedge.

In the results for the year ended 30 September 2005

Derivative instruments utilised by the Group comprise currency swap, interest rate swap, interest rate option and forward interest rate agreements. All such instruments are used for hedging purposes to alter the risk profile of the existing underlying exposure of the Group in line with the Group's risk management policies. Amounts payable or receivable in respect of interest rate swaps are recognised as adjustments to interest expense over the period of the contracts. The Group does not enter into speculative derivative contracts.

(q) Hedging

In the results for the six months ended 31 March 2006

For all hedges, the Group documents, at inception, the relationship between the hedging instruments and the hedged items, as well as its risk management strategy and objectives for undertaking the transaction. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the hedging arrangements put in place are considered to be 'highly effective' as defined by IAS 39.

For a fair value hedge, as long as the hedging relationship is deemed 'highly effective' and meets the hedging requirements of IAS 39, any gain or loss on the hedging instrument recognised in income can be offset against the fair value loss or gain arising from the hedged item for the hedged risk. For macro hedges (hedges of interest rate risk for a portfolio of loan assets) this fair value adjustment is disclosed in the balance sheet alongside the hedged item, for other hedges the adjustment is made to the carrying value of the hedged asset or liability. Only the net ineffectiveness of the hedge is charged or credited to income. Where a fair value hedge relationship is terminated, or deemed ineffective, the fair value adjustment is amortised over the remaining term of the underlying item.

Where a derivative is used to hedge the variability of cash flows of an asset or liability, it may be designated as a cash flow hedge so long as this relationship meets the hedging requirements of IAS 39. For such an instrument the effective portion of the change in the fair value of the derivative is taken initially to equity, with the ineffective part taken to profit or loss. The amount taken to equity is released to the income statement at the same time as the hedged item affects the income statement. Where a cash flow hedge relationship is terminated, or deemed ineffective, the amount taken to equity will remain there until the hedged transaction is recognised, or is no longer highly probable.

(r) Deferred taxation

Deferred taxation is provided in full on temporary differences that result in an obligation at the balance sheet date to pay more tax, or a right to pay less tax, at a future date, at rates expected to apply when they crystallise based on current tax rates and law. Deferred tax assets are recognised to the extent that it is regarded as probable that they will be recovered. As required by IAS 12 – 'Income Taxes', deferred tax assets and liabilities are not discounted to take account of the expected timing of realisation.

It is assumed that all taxable IFRS transition adjustments give rise to tax adjustments to reserves at the current UK tax rate of 30%, although this has yet to be confirmed by HM Revenue and Customs.

(s) Retirement benefit obligations

The expected cost of providing pensions within the funded defined benefit scheme, determined on the basis of annual valuations by professionally qualified actuaries using the projected unit method, is charged to the profit and loss. Actuarial gains and losses are recognised in full in the period in which they occur and do not form part of the result for the period, being recognised in the Statement of Recognised Income and Expenditure.

The retirement benefit obligation recognised in the balance sheet represents the present value of the defined benefit obligation, as adjusted for unrecognised past service cost, and as reduced by the fair value of scheme assets at the balance sheet date.

Both the return on investment expected in the period and the expected financing cost of the liability, as estimated at the beginning of the period are recognised in the result for the period. Any variances against these estimates in the year form part of the actuarial gain or loss.

The assets of the scheme are held separately from those of the Group in an independently administered fund.

The charge to the profit and loss account for providing pensions under defined contribution pension schemes is equal to the contributions payable to such schemes for the year.

(t) Provisions

Provisions are recognised where there is a present obligation as a result of a past event, it is probable that this obligation will result in an outflow of resources and this outflow can be reliably quantified. Provisions are discounted where this effect is material.

(u) Fee and commission income

Other income includes administration fees charged to borrowers, which are credited when the related service is performed and commissions receivable on the sale of insurances, which are taken to profit at the point at which the Group becomes unconditionally entitled to the income.

(v) Share based payments

In accordance with IFRS 2 – 'Share based payments', the fair value at the date of grant of awards to be made in respect of options and shares granted under the terms of the Group's various share based employee incentive arrangements is charged to the profit and loss account over the period between the date of grant and the vesting date.

As permitted by IFRS 1, only those options and awards granted after 7 November 2002 and not vested at 1 January 2005 have been restated on transition to IFRS.

(w) Dividends

In accordance with IAS 10 – 'Events after the balance sheet date', dividends payable on ordinary shares are recognised in equity once they are appropriately authorised and are no longer at the discretion of the Company. Dividends declared after the balance sheet date, but before the authorisation of the financial statements remain within shareholders' funds.

(x) Foreign currency

Foreign currency transactions, assets and liabilities are accounted for in accordance with IAS 21 – 'The Effects of Changes in Foreign Exchange Rates'. The functional currency of the Group is the pound sterling. Transactions which are not denominated in sterling are translated into sterling at the spot rate of exchange on the date of transaction. Monetary assets and liabilities which are not denominated in sterling are translated at the closing rate on the balance sheet date.

Gains and losses on retranslation are included in interest payable or interest receivable depending on whether the underlying instrument is an asset or a liability, except where deferred in equity in accordance with cash flow hedging provisions of IAS 39.

(y) Segmental reporting

Costs attributed to each segment represent the direct costs incurred by the segment operations and an allocation of the costs of areas of the business which serve all segments. Such allocations are weighted by the value of loan assets in each segment, adjusted for the relative effort involved in the administration of each asset class.

3. Segmental results

For management purposes the Group is organised into two major operating divisions, Buy-to-Let Mortgages and Consumer Lending, which includes secured lending and car and retail finance. These divisions are the basis on which the Group reports primary segmental information. All of the Group's operations are conducted in the United Kingdom.

Other Operations comprises closed loan books arising from owner-occupied mortgages and unsecured personal lending operations where no further new business is being written and existing assets are being run down.

Financial information about these business segments is shown below.

Six months ended 31 March 2006

	Buy-to-Let Mortgages £m	Consumer Lending £m	Other Operations £m	Total £m
Interest receivable	171.8	30.2	52.9	254.9
Interest payable	(143.4)	(21.0)	(19.2)	(183.6)
Net interest income	28.4	9.2	33.7	71.3
Other operating income	3.7	8.6	2.9	15.2
Total operating income	32.1	17.8	36.6	86.5
Operating expenses	(9.0)	(4.4)	(11.4)	(24.8)
Provisions	(0.1)	(1.3)	(22.2)	(23.6)
	23.0	12.1	3.0	38.1
Fair value gains/(losses)	-	-	0.9	0.9
Operating profit	23.0	12.1	3.9	39.0

Six months ended 31 March 2005

	Buy-to-Let Mortgages £m	Consumer Lending £m	Other Operations £m	Total £m
Interest receivable	145.8	42.3	53.5	241.6
Interest payable	(128.7)	(34.3)	(33.5)	(196.5)
Net interest income	17.1	8.0	20.0	45.1
Other operating income	5.5	8.3	4.2	18.0
Total operating income	22.6	16.3	24.2	63.1
Operating expenses	(8.3)	(3.8)	(9.0)	(21.1)
Provisions	0.5	(4.4)	(4.6)	(8.5)
	14.8	8.1	10.6	33.5
Fair value gains/(losses)	-	-	-	-
Operating profit	14.8	8.1	10.6	33.5

Year ended 30 September 2005

	Buy-to-Let Mortgages £m	Consumer Lending £m	Other Operations £m	Total £m
Interest receivable	298.2	84.7	102.9	485.8
Interest payable	(263.7)	(68.6)	(58.5)	(390.8)
Net interest income	34.5	16.1	44.4	95.0
Other operating income	13.7	17.2	7.0	37.9
Total operating income	48.2	33.3	51.4	132.9
Operating expenses	(18.2)	(7.9)	(19.1)	(45.2)
Provisions	(1.2)	(4.6)	(10.1)	(15.9)
	28.8	20.8	22.2	71.8
Fair value gains/(losses)	-	-	-	-
Operating profit	28.8	20.8	22.2	71.8

4. Earnings per share

Earnings per ordinary share is calculated as follows:

		31 March 2006	31 March 2005	30 September 2005
Profit for the period (£m)		**32.5**	25.9	55.8
Basic weighted average number of ordinary shares ranking for dividend during the year (million)		**113.1**	114.2	114.1
Dilutive effect of the weighted average number of share options and incentive plans in issue during the year (million)		**5.6**	4.8	4.9
Diluted weighted average number of ordinary shares ranking for dividend during the year (million)		**118.7**	119.0	119.0
Earnings per ordinary share	- basic	**28.8p**	22.7p	48.9p
	- diluted	**27.4p**	21.8p	46.9p

5. Dividends

Amounts recognised as distributions to equity shareholders in the period:

	31 March 2006 £m	31 March 2005 £m	30 September 2005 £m
Final dividend for the year ended 30 September 2004 of 5.7p per share	**-**	6.5	6.5
Interim dividend for the year ended 30 September 2005 of 5.2p per share	**-**	-	5.9
Final dividend for the year ended 30 September 2005 of 7.4p per share	**8.4**	-	-
	8.4	6.5	12.4

An interim dividend of 6.9p per share is proposed (2005: 5.2p per share), payable on 31 July 2006 with a record date of 30 June 2006. This dividend will be recognised in the accounts when it is paid.

6. Financial assets

	31 March 2006 **£m**	31 March 2005 £m	30 September 2005 £m
Loans to customers	**7,232.9**	6,087.0	6,528.7
Fair value adjustments from portfolio hedging	**(1.0)**	-	-
Derivative financial assets	**44.5**	-	-
	7,276.4	6,087.0	6,528.7

7. Net cashflow from operating activities

	Six months to 31 March 2006 **£m**	Six months to 31 March 2005 £m	Year to 30 September 2005 £m
Profit before tax	**39.0**	33.5	71.8
Non-cash items included in profit and other adjustments			
Depreciation of property plant and equipment	**1.6**	1.7	3.8
Amortisation of intangible assets	**0.1**	0.1	0.2
Non-cash movements on borrowings	**61.2**	4.0	7.4
Impairment losses on loans to customers	**23.6**	8.5	15.9
Charge for share based payment	**2.2**	1.1	2.6
Profit on sale of subsidiary	**-**	(0.9)	(0.9)
Loss on disposal of property, plant and equipment	**0.1**	-	-
Net (increase) / decrease in operating assets			
Loans to customers	**(824.9)**	(145.5)	(594.4)
Derivative financial instruments	**(20.6)**	-	-
Fair value of portfolio hedges	**1.0**	-	-
Other receivables	**(0.4)**	1.1	1.0
Net increase / (decrease) in operating liabilities			
Derivative financial instruments	**(39.7)**	-	-
Sundry liabilities	**(14.0)**	4.0	4.1
Cash utilised by operations	**(770.8)**	(92.4)	(488.5)
Income taxes paid	**(8.6)**	(1.6)	(12.2)
Net cash flow used in operating activities	**(779.4)**	(94.0)	(500.7)

8. Net cashflow used in investing activities

	Six months to 31 March 2006 £m	Six months to 31 March 2005 £m	Year to 30 September 2005 £m
Proceeds on disposal of property, plant and equipment	**0.7**	0.9	1.6
Purchases of property, plant and equipment	**(2.5)**	(1.7)	(3.7)
Purchases of intangible assets	**(0.2)**	(0.1)	(0.2)
Sale of subsidiary undertaking	**-**	2.0	2.0
Net cash (used in) / from investing activities	**(2.0)**	1.1	(0.3)

9. Net cashflow from financing activities

	Six months to 31 March 2006 £m	Six months to 31 March 2005 £m	Year to 30 September 2005 £m
Dividends paid	**(8.4)**	(6.5)	(12.4)
Issue of corporate bond	**-**	-	118.0
Issue of asset backed floating rate notes	**1,996.6**	1,297.3	2,444.7
Repayment of asset backed floating rate notes	**(468.3)**	(1,057.4)	(2,102.1)
Capital element of finance lease payments	**(0.3)**	(0.2)	(0.3)
Movement on bank facilities	**(529.3)**	(92.2)	90.6
Purchase of shares	**(6.7)**	(2.9)	(12.4)
Exercise of options under ESOP scheme	**1.2**	0.7	1.5
Exercise of other share options	**0.7**	2.0	2.7
Net cash from financing activities	**985.5**	140.8	530.3

10. Transition to international financial reporting standards

As described in Note 2, these results are presented in accordance with International Financial Reporting Standards as endorsed by the European Union ('IFRS'). On 21 February 2006 the Group announced details of the adjustments to its accounting policies required in order to convert the previously published results to an IFRS basis. All IFRS information relating to the year ended 30 September 2005 disclosed in this statement is derived from that announcement. This document also included reconciliations of the balance sheets and profit and loss accounts previously published to those shown as comparative amounts in this interim financial information. The Group has taken advantage of the transitional provisions of IFRS 1 and these comparative figures do not show the effect of the adoption of IAS 32 and IAS 39.

To enable a more meaningful presentation of results, in addition to the statutory comparative information, the results for the six months ended 31 March 2005 and the year ended 30 September 2005 have been compiled on a proforma basis. This shows the Group's customer loan balances, borrowings and interest income as they would have been shown had IAS 32 and 39 applied to these balances. The remaining adjustments required by these standards relate to fair values and hedging and cannot be applied as the required documentation for these arrangements was not in place at 1 October 2004. A reconciliation between the statutory comparatives and the proforma information was given in the announcement of 21 February 2006. The differences in the segment results and segmental 'loans to customers' figures between the statutory and proforma bases are also detailed in the announcement.

The cash flow statements have also been restated to comply with the requirements of IAS 7 – 'Cash Flow Statements'. These changes represent the re-classification of balances only.

Copies of the announcement made on 21 February 2006 are available from the Group's website at www.paragon-group.co.uk or from the Group Company Secretary, The Paragon Group of Companies PLC, St. Catherine's Court, Herbert Road, Solihull, West Midlands, B91 3QE.

Independent review report

To the Paragon Group of Companies PLC

Introduction

We have been instructed by the company to review the financial information for the six months ended 31 March 2006 which comprises the income statement, the balance sheet, the cash flow statement, the statement of recognised income and expenditure, the reconciliation of movements in consolidated equity and related notes 1 to 10. We have read the other information contained in the interim report and considered whether it contains any apparent misstatements or material inconsistencies with the financial information.

This report is made solely to the company in accordance with Bulletin 1999/4 issued by the Auditing Practices Board. Our work has been undertaken so that we might state to the company those matters we are required to state to them in an independent review 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 formed.

Directors' responsibilities

The interim report, including the financial information contained therein, is the responsibility of, and has been approved by, the directors. The directors are responsible for preparing the interim report in accordance with the Listing Rules of the Financial Services Authority which require that the accounting policies and presentation applied to the interim figures are consistent with those applied in preparing the preceding annual accounts except where any changes, and the reasons for them, are disclosed.

International financial reporting standards

As disclosed in note 1, the next annual financial statements of the Group will be prepared in accordance with International Financial Reporting Standards as adopted for use in the EU. Accordingly, the interim report has been prepared in accordance with the recognition and measurement criteria of IFRS and the disclosure requirements of the Listing Rules.

Review work performed

We conducted our review in accordance with the guidance contained in Bulletin 1999/4 issued by the Auditing Practices Board for use in the United Kingdom. A review consists principally of making enquiries of group management and applying analytical procedures to the financial information and underlying financial data and, based thereon, assessing whether the accounting policies and presentation have been consistently applied unless otherwise disclosed. A review excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions. It is substantially less in scope than an audit performed in accordance with International Standards on Auditing (UK and Ireland) and therefore provides a lower level of assurance than an audit. Accordingly, we do not express an audit opinion on the financial information.

Review conclusion

On the basis of our review we are not aware of any material modifications that should be made to the financial information as presented for the six months ended 31 March 2006.

Deloitte & Touche LLP
Chartered Accountants
Birmingham
23 May 2006

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