Homeloans (No. 4) PLC
Multi Class Mortgage Backed FRNs

UK-MBS

EXPECTED CLOSING DATE:
[•] 2002

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This pre-sale report addresses the structure and characteristics of the proposed transaction based on the information provide to Moody's as of April 2002.
*Investors should be aware that certain issues concerning this transaction have yet to be finalised. Upon conclusive review of all documents and legal information as well as any subsequent changes in information, Moody's will endeavour to assign **definitive** ratings to this transaction. The definitive ratings may differ from the **prospective** ratings set forth in this report. Moody's will disseminate the assignment of definitive ratings through its Client Service Desk..*

TRANSACTION IN BRIEF:

	Class A	Class B	Class C
Rating:	**(P)Aaa**	**(P)A2**	**(P)Baa2**
Amount:	[£198.0 million]	[£16.5 million]	[£5.5 million]
Coupon:	Libor + [•]bps	Libor + [•]bps	Libor + [•]bps
Step Up Date:	15th June 2008	15th June 2008	15th June 2008
Step Up Margin:	[•]	[•]	[•]
Final Maturity:	15th Mar. 2019	15th Sept. 2028	15th Sept. 2028

Interest Payment Dates:	15th day in March, June, September and December
Issuer:	Homeloans (No.4) PLC
Originator:	The National Home Loans Corporation plc in respect of Local Authority Mortgages, and Société Générale
Servicer	Paragon Finance PLC
Servicer of Last Resort:	Global Home Loans Limited
Trustee:	Citicorp Trustee Company Limited
Lead Manager:	Barclays Capital
Asset Characteristics:	First lien residential mortgages to individuals in England, Wales and Scotland

Summary of Provisional Pool (as at 28th February 2002):

Count:	6,150 residential loans
Provisional Balance less Accrued Arrears:	£236,397,788.75
Provisional Balance:	£270,702,727.86
LTV:	WA: 69.34%; WA LTV Indexed to Halifax 45.24%
Loan Size:	£38,438.66 Max: £300,429.17
Performance:	**Current**: (inc <=1 month arrears) £126,716,169.18 **Arrears**: 1-3 months £14,154,506.28 3-6 months £10,500,752.91 6+ months £85,026,360.38
Loan Usage:	Purchase 46.78%, Remortgage 53.22%
Concentration:	North 1.00%; N.West 7.24%; Yorks 2.63%; E.Midlands 8.33%; W. Midlands 8.94%; E.Anglia 3.42%; S.East 41.47%; S.West 6.89%; G.London 14.81%; Wales 2.45%; Scot 2.82%
Seasoning:	WA: 156.5 months 1985 0.09%; 1986 4.21%; 1987 14.59%; 1988 15.40%; 1989 25.31%; 1990 27.17%; 1991 13.21%, 1992 0.01%; 1993 0.02%
Credit Support:	First Loss Fund (1.90% of the principal balance of the notes at closing), the Class B Notes, the Class C Notes and Excess Spread.
Launch Date:	[•] 2002

RATING OPINION

Moody's has assigned prospective long term credit ratings of (**P**)**Aaa** to the Class A Notes, (**P**)**A2** to the Class B Notes and (**P**)**Baa2** to the Class C Notes of the Issuer.

Moody's issues prospective ratings in advance of the final sale of securities, and these ratings only represent Moody's preliminary opinion. Upon a conclusive review of the transaction and associated documentation, Moody's will endeavour to assign definitive rating to the Notes. A final rating may differ from a prospective rating.

The rating of the Class A Notes is based upon an analysis of the characteristics of the mortgage pool backing the Notes, the protection the Notes receive from credit enhancement against defaults and arrears in the mortgage pool, and the legal and structural integrity of the issue.

The ratings of the Class B and Class C Notes are based on the above factors, and on an assessment of the extent of their subordinate position within the structure.

The ratings of each of the Notes address the timely payment of interest, and ultimate payment of principal.

Collateral

The portfolio consists of highly seasoned first lien residential mortgage loans; all originated between 1985 and 1993. They were previously securitised from 1994 to 1998 in six deals (Homer Finance 3, Homeloans 1-3, and Finance for People 1 & 2). The mortgages were originated during the boom time of the late 1980's and with the exception of the Société Générale originated assets, with limited certification of income, and a small amount of properties purchased under the Right to Buy scheme (former Local Authority properties purchased by the tenants at a discount to market value). The combination of the real estate market downturn and high interest rates of the early 1990's resulted in a period of high arrears and losses in portfolios originated during that time, with many borrowers suffering from negative equity. Moody's has some concerns that a minority of borrowers may remain in a negative equity position, as prior loss experience suggests. Some marginal properties, that were considered desirable "starter homes" in that property market, may have limited re-sale value today, even after more than a decade of rising house prices.

The current pool represents the remainder of the loans originated by Paragon's predecessor (The National Home Loans Corporation plc and affiliated entities) during that period. It is characterised by high arrears, and a significant number of borrowers suffering from financial hardship. Approximately [46]% of the provisional pool is 1 or more payment in arrears (Arrears Mortgages) and approximately [31]% of the loans are 12 or more payments in arrears. The weighted average LTV of this portfolio based on the latest available valuations is 69%, but when indexed for house price inflation using the Halifax index, the current weighted average LTV becomes [45]%. Although realised loss data from the prior securitisations suggest that some of the affected properties have not appreciated in line with the market, or the indexed valuations may be inaccurate, the rolling average loss severity rate has shown steady improvement over the last few years.

Moreover, about [19]% of the loans in the provisional pool presently have their interest paid by the Department of Work and Pensions ("DWP"), formerly called the Department of Social Security (DSS) due to the unemployment of the borrower, and may therefore, be regarded as essentially I/O loans, [98]% of which are due to mature within the next 15 years. The DWP will pay interest due on the portion of a mortgage representing the house price of up to a balance of £100,000, for as long as interest is due and payable on the loan. The DWP subsidy does not cover scheduled principal repayment. Also, rather than using the contractual interest rate on the loans in question, the DWP interest payments use the "Standard ISMA rate," calculated using the Building Societies basic rate of interest for mortgages, with adjustments for movements in the basic rate. The Standard ISMA rate is currently 5.34%. Borrowers may also make contributions in addition to these DWP payments.

Moody's has some concerns about these loans in particular, because borrowers who require DWP assistance to pay for their housing are less likely than others to have the financial ability to continue necessary maintenance, where required. Therefore, it is possible that these properties, especially ones that have had several years of DWP involvement are in worse condition than the rest of the pool. In addition, the DWP loans have had higher arrears than the general pool. [37]% of the DWP loans are 12 or more payments past due. Higher arrears multiples might also translate into higher loss severity due to among other things, accrual of interest.

Although we might expect the DWP properties to be more marginal and thus to have a lower average value, the average loan amount for the DWP properties is just under £[41,000], while the average for the pool is £[38,439]. This fact may provide some comfort that these properties are not located disproportionately in low-value areas. Moreover, loss severity for the DWP loans has not been materially different from the rest of the portfolio. Both the weighted average sales price as a function of loan balance and the weighted average loss severity for the DWP loans is similar to that of other repossessed properties in the pool, suggesting that the DWP properties are similarly saleable.

A positive factor of the portfolio, is the high “payment rate,” which is the ratio of all amounts received on the pool in a month to what was contractually due in that month. Over the last three years, the payment rate of the portfolio has generally been above 100%, and at times as high as 105%. Because these borrowers are charged interest on arrears, even though many of them may have been making their contractual payment for years, they may still remain seriously delinquent. Further, the arrears multiple is based on the contractual payment due. Since interest rates have fallen significantly since origination of these loans, current contractual payments have likewise fallen. Thus, interest on arrears, combined with an arrears multiple based on lower current contractual payments due, may overstate the number of payments actually missed by a borrower.

In addition, the redemption rate of the pool has been fairly high, running at about [25]%, and generally proportionally across the arrears buckets. The DWP loans have also been redeeming albeit, at a somewhat slower speed. The lower CPR of the DWP loans does not come as a surprise, since borrowers who have their mortgage interest paid by an outside source have less incentive to refinance. The prepayment rate and its proportionality across the pool provide comfort, since it suggests that many of these borrowers have the ability to refinance their debt or sell their property. It may indicate that the overall quality of the pool is remaining stable, rather than having all the “good borrowers” refinance, leaving only borrowers with run down homes and negative equity positions.

Credit Enhancement

Excess Spread

The first layer of protection is excess spread in the transaction, which is the difference between (1) the income received from the mortgages and other investments, and (2) the coupon on the Notes plus various ongoing costs.

The transaction benefits from high excess spread. As of the Provisional Pool Date, the loans provided a gross margin in excess of [4.5]%, and the Mortgage Administrator covenants that the average charging rate will be at least LIBOR plus [4.5]%.

The loans are subject to a Minimum Mortgage Rate (“MMR”), which provides some guarantee as to the amount of excess spread that will be available; under the MMR, the Administrator must set the rate on the variable rate mortgages in the portfolio so as to ensure that the weighted average margin of the portfolio taken as a whole plus any other income received by the SPV is at least [4.5]% in excess of the LIBOR rate applicable to the Notes, although there is an option for the Issuer to borrow further amounts under the subordinated loan made by Paragon Finance PLC (PFPLC) so as to cover the shortfall that would result absent the MMR. Assuming the MMR for each mortgage is satisfied, (and fixed and discount periods no longer apply), the spread initially amounts to approximately [3.75]% pa after payment of Note interest and servicing costs.

The credit enhancement value of excess spread also depends on the timing of principal losses. Excess spread is available on a “use it or lose it” basis and so, if not used to top up the First Loss Fund or to reduce the Principal Deficiencies Ledger, it is paid back to PFPLC via the Subordinated Loan and other profit extraction mechanisms; which might occur before losses on the portfolio have shown through. The value of the Excess Spread was assessed by Moody’s under a variety of adverse conditions.

Pre-Closing Arrears

Another beneficial aspect of this transaction is the treatment of the payments due on the Arrears Mortgages representing amounts which have become due, but remain unpaid (Purchased Pre-Closing Accruals and Arrears). These amounts, as of the Provisional Pool Date, had a value of £[34.3] million. Purchased Pre-Closing Accruals and Arrears will be sold to the Issuer via the Subordinated Loan, and will provide additional credit support for the Notes. Any amounts collected from borrowers, including amounts representing Purchased Pre-Closing Accruals and Arrears (PCAs) will be applied to current interest, principal and finally to PCAs. Therefore, as the PCAs are received they will be used to cover senior liabilities, including note interest, then to replenish the First Loss Fund and then to cover any balances on the PDL, which is a different treatment from the prior securitisations. Since historic loss data arises from a treatment that clears the PCAs before redeeming mortgage principal, it overstates realised loss of repossessed properties by about [15]% in comparison with what would have resulted from the allocation used in this securitisation.

First Loss Fund

The next layer of protection for investors in the Notes is the First Loss Fund (equal to [1.9]% of the principal balance of the notes at closing). This fund is available to pay interest and senior cost obligations of the Issuer should there be insufficient spread on the assets to meet these obligations. The fund is topped up, in priority to the elimination of any principal deficiencies on the Principal Deficiency Ledger until all the Class A Notes are redeemed, using excess spread. The required balance of the First Loss Fund may amortise in line with the mortgage collateral so that it equals [3.8]% of the current principal balance of the outstanding mortgage pool, but only if (a) there is no debit balance on the PDL, and (b) less than [6]% of the pool by principal balance is more than 3 months in arrears. Moody's believes that these tests are very unlikely to be met.

Principal Subordination

The third layer of protection for investors is the subordination of the principal balance of the Class B Notes and Class C Notes to the A Notes. The Class A Notes redeem sequentially but begin to redeem pro rata with the Class B Notes and Class C Notes after 5 years but only if:

- the ratio of Class B Notes and Class C Notes to Class C Notes, Class B Notes and Class A Notes is at least 2.5 times the ratio calculated as at closing;
- there is no debit balance on the PDL;
- less than 20% of the pool by principal balance is 3 or more months in arrears; and
- pro rata redemption would not cause the sum of the principal balance of the Class B Notes and the Class C Notes to fall below an amount equalling 4.7% of the principal balance of the Notes at closing.

Interest/Interest Subordination

Further protection is provided via the subordination of interest due under the Notes; on each interest payment date, all income (after paying certain senior costs and expenses) is allocated first to pay Class A interest, then Class B interest, and then Class C interest.

Interest/Principal Subordination

In addition, in certain circumstances, Class B and Class C Note interest is subordinated to payment of principal under the Class A Notes. The Class C Note subordination occurs where outstanding principal losses exceeds the then Class C Notes and the Class B Note subordination will occur where outstanding principal losses exceed the then Class B and Class C Notes; in these circumstances, payment of Class C interest or Class B and Class C interest is subordinated to the topping-up of the First Loss Fund and to the reduction of the PDL. Therefore, upon subordination, Class B and Class C interest is effectively subordinate to A Note interest and principal, but not Class B and Class C principal.

Liquidity

Several levels of protection are available to investors to counter the effect of temporary shortfall in cashflows from the loans caused by delinquencies in the pool or any interruption in the servicing functions or cash collection functions. The Issuer does not have the benefit of a separate liquidity facility. Moody's believes that the First Loss Fund, which is topped-up from Excess Spread before Excess Spread is applied in reduction of the PDL, provides adequate liquidity support for the transaction.

Principal Paying Interest

The Issuer has the ability to use principal receipts under the mortgage loans to meet its senior expenses obligations and interest due under the Class A, B and C Notes. This provides substantial protection for investors in the Class A Notes against a gradual deterioration in the arrears performance of the portfolio.

First Loss Fund

As described above, the First Loss Fund is available to cover interest shortfalls under the Notes. The value of the liquidity support provided by the First Loss Fund is increased by the fact that the First Loss Fund is topped-up prior to payments being made to investors in respect of any PDL balances that may arise within the structure, and replenishment of the First Loss Fund ranks ahead of the reduction of any outstanding Principal Deficiency Ledger. The availability of the First Loss Fund to pay Class B and Class C Note interest is, however, limited in the manner described in "Interest/Principal Subordination" above.

Collections and Bank Accounts

The vast majority of payments under the Loans are collected by Paragon Finance (PLC) and PML under the direct debit scheme. All receipts in respect of the loans will be paid directly into the PFPLC or PML collection account, and will be held on trust for the Issuer pending transfer into the transaction account of the Issuer. The transaction account is a dedicated account of the Issuer held with National Westminster Bank Plc (**Aa1**, **Prime-1**). Cash in the transaction accounts must be invested by PFPLC as administrator in eligible investments which meet certain criteria, including a requirement that the investments are rated either Aaa or Prime-1 and mature prior to the next interest payment date

Interest Rate Risk

The mortgage loans either charge interest at a variable rate set by PFPLC (83% of the Provisional Pool), or by reference to 3-month LIBOR (16% of the Provisional Pool), or by reference to the rate set by the Secretary of State in relation to the Local Authority mortgages (1% of the Provisional Pool) whereas payments under the Notes are to be calculated by reference to 3-m sterling LIBOR. The MMR mechanism described above partially mitigates this risk because it ensures that weighted average rate under the mortgage loans exceeds LIBOR under the Notes plus the relevant margins. However, as mentioned above, the protection afforded by this mechanism is susceptible to a number of factors such as relative prepayment speeds of the various loan types in the portfolio.

Although there are no fixed or capped rate loans in the Provisional Pool, the Issuer is obliged to enter into suitable arrangements with respect to the hedging of fixed rate or capped rate loans created as a result of conversion (see below).

Conversion

The Servicer may alter the payment method between repayment and interest only and may also convert fixed rate into floating rate mortgages and vice versa. However, there are pre-conditions to any conversion between interest charging methods; for example, if required to maintain the ratings on the Notes, appropriate hedging must be in place.

Further Advances

The Issuer may use principal receipts from the mortgage portfolio to make further advances to the mortgage borrowers, but the cumulative amount of further advances is subject to a cap of £7 million, and is also conditional on the Issuer's continued compliance with various contractual restrictions contained in the transaction documents. In addition, if Moody's indicates to the Issuer that the making of additional Further Advances will result in a downgrade of the Notes, then, unless the First Loss Fund is increased to a level such that Moody's confirms the ratings of the Notes will not be downgraded if additional Further Advances were to be made, the Issuer will no longer be entitled to make Further Advances. Arrears Mortgages are ineligible for Further Advances.

Servicing

PFPLC is the transaction's mortgage administrator, with an experienced team of collection staff specifically for the servicing of this portfolio. PFPLC views the repossession of properties as a last resort, and may decide to enter into short-term arrangements if a loan remains commercially viable despite being in arrears. However, in such cases PFPLC may continue to obtain an Order of Possession which it will suspend so long as the arrangement with the borrower remains satisfactory. Moody's believes that Paragon has a well-developed servicing business with a track record of successful collections and arrears management in the United Kingdom. In addition, Global Home Loans Limited is the servicer of last resort.

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