66 ASSET-BACKED SECURITY (ABS) INSTRUMENT & MARKET FEATURES

1. Which of the following statements about credit enhancement structures in asset-backed security (ABS) securitizations is most accurate?
   (A) The level of excess spread is independent of the coupon rate in the ABS.
   (B) Higher levels of collateral are beneficial for generating excess spread.
   (C) Overcollateralization is necessary to earn excess spread in the ABS.

2. Under a waterfall structure:
   (A) tranches do not receive a pro rata share of principal and interest payments.
   (B) principal repayments are first directed to the subordinated tranches.
   (C) senior tranches carry more prepayment risk than junior tranches.

3. An asset-backed security with a senior/subordinated structure is said to have:
   (A) credit tranching.
   (B) prepayment tranching.
   (C) time tranching.

4. A covered bond that may postpone the originally scheduled maturity date by as much as a year to delay default is:
   (A) a soft-bullet covered bond.
   (B) a conditional pass-through covered bond.
   (C) a hard-bullet covered bond.

5. Which of the following classes of asset-backed securities typically includes a lockout period?
   (A) Auto loan ABS.
   (B) Credit card ABS.
   (C) Non-agency residential MBS.

6. Consider the asset-backed security (ABS) structure in the table below, including the various tranches and collateral. If the market reference rate (MRR) is 3%, determine whether credit risk is fully mitigated by this structure.

Tranche Name	Face Value ($ mil)	Interest Rate
Tranche A senior notes	$120	MRR + 0.25%
Tranche B subordinated notes	$20	MRR + 1.25%
Tranche C equity tranche	$10	–
Collateral	$150	MRR + 0.75%

(A) Yes, because the excess spread is zero.
(B) Yes, because the excess spread is positive.
(C) No, because the excess spread is negative.

7. A company originating an asset-backed security (ABS) has built up significant reserves within the ABS structure in order to absorb credit losses in collateral. This credit enhancement type is best described as:
(A) excess spread.
(B) credit tranching.
(C) overcollateralization.

8. A covered bond that is in default if the issuer fails to make a scheduled payment is:
(A) a soft-bullet covered bond.
(B) a hard-bullet covered bond.
(C) a conditional pass-through covered bond.

9. In contrast with most asset-backed securities (ABS), a collateralized debt obligation (CDO):
(A) employs a collateral manager.
(B) has senior and subordinate tranches.
(C) is issued through a special purpose vehicle.

10. Based on the table below illustrating an asset-backed security (ABS) structure, what is the value of the equity tranche (in $ millions)?

Tranche Name	Face Value ($ mil)	Interest Rate
Tranche A senior notes	$120	MRR + 0.25%
Tranche B subordinated notes	$20	MRR + 1.25%
Tranche C equity tranche	$10	Variable
Total	$150	

(A) 30.
(B) 0.
(C) 10.

11. Compared to otherwise equivalent asset-backed securities, covered bonds offer:
    (A) lower credit quality.
    (B) recourse to the issuing firm.
    (C) higher yields.

12. A synthetic collateralized debt obligation (CDO) is backed by a pool of:
    (A) credit default swaps.
    (B) leveraged bank loans.
    (C) other CDOs.

13. A collateralized debt obligation (CDO) in which the collateral is a pool of residential mortgage-backed securities is most accurately described as a:
    (A) collateralized loan obligation (CLO).
    (B) structured finance CDO.
    (C) synthetic CDO.

14 With respect to auto-loan backed ABS:
    (A) all of them have some sort of credit enhancement.
    (B) some of them have some sort of credit enhancement.
    (C) the underlying loans are collateralized so no credit enhancement is necessar