67 MORTGAGE-BACKED SECURITY (MBS) INSTRUMENT & MARKET FEATURES

1. A mortgage-backed security has a pass-through rate of 4.3%. The average interest rate on its underlying pool of mortgages is 4.5%. The difference between these rates is most *likely* due to:
   (A) faster-than-expected prepayments.
   (B) issuance and servicing costs.
   (C) slower-than-expected prepayments.

2. When evaluating the loans backing a commercial mortgage-backed security based on credit ratios, which of the following most likely indicate better credit quality?
   (A) Lower debt-service coverage ratios and higher loan-to-value ratios.
   (B) Higher debt-service coverage ratios and higher loan-to-value ratios.
   (C) Higher debt-service coverage ratios and lower loan-to-value ratios.

3. In a commercial mortgage-backed security (CMBS), which of the following is an example of CMBS-level call protection?
   (A) Prepayment lockout.
   (B) Residual tranche.
   (C) Yield maintenance charges.

4. Which of the following statements concerning the support tranche in a planned amortization class (PAC) CMO backed by agency RMBS is least accurate?
   (A) The support tranches are exposed to high levels of credit risk.
   (B) The purpose of a support tranche is to provide prepayment protection for one or more PAC tranches.
   (C) If prepayments are too low to maintain the scheduled PAC payments, the shortfall is provided by the support tranche.

5. Strategic default by a mortgage borrower is most likely if the loan is:
   (A) non-amortizing.
   (B) non-conforming.
   (C) non-recourse.

6. An agency RMBS pool with a prepayment speed of 50 PSA will have a weighted average life that is:
   (A) equal to its weighted average maturity.
   (B) greater than its weighted average maturity.
   (C) less than its weighted average maturity.

7. A mortgage is most attractive to a lender if the loan:
   (A) has a prepayment penalty.
   (B) is convertible from fixed-rate to adjustable-rate.
   (C) is non-recourse.

8. Extension in an agency residential mortgage-backed security is most likely to result from:
   (A) exhaustion of a support tranche.
   (B) a decrease in interest rates.
   (C) slower-than-expected prepayments.

9. A sequential-pay CMO has two tranches. Principal is paid to Tranche S until it is paid off, after which principal is paid to Tranche R. Compared to Tranche R, Tranche S has:
   (A) less contraction risk and more extension risk.
   (B) more contraction risk and less extension risk.
   (C) more contraction risk and more extension risk.

10. The type mortgage-backed security that is most likely to offer significant call protection is:
   (A) a commercial mortgage-backed security.
   (B) an agency residential mortgage-backed security.
   (C) a non-agency residential mortgage-backed security.

11. The pool of loans backing a commercial mortgage-backed security consists of:
   (A) both recourse and nonrecourse loans.
   (B) nonrecourse loans only.
   (C) recourse loans only.

12. A renegotiable mortgage has a fixed interest rate that:
   (A) changes to a different fixed rate during its life.
   (B) changes to a variable rate during its life.
   (C) the borrower may change to a variable rate.

13. An annualized measure of the prepayments experienced by a pool of mortgages is its:
    (A) conditional prepayment rate.
    (B) PSA prepayment benchmark.
    (C) single monthly mortality rate.

14. The primary motivation for investing in the support tranche of a planned amortization class CMO, compared to investing in another tranche, is that the support tranche offers:
    (A) a higher interest rate.
    (B) more protection against contraction risk.
    (C) more protection against extension risk.

15. An investor in mortgage-backed securities who is concerned about extension risk but willing to accept contraction risk should most appropriately invest in:
    (A) agency residential mortgage-backed securities.
    (B) sequential-pay collateralized mortgage obligations.
    (C) planned amortization class collateralized mortgage obligations