Question #1 of 6

Question ID: 1574405

Total cash flows to investors in an ABS issue are:

A) equal to the total interest and principal payments from the underlying asset pool if only one class of ABS has been issued from the trust.

B) equal to the total interest and principal payments from the underlying asset pool.

C) less than the total interest and principal payments from the underlying asset pool.

Explanation

Cash flows from the underlying asset pool are used to pay fees to the servicer as well as payments to the ABS investors. Thus payments to investors are less than the total cash flows from the pool of assets.

(Module 65.1, LOS 65.b)

Question #2 of 6

Question ID: 1574402

Securitization *least likely* benefits the financial system by:

A) increasing liquidity for mortgages and other loans.

B) increasing the amount banks are able to lend.

C) removing liabilities from bank balance sheets.

Explanation

By enabling banks to raise cash by selling their existing loans and mortgages (which are balance sheet assets for banks), securitization increases the amount banks are able to lend.

(Module 65.1, LOS 65.a)

Question #3 of 6

Question ID: 1574403

One of the primary benefits of securitization is that it:

A) improves the collectability of the loans that are securitized.

B) improves the legal claims of the security holders to the loans that are securitized.

C) removes problem assets from the issuing firm's balance sheet.

Explanation

Securitization reduces the cost of funding the assets. One way that is accomplished is through the transfer of the underlying financial assets to a special purpose entity so that securities holders have clear legal claim to them, something they may not have if they were to invest only in the securities of the securitizer, such as a bank. Securitization does not have improved collectability as a primary benefit. Problem loans are not good candidates for securitization because institutional investors require a minimum credit quality and even well performing loans can require internal or external credit enhancement for the securitized assets.

(Module 65.1, LOS 65.a)

Question #4 of 6

Question ID: 1574404

Which of the following is *least likely* a benefit of securitization?

A) Removing liabilities from the balance sheet.

B) Reducing funding costs.

C) Increasing the liquidity of balance sheet assets.

Explanation

Financial assets are securitized, not liabilities.

(Module 65.1, LOS 65.a)

Question #5 of 6

Question ID: 1574406

The special purpose entity (SPE) in a securitization is:

A) a subsidiary of the seller.

B) an entity independent of the seller.

C) a joint venture partner of the seller.

Explanation

The SPE in a securitization must be a legal entity independent of the seller so that the seller's creditors do not have a claim against the securitized assets.

(Module 65.1, LOS 65.b)

Question #6 of 6

Question ID: 1574407

Asset-backed securities (ABS) may have a higher credit rating than the seller's corporate bonds because:

A) ABS are investment grade while corporate bonds may be speculative grade.

B) the seller's ABS are senior to its corporate bonds.

C) they are issued by a special purpose entity.

Explanation

The SPE in a securitization is bankruptcy-remote from the seller, which means the seller's creditors do not have a claim against the pool of assets underlying an ABS. As a result, the ABS may have a higher credit rating than the seller's corporate bonds.

(Module 65.1, LOS 65.b)