

- AAA-rated senior bonds, 173
- Accretion, 131
- Accretion-directed (AD) bonds, 132
- Accretion-directed (AD) cash flows, generation, 131e
- Accretion-directed (AD) tranches, 130–134
- Accretion direction, 106
- Accrual bond class, 133e
- Adjustable rate agency pooling, 29–30
- Adjustable-rate mortgage (ARM), 8–9
 - base servicing, 29–30
 - fixed rate loan, refinancing, 78
 - payments, 9
 - products, trading, 37
 - unpopularity, 88
- Adverse selection, 96, 172
- Agency ARM market, pooling practices, 29–30
- Agency ARM pools, 32
- Agency-backed MBS, 245–246
- Agency CMOs
 - deal, creation, 25–26
 - key rate durations, 273e
 - total returns, 270e–272e
- Agency inverse floater, yield-to-index matrix, 261e
- Agency MBS
 - analysis, 281
 - creation, 27–30
- Agency PAC, yield-to-price table, 252e
- Agency PAC CMO
 - average lives/modified durations, 257e
 - yield-to-price table, 256e
- Agency pass-through, cash flow allocation, 28e
- Agency pooling, private-label deal execution (contrast), 173–176
- Agency pools, cash flow generation, 44–45
- Agency support CMO, yield-to-price table, 251e
- Alternative-A loans (alt-A loans), 5, 7–8
 - securitization, 174
- Amortizations
 - ARM loans, 15–16
 - exclusion, 52
 - schemes, alternatives, 80
 - types, 9–10
- Annualized total return, calculation, 227
- Anti-TTIB, initial coupon rate, 160
- Asset-backed securities (ABSs)
 - deal
 - residual, 196
 - structural components, 201–202
 - structuring, focus, 207–208
- Asset-backed securities (ABSs) structures
 - basis risk, 197–198
 - excess spread, 205e
 - fundamentals, 194–199
- Asset-backed securities (ABSs) transactions, structuring decisions, 202
- Available credit support, evaluation, 294–296
- Available funds
 - cap, 197
 - instantaneous rate shift scenarios, example, 198e
- Back ratio, 7
- Bank bonds, 136
 - average life profile, 139e
 - creation, options, 137e–138e
- Barbell bonds, 126
- Base-case assumption, 249
- Base-case average life, 263
- Base-case prepayment assumption, usage, 62
- Base-case prepayment speed, usage, 262
- Baseline prepayments, 306
- Base servicing, 27–28
- Basis risk, impact, 197–198
- Beacon model (Equifax), 6
- Bear flattener scenario, 272
- Bear steepener, 272
- Binomial model, usage, 214–215
- Bloomberg medians, usage, 248
- Bond equivalent effective margin (BEEM), usage, 260–261
- Bond equivalent yield (BEY), 212
- Bonds
 - average, life profile, 133
 - base-case average, 139
 - negative convexity, 240
 - price compression, 240–241
 - price-yield function, 232
 - principal payments, timing, 248–249
 - principal windows, 249
 - stress, 255
 - structuring, 125
 - valuation, alternatives, 276–277
- Borrowers
 - classification, 306
 - credit, change, 90
 - equity accumulation, patterns, 15
 - inefficiencies, 85–87
 - refinancing decisions (complication), mortgage lending (impact), 82
 - servicer interface, 4
- Breakeven calculation, 38
- Bullet agency debenture
 - parallel-shift scenarios, 270e
 - total returns, difference, 271e, 272e
- Bull steepener, 272
- Burnout, 310–311
- Buybacks, 190–191
- Call risk, 170
- Cap corridors, usage, 186
- Cash benchmark, 269
- Cash flow allocation, 200
 - mechanism, 109
 - turboing, impact, 196e
- Cash flows
 - average lives, 180e
 - barbelling, 139

- Cash flows (Cont.)
 breaks, 249
 calculation, 51, 218
 components, 57
 duration, 234
 generation, 44–45, 236
 present value, determination, 219
 priority, 30–31
 problems, mitigation, 93–94
 projection, 218, 290–291
 schematic, 171e
 structure, implications, 179
 structuring, 44–46
 logic, 102–103
 uncertainty, 116
 volatility, support bond
 absorption, 208
 waterfall, schematic representation, 197e
 yield, 213
- Cash-out activity, 78
 drivers, 83
 limitation, 80
- Cash-out refinancings, 6, 19, 78
 importance, 89–90
 viewpoint, 82–83
- Cash window, 29
- Catalyst, 178
- Cleanup calls, 168
- Collateral, 25–26
 aggregate note rate, 104–105
 average life, 116e, 121e
 balances, 173e
 cash flows, 215
 pricing speed, usage, 111
 principal payment, 115
 stripping, floater-inverse IO
 combination (usage), 154e
 tranche losses, differentiation,
 291
 usage, 101
- Collateralized mortgage obligations (CMOs), 25–26
 CMO-and-cash portfolios, 274
 deal, 109
 evaluation, 245
 sequential pay structure, VADM
 tranche (inclusion), 135e
 structure, examples, 121e, 126e
 structuring, fundamentals,
 106–107
- Collateralized mortgage obligations (CMOs) tranches, 245
 passthroughs, comparison, 269
 sensitivity, 225
- Collateral pool, 142
- Collateral pool stripping
 IO tranche, creation, 144e
 trust IO/PO, creation/recombination, 145e
- Combined LTV (CLTV), 6
- Committed loan, 35
- Companion bonds, 119
- Complete prepayment, 50
- Conditional prepayment rate (CPR), 51
 calculations, 55–56
 concept, usage, 65
 example, 258e
 usage, 52–53
 vector, 91
 PSA, contrast, 92e
- Conduits, 103
- Conforming balance
 execution, comparison, 176e
 limit, 11
- Conforming-balance collateral, 168
- Constant Maturity Treatment (CMT), 8
- Consumer lending rates (generation), MBS markets (role), 40–44
- Consumer mortgage market
 overview, 3
- Conventional loans, 10–11
 guarantees, absence, 11
- Convexity, 231, 238–241
 measurement/calculation,
 238–239
 price adjustment, 239–240
 risk measure, 239e
 spread widening, contrast, 241e
- Corporate bonds, call risk, 17
- Corporate credit theory, borrower default expectation, 94
- Corridor-cap floaters, 156,
 185–188
 behavior, 186
- Corridor floaters, effective cap,
 187e
- Coupons
 adjustment, 106
 boosting, 143–147
 creation, 34e
 leverage (multiple), 149
 mortgages, spread, 232
 reset formula, 276
 stripping, 143–147
 inverse IOs, usage, 152–156
- Coverage ratios
 estimation, 295e
 measurement uses, 296
 usage, 303
- Credit
 bucket, default percentages
 (arbitrariness), 296
 classification, 5–7
 exposure, analysis, 20
 guarantees, 10–11
 inputs, interaction, 292–294
 IOs, 283
 evaluation, 296
 OAS, 300
 risk, 20–22
 scores, 6
 stack, 281
 support, 104, 203–204
 evaluation, 294–296
 tranching, 106
- Credit enhancement, 24–25
 cost, 174
 percentage, 195
 presence, 167–168
- Credit performance
 evolution, 284–290
 factors, 93–94
- Credit-related losses, 31
- Credit-related prepayments, 50
- Credit-related prepayments, calculation/report, 95
- Cross-collateralization, 207
- Crossover point, occurrence,
 117–118
- C tranches, 204
- Cumulative default rate (CDR),
 69, 282
 curve, 72
 projections, 292
 unchanged transition matrix,
 usage, 289e
 usage, 293e
 disadvantages, 71
- Cumulative home price percentage, change, 83e
- Current LTV (CuLTV), 6, 21
- Curtailments, 19, 50
- CUSIP number, usage, 246
- Davidson, Andrew, 307
- Deal-specific factors, 283–284
- Declining balance schedule,
 creation, 198
- Decrement (DEC) tables, 190
- Deep MI, 206
 policy, incremental protection,
 206–207
- Default risk, 20–22
- Defaults, 20–21
 analysis, 50–51
 assumptions, 75
 dollar amount, voluntary
 prepayment speed (relationship), 70–71
 frequency, factors, 93–94
 involuntary prepayments,
 relationship, 92–97
 measurement, 49, 67–68
 measures, 68–72
 monthly dollar amounts, 71e

- prepayments, interactions, 96–97
- terminology, 66–75
- Delinquencies, 20
 - importance, 67
 - measures, 68
 - terminology, 66–75
- Department of Housing of Urban Development (HUD), 10–11
- Derivative contracts, 203–204
- Digital PO, example, 160e
- Digital TTIB, 159–160, 160e
- Discount loan groups, 32
- Discount margin (DM), 260–261
- Discount-premium split, variation (creation), 154
- Discount tranche size, 147e
- Dodd-Frank Wall Street Reform and Consumer Protection Act, 202
- Dollar duration, 233
- Dollar roll, 39e
 - market, financing, 37–40
 - transaction, 37–38
 - valuation, 37–38
- Dollar value of a basis point (DVBP), 233
- Doubling test, satisfaction, 172
- Drop (price difference), 38
- Due on sale clause, 12
- Due-on-sale provisions, 51–52
- Duration, 231–238
 - calculation, 233–234
 - defining, 232–233
 - estimate, 236
 - interpretation, 232
 - profile, unevenness, 273
 - risk measure, example, 232e
- Dynamic prepayment scenarios, 254–260
- Dynamic prepayment speeds, 254
- Early-pay defaults (EPDs), 21
- Earnings per share (EPS), volatility, 119
- Effective bands, 123
 - example, 128e
 - structuring bands, comparison, 128
- Effective cap, 186, 187
- Effective duration, 234–235
- Eighth-coupon pools, origination, 27
- Emperica model (Transunion), 6
- Empirical duration, 236–237
- Employee Retirement Income Security Act (ERISA), 176, 190
- Equifax, Beacon model, 6
- Equity, underwater status, 90
- Estimated credit performance, measurement, 21
- Estimation error, impact, 19
- Excess servicing, 28
 - absence, 30
 - structuring, example, 162e
- Excess servicing IOs, 160–166
 - tranches, structuring (schematic representation), 164e
- Excess spread, 104–105, 148
 - difference, 194
 - example, 195e
 - structures, 106
- Exchangeable tranches, 165–166
 - designation, 188
- Experian, Fair Isaac Risk Model, 6
- External credit enhancement, usage, 206
- Fair Isaac Company (FICO) scores, 6, 7–8
- Fair Isaac Risk Model (Experian), 6
- Fallout, 35
- Federal Financial Institutions Examination Council (FFIEC), 126
 - rules, 134, 136
- Federal Home Loan Mortgage Corporation (FHLMC), 10–11
- Price Index, reports (2010), 83
- refinancings, quarterly percentage, 82e
- Survey Rate, 86e, 88e
- Federal Housing Administration (FHA)
 - experience, 51
 - housing credit support, 10
- Federal Housing Finance Board, average home price publication, 11
- Federal National Mortgage Association (FNMA), 10–11
 - loan limits, 11
 - MBS prices, 325e, 326e
 - prices, 325e
- 50 PSA, graphical depiction, 55e
- Financial engineers, 309
- First lien, 4–5
- First-loss tranche, loss absorption, 30–31
- First-pay defaults (FPDs), 21
- 5/1 hybrid ARM, interest-only period, 10
- Fixed income valuation modeling, 214
- Fixed maturity bond, MBS (contrast/performance profile), 19e
- Fixed rate agency pooling, 27–29
- Fixed rate conventional loans, prepayment S-curves (usage), 79e
- Fixed rate interest, allocation, 149e, 185e
- Fixed rate interest only loan, interest-only hybrid ARM (comparison), 16
- Fixed rate IO tranches, 165
- Fixed rate loan, 14e
- Fixed rate mortgages, 8
- Fixed-to-ARM refinancings, popularity (variation), 88–89
- Fixed tranches, creation, 165
- Floater-inverse combinations, mechanics, 152e
- Floater-inverse floater combinations, 147–156, 277
 - generation, 150
 - tranche restructuring, 153e
- Floater-inverse floater-TTIB combination, mechanics, 157e
- Floater-inverse IO combination creation, 154, 155
 - structuring, 185–186
- Floaters, 106, 141
 - coupon, example, 151
 - effective cap, 278
 - inverse floaters, interest payments (annual division), 153e
 - reset, 188
 - size, impact, 156
 - structuring, fundamentals, 148
- Floating rate, fixed rate interest (allocation), 185e
- Floating rate bonds
 - structures, 147–148
 - structuring, 185–186
- Floating rate tranche, allocation, 149e
- Foreclosure, 283–284
- Forward LIBOR, 205e
 - increase, 204
- Forward market, 36
- Four-tranche sequential-pay structure, example, 112e, 133e
- Front months, 37
- Front ratio, 7
- Fully amortization loans, 9
- Funds, implied cost (drop expansion), 38
- Governing documents, 189–191
- Government loans, 10
- Government National Mortgage Association (GNMA), 10–11
- Government-sponsored enterprises (GSEs), 10–11
 - Selling/Service defaults, 191 shelf, 167
- Gross interest, example, 195e
- Guaranty fees (g-fees), 24–25, 27

- Guaranty fees (Cont.)
 bought down, absence, 30
 capitalization/bought down, 29
- Hedge ratios, 237–238
- Hershovitz, Michael, 307
- High-LTV loans, 93
- Historical credit performance, measurement, 21
- Ho, Thomas, 242
- Home equity loans (HELs), 50
 usage, 65–66
- Home equity prepayment (HEP), 65–66, 66e
- Homeowner equity/credit, changes, 89–90
- Home price appreciation (HPA), 300, 302
- Home prices, change, 90
- Horizon price, calculation, 227
- Hybrid ARMs, 9
 interest-only feature, 9–10
 note rates, example, 16
 prepayment speeds, 255
 transaction, examination, 291
- Implied prepayment distribution, 324, 325e
- Implied turnover rate, 81e
- Imputed coupon, 307
- Income ratios, 7
- Incremental returns, noncallable debenture (contrast), 269, 271
- Initial cap, 9
- Instantaneous rate shift scenarios, 198e
- Insurance wrap, 206
 mortgage insurance, contrast, 206
- Interest
 bonds (shift), leverage (impact), 181
 divisions, 106
 flow chart, 201e
 payments, annual division, 153e
 shortfalls, 284
- Interest cash flow
 conversion, 194
 generation, 175
- Interest-only (IO) creation (IOette), 143
- Interest-only (IO) face value, 144
- Interest-only (IO) hybrid ARM, fixed rate interest only loan (comparison), 16
- Interest-only (IO) loan, balance, 15
- Interest-only (IO) notional face value, 143
- Interest-only--principal-only (IO-PO) deals, creation, 161
- Interest-only--principal-only (IO-PO) trust, 142
- Interest-only (IO) product, 9
- Interest-only (IO) security, 26
- Interest-only (IO) stripping, 106
- Interest-only (IO) tranches, 141
 creation, 144e
 notional sizing, 145
- Interest rate paths
 cash flows, 218, 219
 number, 224–225
 present values, distribution, 220
 set, shift, 236
- Interest rates, 8–9
 assumptions, 300, 302
 note rates, 8, 13
 random paths, generation, 217–218
 up-front fees, combinations, 85
- Internal credit enhancement, requirements, 169
- Internal rate of return (IRR), 290–291
- In-the-money loans, 79
 responsiveness, absence, 80
- In-the-moneyness, calculation (distortion), 80
- Inverse coupons, rate, 151
- Inverse face value, 159
- Inverse floaters, 106
 analysis, 261
 calculation, 275
 evaluation, 274–279
 initial coupon, 159
 leverage, 159
 multiple, calculation, 151
 valuation, 275
- Inverse interest, example, 151
- Inverse IO (IO), 148, 267
 principal component, absence, 154
 purchase, yield curve (impact), 155
 tranches, fixed rate interest (allocation), 185e
 usage, 152–156
- Inverse leverage, 159
- Involuntary prepayments, 50, 94–96
 defaults, relationship, 92–97
 report, 95
 speeds, projection generation (iterative calculation usage), 288
- Issues structuring, 203–208
- Judicial states, 283
- Jumbo loans, 12
- Junior bonds, principal value, 282–283
- Junior loans, 5
- Junior securities, evaluation, 296
- Kalotay-Yang-Fabozzi (KYF)
 MBS valuation approach, 305–306, 308
- Kalotay-Yang-Fabozzi (KYF)
 option-based mortgage valuation model, 311
- Key rate durations, 242
 example, 273e
- Laggards, 309
 distribution, 321e
 effect, 320
 examination, 319–322
 KYF definition, 310
 spacing changes, fair MBS coupon, 324e
 spread, distribution, 320–322
 List cash flow, 111
- Leaper-laggard distribution, 317
- Leaper-laggard spreads, range, 319
- Leapers, 309
 effect, 320
 examination, 319–322
 KYF definition, 310
- Legacy assets, 102
- Legacy bonds, evaluation, 303
- Lending rate, points (calculation), 43e
- Lesser-of-schedule, 198
- Level risk, 241–242
- Leveraged sequentials, 179
 structures, average life (percentage increase), 180e
- Lien status, 4–5
- Life cap, 9
- Loans
 aggregation, 29
 amortization schedules, reduction, 13–14
 balances, 11–12
 breakdown/grouping, 33
 collateral, impact, 188
 collateralization, 90
 current status, classification, 68
 default, 288
 delinquency, 67–68
 classifications (OTS method), 68
 due-on-sale provisions, 51–52
 interest payment, minimum payment (sufficiency), 17
 LTV, inverse, 83
 recasting, 9

- season, 90
- securitization, historical shifts, 44
- stratification, 34e
- termination, 285
- timeline, 35e
- Loans-to-bonds business model, 23
- Loan-to-value (LTV) ratios, 6
 - comparison, 206
- Loan-to-value (LTV) threshold, 284
- Localized PACs, 181–185
 - payment schedules, 184e
- Locked loan, 35
- Locked-out tranches, 116
 - principal/cash flow timing, 131
- Lockout, 177
 - period, 9
 - schedule, 207–208
- London Interbank Offered Rate (LIBOR), 8
 - actual/360 day count basis, 260–261
 - assumption, 276
 - curve, usage, 217, 223
 - decline, 150
 - forward LIBOR, 205e
 - assumption, 204
 - initial rate, assumption, 151
 - LIBOR-based floaters, 196–197
 - LIBOR plus 50, 158
 - OAS values, 276
 - strike rate, comparison, 159
 - swap curve, 312
- London Interbank Offered Rate OAS (LOAS), 217
- Long-term performance trends, projection, 288e
- Loss
 - allocation, 284
 - matrix analysis, 296–297
 - measurement, 67–68
 - rate, 75
 - surfaces, three-dimensional
 - surfaces (creation), 297
 - terminology, 66–75
- Loss-adjusted yield, 290–291
 - metric, 296–297
- Loss severity, 21–22, 282
 - assumptions, 75
 - collateral/bond projected losses, 292e
 - measures, 72–75
 - rate, calculation, 75
- Lower-coupon MBS, prepayment speeds, 80
- Macaulay, Frederick, 233
- Macaulay duration, 233–234
- Manufactured housing loans (MHs), 50, 65–66
- Manufactured housing prepayment (MHP) curve, 66, 67e
- Manufacturing defects, 191
- Market price, calculation, 221
- Maturity bucket, 242
- Maturity-matched mortgage, usage, 318
- Mean standard error (MSE), 224
- Media effects, 86, 319
- Metrics, generation, 49
- Mezzanine bonds, 173
- Mezzanine tranches, 173
- Model-equivalent CPRs, estimation, 302
- Model-generated analysis, 297, 300, 302
- Modeling error, impact, 19
- Modified duration, 233–234
- Modified loans, treatment, 284
- Monte Carlo simulation, 211, 245
 - methodology, steps, 216–220
 - OAS analysis, relationship 262–267
 - overview, 215–216
 - process, schematic, 221e
 - usage, 214–226, 275–276
- Monthly cash flow
 - construction illustration, 57–65
 - discounting, 222e
 - pass-through example, 58e–59e, 61e–62e, 63e–64e
 - PSA assumption, example, 113e–114e
- Monthly CDRs, PSA (usage), 75e
- Monthly default rate (MDR), 69, 70, 288
- Monthly defaults (calculation), SDA/PSA (usage), 73e
- Monthly interest cash flows, calculation, 26
- Monthly payment factor, calculation, 13
- Monthly principal cash flow allocations, 179e
- Monthly principal payments, 122e
- Mortgage ABS, 167
- Mortgage ABS deals
 - cash flow waterfall, schematic representation, 197e
 - credit enhancement, 199–201
 - credit structure, factors, 201–202
 - structuring, 193
 - triggers, 200–201
- Mortgage-backed securities (MBSs), 4, 10
 - average lives/durations (shortening), prepayment speeds (impact), 257
 - cash flows, monthly occurrence, 212
 - demand, short position attributes, 156–157
 - derivatives, 129
 - evaluation, variable coupon rates (usage), 260–262
 - hedge ratio, 237–238
 - market, dislocations, 168–169
 - MBS-specific OAS, 323
 - optimal coupon, calculation, 42
 - pools, demand (front months), 37–38
 - prepayment
 - rates, measurement, 51
 - terminology, addition, 60
 - prices, time series, 237
 - returns factors, 274
 - riskiness, 234–235
 - structuring, 134–140
 - process, 45–46
 - structuring techniques, 101, 109
 - total return, 226–227
 - trading, 35–40
 - types, creation, 24–34
 - valuation, 323–326
 - framework, 323
 - KYF approach, 305–306
 - option-theoretic approach, 305
 - option-theoretic models, 306–307
 - techniques, 211
- Mortgage-backed securities (MBSs) market
 - cumulative percentage, 84e
 - growth/development, 23–24
 - overview, 23
 - role, 40–44
 - structure, 36–37
- Mortgage Bankers Association (MBA)
 - ARM Percentage, FHLMC Survey Rate (contrast), 88e
 - delinquency classification, 68
 - Refi index, FHLMC survey rate (contrast), 86e
 - refinancing applications index, usage, 86
- Mortgage credit analysis, 5
 - characterization, 7–8
- Mortgage insurance (MI), insurance wrap (contrast), 206
- Mortgage loans
 - mechanics, 12–17

- Mortgage loans (Cont.)
 prepayments, measurement, 64–65
 transformation, 24–25
- Mortgage market
 composition/performance, change, 3
 kingdom classification, 103
- Mortgage pass-through securities, prepayments (interest rate path dependence), 215
- Mortgage pools
 interest components, 318e
 market prices, 308
 naive laggard distribution value, factors, 322e
- Mortgage prepayments
 penalties, 12
 risk, 17–19
- Mortgage products
 risks, 17–22
 structuring, 103–106
- Mortgage rates
 term structure, 311–313
 turnover, impact, 313–314
- Mortgage-related asset-backed securities, 167
- Mortgage-related principal/interest, structuring (differences), 142
- Mortgages
 cash flows, 45, 307
 impact, 186–187
 defining, attributes, 4–12
 derivatives products, valuation, 317–318
 fair coupon, 316e
 industry, changes/dislocations, 3–4
 lending, impact, 82
 option-based prepayment model, 307–311
 overview, 3, 4–12
 payment factor, calculation, 13
 price performance, 19
 refinancability, 315–316
 refinancing efficiency, 315e
 risks, 17–22
 sector, credit exposure (analysis), 20
 strips, market, 26
 structures, closed universes, 45
 valuation, 311–318
 value, refinancing behavior (impact), 321e
- Mortgage securities
 theoretical value, computation, 219–220
 valuation, 216–220
- Mortgage servicing rights (MSRs), 28
 result, 160–161
- Moving Treasury Average (MTA), 8
- Multiple (coupon leverage), 149
- Municipal bonds, call risk, 17
- Naive distribution, 322
- Naive laggard distribution, 321
- Negative amortization ARM, 9
 payment structure, 16
- Negative convexity, 19
- Negative overcollateralization, 284
- Net interest, example, 195e
- Net interest margin (NIM) bond, 204, 206
- Net note rate, 32
- No-cash refinancing, 6
- No income-no asset programs, 7
- Nominal spread, 213
 limitations, 211
 OAS, comparison, 223
- Nonaccelerated seniors (NAS) bonds, 106
 cash flows, 177e
 distribution percentage, 177–178
 lockout, 177
 origins, 176–177
 percentage, 177–178
 presence, 178
 principal payments, impact, 177
 structuring, 207–208
- Nonagency MBS
 deal-specific factors, 283–284
 returns, factors, 281–284
- Nonagency pool, note rate example, 69
- Nonagency private-label deal, 103
- Noncallable debenture, incremental returns (contrast), 269, 271
- Noncontiguous interest-only hybrid ARM, 10
- Noneconomic residual, 195–196
- Nonjudicial states, 283
- Nonprepayable mortgages, fair coupon, 312e
- Nonrecoverable losses, absorption, 30–31
- Nonrefinanceable mortgage, fair coupon, 313e
- Note rate, 8
 loans, pooling options, 41e
 securitization, 32
 strata, execution (optimum), 42
- Notional value, calculation, 165
- Office of Thrift Supervision (OTS), delinquency classification, 20, 68
- 100% Prepayment Assumption, 65
- 100 PSA, graphical depiction, 54–55
 graphical depiction, 54e, 55e
- Option-adjusted convexity (OAC), 265
- Option-adjusted duration (OAD), 234–236, 265
- Option-adjusted spread (OAS), 211, 220–223
 analysis
 Monte Carlo simulation, relationship, 262–267
 usage, 214–226, 266
 calculation, Monte Carlo simulation (usage), 262–263
 determination, 222–223
 interpretation, 223
 measure, pitfalls, 225–226
 model output, 264e
 output, 266e
- Option cost, 223–224, 265
 calculation, 223
- Optionless bullet mortgage yield curve, 312e
- Original balance, 36
- Original loan term, 5
- Original LTV, 6
- Original tranche coupon, usage, 145–146
- Out-of-the-money MBS, prepayment speeds, 254
- Out-of-the-money pools, prepayments, 79
- Out-of-the-money rates, 19
- Outstanding balances, note rate cumulative percentages (comparison), 84
- Overcollateralization (OC), 32
 creation, 199–200
 difference, 195–196
 meaning, 194–195
 requirement, mitigation, 202
 structures, 32, 105, 167, 193
- Parallel-shift rate scenarios, 248
- Parent tranche, 275
 calculation, 277
 stripping, 146
- Partial durations, 242
- Partial prepayment, 50
- Passthroughs, 58e–59e
 CMO tranches, comparison, 269
 valuation, complexity, 215
- Payment option ARM, 9

- Payment spike (payment shock), 89
- P bonds, 204–206
- Pension funds, ERISA rules, 176
- Performance measure, total return (usage), 268
- Periodic cap, 9
- Periodic coupon interest, payment, 112, 121, 126
- Periodic total return, calculation, 227
- Planned amortization classes (PACs), 116–129
 - average lives, 127e
 - balance schedule, 119
 - band drift, 259
 - cash flows, 125–126
 - CMO, yield-to-price table, 253e
 - effective bands, 128e, 259, 260e
 - incremental returns, 272
 - localization, 181–185
 - PAC-support structure, 116–129
 - execution, improvement, 144–145
 - graphic representation, 120e, 125e
 - outstanding balances, 258e
 - proportion, 123
 - profile, 263e
 - schedule, 117, 119
 - creation, 118e
 - example, 118e, 120e, 122e
 - generation, 182
 - stability, 259
 - stripping, 144–145
 - structuring, SSTs (contrast), 183, 185
 - structuring process, 116–117
 - tranches, 126
 - yield table, example, 230
- Planned amortization classes (PACs) bonds
 - consideration, 220
 - series, creation, 126–129
 - yield matrix, 250
- Pool, 24
 - coupon rate, change, 30
 - original balance, 36
- Pooling and Servicing Agreement (PSA), 189
 - detailed information, 190
- Pooling practices, 28–29
- Pooling up/down, 29
- Pool WACs, range, 162
- Portfolio barbells, 274
- Preidentified pools, trading, 36
- Premium loan groups, 32
- Premium tranche size, 147
- Prepayable, nonrefinanceable mortgage, fair coupon, 313e
- Prepayment rates
 - assumptions, 54
 - time, passage, 90–92
- Prepayments, 124e
 - acceleration, 123
 - analysis, 50–51
 - attribution, 19
 - burnout, 310–311
 - classification, 307
 - consensus speeds, Bloomberg medians (usage), 248
 - defaults, interactions, 96–97
 - duration, 242, 243
 - dynamic scenarios, 254–260
 - fundamentals, 77–85
 - increase, 19–20
 - measurement, 49
 - models, LIBOR usage, 217
 - penalties, 12
 - payments, 204
 - prioritization, 106
 - risk, 17–19
 - S-curves, 79e
 - terminology, 50–52
 - vectors, 93e, 221e, 254–260
- Prepayment speeds
 - assumption, 115–116
 - calculation, 52
 - deceleration, 50
 - differences, 187e
 - expectation, 174–175
 - factors, 85–92
 - impact, 124e
 - range, designation, 116
 - time-related changes, 91
 - usage, 198
- Price compression, 240–241
- Price difference (drop), 38
- Price effects, impact, 241e
- Price-to-yield matrix, creation, 246
- Price-yield curve, movement, 241
- Prime deal, 193
- Prime loans, 5, 7
- Prime mortgages, 103
- Prime private-label structures, 104–105
- Principal
 - balance, remainder, 15e
 - closed universe, 109
 - divisions, 106
 - flow chart, 201e
 - lockout, 249
 - value, 318e
 - window, 248–249
- Principal component analysis (PCA), 225
- Principal-only (PO) face value, 144
- Principal-only (PO) percentage, calculation, 33
- Principal-only (PO) security, 26
- Principal-only (PO) tranches, 141
- Principal paydown window, 115
- Principal-paying inverses, structuring, 148–149
- Principal payments
 - disbursement, 112, 121, 126
 - schedule, generation, 117
- Principal return
 - amount/timing, 282–283
 - prepayments/factors, impact, 77
- Private label
 - consideration, 167
 - generic term, 25
- Private-label ARM deals, shifting interest mechanism, 172
- Private-label CMOs, structuring, 167
- Private-label credit enhancement, 169–176
- Private-label deals, 25, 167, 168
 - cleanup calls, 168
 - execution, agency pooling (contrast), 173–176
 - impact, 181
 - limitation, 186
 - monthly principal cash flow allocations, 179e
 - note rates securitization, 32
- Private-label deals (collateralization), loans (impact), 168
- Private-label MBS returns, estimation process, 290–303
- Private-label MBS tranches, yield tables (example), 298e
- Private-label PAC market, non-standardization, 182
- Private-label pass-throughs, direct sale, 31
- Private-label prime sector, inefficiency, 104
- Private-label securitization, 30–33
- Private-label senior structuring, variations, 176–189
- Private-label transactions, 24–25
 - deal size, 105
- Products
 - large-scale transitions, 89
 - transitions, 78, 87–89
- Property, sale/destruction, 18
- Prospective prepayment curve (PPC), 60, 168
 - base-case prepayment assumption, usage, 62
- Prospectus Supplement (ProSup), 189

- Public Securities Association (PSA)
 assumption, 57
 CPR vector, contrast, 92e
- Public Securities Association (PSA) prepayment, 51
 benchmark, 53–65
 assumption, 54
 calculations, 55–56
- Quarter-coupon pools, origination, 27
- Quarterly single-family existing home sales/total single family homes, implied turnover rate, 81e
- Rate-and-term refinancing, 6, 78
- Rate and term refinancings, 19
- Rate duration, 242
- R bond, face value, 196
- Real estate mortgage investment conduit (REMIC) structures, impact, 165–166
- Real estate owned (REO), 286e, 287e, 289
 delinquency, 296
- Real market prices, KYF model application, 324
- Recovered principal (recoveries), 95
- Recovery percentage, 282
- Refinanceability, assessment, 85
- Refinanceable mortgage, fair coupon, 320e
- Refinancing (refi), 19
 activity, 81–85, 87
 behavior, 307
 model, 309–310
 decision, 314–316
 efficiency, 87, 306, 309
 incentive, degree, 79
 option
 cost, 317e
 market cost, 316–317
 rate paths, simulation, 217–218
- Registration entity, 24–25
- Regression analysis, usage, 236
- Reinvestment risk, 131, 212–213
- Representations, 190
- Representative paths, 225
- Required servicing, 27–28
- Resecuritizations of real estate mortgage investment conduits (re-REMICs), 188–189
 creation, 188–189
 comparison, 206
- Residential deal, 193
 rating agencies, impact, 201–202
- Residuals, 196, 204–206
- Reverse engineered transaction, 218
- Risk-based pricing, 85
- Risk measures, 242–244
- Roll (dollar roll), 37–38
- Rolldown effect, 269
- Roll matrices (transition matrices), 284–285
- Runoff strategy, 268
- Savings, determination, 314
- Scheduled principal payments, 52
- S-curves, example, 79
- Seasonality, 91
- Seasoned mortgages/tranches, 317–318
- Seasons, 90, 105
- Second lien, 5
- Securities
 base-case yields/returns, evaluation, 302
 monthly cash flows, 222e
 OAS output, 266e
 outputs, interpretation, 302–303
 prepayment conventions, home equity/manufactured housing loans (backing), 65–66
 returns, evaluation, 267
- Securities and Exchange Commission (SEC), requirements relaxation, 202
- Securities Industry and Financial Markets Association (SIFMA), 23
 calendar development, 36
 name change, 53
- Senior bonds (triple-A bonds), 102
 restructuring, 189
- Senior MBS, evaluation, 245
- Senior mezzanine (SM) tranche, 297
 examination, 291
 yield/bond loss matrix, 299e
 yield matrix, evaluation, 302
- Senior non-NAS principal cash flows, 181
- Senior pass-throughs, 25
- Senior private-label mortgage-backed securities, credit risk, 281
- Senior private-label pass-throughs, cash flow generation, 44–45
- Senior securities, sale (creation), 174
- Senior-subordinate deal (senior-sub deal), 31
- Senior-subordinate structure, 31e
 sector creation, 104
- Senior-subordination structures, 167
- Senior tranches, 275–276
 credit support, 104
 protection, 30–31
- Sequential bonds, average life, 134e
 extension, 249–250
- Sequential-pay CMO, 111
- Sequential-pay structure, example, 112e
- Sequential tranching, 110e
- Servicers, 4
- Servicing cost, effect, 312
- Settlement dates, price difference (drop), 38
- Shifting interest bonds, impact, 178
- Shifting interest mechanism, usage, 170–171
- Shifting interest structures, 167
- Shift percentage, 177–178
- Short interest rates, level, 196–197
- Short support (front support), 140
- Short-term interest rate paths, usage, 218
 simulation, 217–218
- Short-term rates, path, 276
- Simulated spot rate, simulated future one-month rates (relationship), 219
- Single monthly mortality (SMM) rate, 52–53
 calculations, 53, 55–56, 60
- Sinkers, 183
- Six-pack securities, 169
- Six-pack subordinates, 199
- Soft penalties, 12
- Specified pool trade, 36
- Splits, 31, 103
- Spread
 duration, 242, 243
 matrices, 246–262
 widening, convexity (contrast), 241e
- Spread-to-price tables, 246
- Standard default assumption (SDA)
 convention, usage, 71–72
 prepayments, effects (absence), 72e
- Stated-income programs, 7
- Static cash flow yield analysis, 211–213
- Stipulated trade, 36
- Strategic default, 6, 94

- Strike rate, holding, 159
- Structure creation, super-stable bond (usage), 183e
- Structured securities, creation, 25
- Structuring options, 136
 - total face value, payment (percentage), 139e
- Structuring speed, 109–110
- Subordinate balances, 173e
- Subordinate classes, 25
- Subordinates
 - sector deal, size, 105
 - shifting interest, example, 171e
 - six-pack, 199
 - tranches (splits), 31
- Subordination, 30–31
 - measurement, 170e
 - percentages (splits), 103
- Subprime ABS structure, principal/interest (flow chart), 201e
- Subprime loans, 5
- Subprime sector, loans components, 104
- Super floaters, creation, 151
- Super-NAS bonds, 178
- Super-senior (SS) bonds, 173
 - integrated model, partial output, 300e–301e
- Super-senior (SS) tranches, 297
 - examination, 291
 - losses, absence, 291
- Super-stable bonds
 - creation, 183e
 - average life/profile, 184
 - payment schedules, 184e
- Super-stable tranches (SSTs), 182
 - PAC structuring, contrast, 183, 185
- Super-state bonds, 181–185
- Supply-demand imbalances, impact, 38
- Support bonds, 119
 - average life/duration profile, 136e
 - cash flow volatility absorption, 208
 - sequential tranche, 129
- Support POs, 267
- Swaps
 - contracts, usage, 198–199
 - notional value, 203
- Targeted amortization class (TAC) bonds, 130
- Teaser period, 89
- Third-party originators, 87
- 300 PSA, graphical depiction, 55e
- Threshold refinancing pricing model, 307
- Time horizon, evaluation, 268
- Time tranching, 106, 110–116
- To-be-announced (TBA) market, 37
 - below-market financing, 40
- To-be-announced (TBA) trade, 36
- Total annual floater, example, 151
- Total face value, payment percentage, 139e
- Total rate of return (TR), 245
 - analysis, usefulness, 274
- Total return analysis, 211, 226–229, 268–274
 - biases, 269
 - flexibility, 228–229
 - profile, 263e
- Total returns, 228e
 - difference, 270e, 271e
- Total SMM, calculation, 70
- Tranches
 - average lives, 135e
 - cash flows, graphic representation, 132e
 - coupon rate, reduction, 146e–155e
 - coverage ratios, calculation, 295e
 - face value, creation, 165e
 - falling out, 111
 - losses, collateral (differentiation), 291
 - notional value, 165
 - projected yields, 293e, 294e
 - size, measurement, 170e
 - target coupon, 145–146
- Transactions
 - capital structure, evaluation, 294
 - credit profile, 295e
 - life cycle, 285
 - cumulative losses, estimation, 294, 296
- Transition matrices (roll matrices), 284–285
 - example, 286e
 - performance, multiplication, 287e
 - population profile, application, 287e
- Transunion, Emperica model, 6
- Treasury equivalents, 237–238
- Turboing, 196e, 198
- Turnover, 77–78
 - activity, 80–81
 - impact, 313–314
 - implied turnover rate, 81e
 - model, 308
 - rates, 19
- Two-tiered index bonds (TTIBs), 156–160
- combinations, 106
- constant, 158
- coupon/strike level, utilization, 158
- face value, 159
- presence, 279
- reset formula, 158
- size, coupon/strike level (impact), 157–158
- variation, 159–160
- Unleveraged sequentials, 179
 - structures, average life (percentage increase), 180e
- Unscheduled principal payments, 31–32, 50
 - prepayment speed capture, 95
- Unsecuritized servicing, markets, 161
- Up-front fee, 29
- interest rates, combination, 85
- U.S. Treasury equivalents, 237–238
- U.S. Treasury yields, time series, 237
- Variable prepayment speeds, 254
- Vectors, usage (scenario), 254–255
- Very accurately date maturity (VADM), 132
 - creation, 134
- Veterans Administration (VA), housing credit support, 10
- Volatility
 - constant level, 232
 - duration, 242, 243
- Voluntary prepayment rate (VPR), 95–96, 288
 - impact, 293
 - unchanged transition matrix, usage, 289e
- Voluntary prepayments, 50, 94–96
 - report, 95
- Voluntary prepayment speed
 - default dollar amount, relationship, 70–71
 - projection generation, iterative calculation (usage), 288
- Voluntary SMM, calculation, 69
- Warranties, 190
- Weighted average coupon (WAC), 29–30, 248
 - bucket, percentage, 84–85
 - impact, 161
 - rate, 57, 111
 - receptivity, 32

- Weighted average coupon (Cont.)
 tranches, 161
 creation, 165
 representation, 163, 165
- Weighted average coupon IO
 (WAC IO), notional value, 33
- Weighted average coupon PO
 (WAC PO)
 creation, 44
 size, 33, 42
 valuation, 42
- Weighted average loan age
 (WALA), 55, 248
- Weighted average maturity
 (WAM), 57, 248
- Whippy supports, 121
- Whipsaw scenarios, 229
- Whole loan, 11
- Wide-window front sequential,
 time tranching, 181
- XS tranches, 204
- Yield
 analysis, 296–297
 measures, problems, 212
 table, 246
 three-dimensional surfaces,
 creation, 297
- Yield curve
 change scenarios, 271e, 272e
 flattening/steepening, 271
 risk, 241–242
 shifts, 268
 steepness, 87
- Yield matrices, 246–262
 examples, 297, 298e
 usage, 249–250
- Yield-to-index matrix, usage,
 261–262
- Yield-to-price table, 246
 example, 247e
 Y structure, 172, 207
- Z-bonds, 130–134
 accretions, 134
 generation, 131e
 short support (front support),
 140
 structuring, 134
- Zero-coupon bonds, 131
- Zero-volatility (Z-Vol) OAS,
 223, 265
- Z-spread, 211, 213–214
 OAS, comparison, 223
- Z-VADM combination, 189