Answers to Quiz 6- Chapter 12

Agency Collateralized Mortgage Obligations (CMO) and Stripped Mortgage-Backed Securities (SMBS)

1. The bond classes created with CMOs are commonly referred as
   A. REMICs
   B. clusters
   C. pools
   D. tranches
   E. none of the above

2. Which one of the following statements is true?
   A. The creation of a CMO eliminates prepayment risk.
   B. An agency CMO does not carry the same credit risk as an agency pass-through security.
   C. Fannie Mae does not issue CMOs.
   D. The creation of a CMO can only redistribute the various forms of prepayment risk among different classes of bonds.
   E. The creation of a CMO eliminates credit risk.

3. CMOs issued by agencies are referred by the agencies as
   A. Real Estate Mortgage Investment Conduits
   B. Real Estate Monthly Investment Classes
   C. Real Estate Mortgage Incremental Conduits
   D. Real Estate Mortgage Interest Contracts
   E. Real Estate Mortgage Investment Contracts

4. Which one of the following statements is NOT true?
   A. Support bonds are the riskiest bonds within a CMO structure.
   B. Targeted amortization class (TAC) bonds are created so as to provide protection against contraction risk but not against extension risk.
   C. A reverse TAC provides protection against extension risk but not against contraction risk.
   D. Agency CMOs and SMBs are derivative mortgage products.
   E. In a CMO, there are no rules for the distribution of interest and principal from the collateral.

5. A Stripped Mortgage-Backed Security is created by
   A. assigning distribution of principal and interest of the underlying pass-through security in equal portions to two classes of bonds.
   B. assigning distribution of principal and interest of the underlying pass-through security in unequal portions to two classes of bonds.
   C. assigning distribution of principal and interest of the underlying pass-through security into two bonds so that the two bonds have the same price/yield relationship as the underlying pass-through security.
   D. creating zero-coupon securities from U.S. Treasurys.
   E. none of the above