Financial Analysts Journal ›
Volume 61, 2005 - Issue 3

324 Views | 2 CrossRef citations to date | 6 Altmetric

REFLECTIONS

The Structured Finance Market: An Investor's Perspective

Frank J. Fabozzi , CFA

Pages 27-40 | Published online: 02 Jan 2019

Cite this article https://doi.org/10.2469/faj.v61.n3.2725

Sample our Tourism, Hospitality and Events Journals
>> Sign in here to start your access to the latest two volumes for 14 days

References Supplemental Citations Metrics Reprints & Permissions

Read this article

Abstract

The largest sector of the U.S. investment-grade fixed-income market is structured products—mortgage-backed securities and asset-backed securities. Issues and challenges currently facing investors who participate in this market sector include legal issues (e.g., consumer lending legislation), market structure (e.g., the role of the government-sponsored enterprises), and analytical methods (e.g., prepayment modeling). An important current concern is the need for education and training in the structure ff and for equity a

Asset-b g. In cont ent shifts from the ivables and/or a s does not generate tized is mortgage loans (residential and commercial), which are referred to as mortgage-

About Cookies On This Site

We and our partners use cookies to enhance your website experience, learn how our site is used, offer personalised features, measure the effectiveness of our services, and tailor content and ads to your interests while you navigate on the web or interact with us across devices. You can choose to accept all of these cookies or only essential cookies. To learn more or manage your preferences, click "Settings". For further information about the data we collect from you, please see our Privacy Policy

Accept All
Essential Only
Settings

backed securities (MBS). Collectively, ABS and MBS are referred to as “structured products,” and as of the end of 2004, these securities represented about 40 percent of a broad-based investment-grade U.S. bond index and slightly more than half of the investment-grade products in the same index.

Starting with a brief discussion of why asset securitization has been a major financial innovation, the article discusses current issues and challenges investors who participate in this market sector face-legal issues, questions of market structure, and analytical issues. Legal risk is a major concern to investors in the structured products market and represents the greatest threat to the growth of this sector of the bond market. The most critical issue is the long-standing view that investors in a structured product are protected from the creditors of the seller of the collateral because of the so-called bankruptcy remote trust/true sale opinion. In this concept, when the seller of the collateral transfers it to the trust (a special-purpose vehicle), the transfer represents a “true sale”; therefore, in the case of the seller's bankruptcy, the bankruptcy court cannot penetrate the trust to recover the collateral or cash flow from the collateral. The bankruptcy remote trust/true sale opinion has never, however, been fully tested.

Issues related to the market's structure are the role of the Government National Mortgage Association and two government-sponsored enterprises, the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation; the survival of the “to be announced” market (an important market innovation that works like a forward contract and has fostered the development of the fixed-rate agency pass-through security market); corporate issues masquerading as securitizations; the role of the servicer/trustee; and the increased use of derivatives (including credit default swaps and the relatively new prepayment derivatives). These issues all have an impact on valuation and trading strategies in the structured finance market.

The anal (including prepaym manage nalytical chall erest rate risk (du e collateral's cash flo jecting cash flows for e, the timing of defaults, and the recovery rate. Default modeling for structured products is in

About Cookies On This Site

We and our partners use cookies to enhance your website experience, learn how our site is used, offer personalised features, measure the effectiveness of our services, and tailor content and ads to your interests while you navigate on the web or interact with us across devices. You can choose to accept all of these cookies or only essential cookies. To learn more or manage your preferences, click “Settings”. For further information about the data we collect from you, please see our Privacy Policy

Accept All

Essential Only

Settings

its infancy. Portfolio managers whose mandate is to outperform a broad-based bond index face the problem of constructing a portfolio that has the desired tracking error vis-à-vis the agency pass-through sector of a bond index. Unlike replicating the U.S. Treasury, agency, and credit sectors of a bond index, replicating the pass-through sector is fraught with difficulties.

Finally, the article addresses two groups of investment professionals who are badly in need of education and training in structured finance—compliance staff and equity analysts.

In preparing this article, I greatly benefited from discussions with and comments by the following individuals: Mark Adelson, Anand Bhattacharya, Bill Berliner, Howard Chin, Andrew Davidson, Todd Fasnella, Patrick Fitzsimonds, Laurie Goodman, Dennis Kraft, Alexander Levin, John McElravey, Stefania Perrucci, Edward Reardon, Alex Roever, Andrew Samawi, and Tom Zimmerman.

Related research

People also read | Recommended articles | Cited by 2

About Cookies On This Site

We and our partners use cookies to enhance your website experience, learn how our site is used, offer personalised features, measure the effectiveness of our services, and tailor content and ads to your interests while you navigate on the web or interact with us across devices. You can choose to accept all of these cookies or only essential cookies. To learn more or manage your preferences, click "Settings". For further information about the data we collect from you, please see our Privacy Policy

Accept All

Essential Only

Settings

Copyright © 2024 Informa UK Limited Privacy policy Cookies Terms & conditions Accessibility

Taylor & Francis Group an informa business

Registered in England & Wales No. 3099067
5 Howick Place | London | SW1P 1WG

About Cookies On This Site

We and our partners use cookies to enhance your website experience, learn how our site is used, offer personalised features, measure the effectiveness of our services, and tailor content and ads to your interests while you navigate on the web or interact with us across devices. You can choose to accept all of these cookies or only essential cookies. To learn more or manage your preferences, click “Settings”. For further information about the data we collect from you, please see our Privacy Policy

Accept All

Essential Only

Settings