

CIBC World Markets NHA Mortgage-Backed Securities

If you are looking for an alternative fixed income investment that combines attractive yields with the security of a government guarantee and the convenience of monthly income, consider NHA Mortgage-Backed Securities (MBS).

What are Mortgage-Backed Securities?

NHA Mortgage-Backed Securities are investments that represent ownership in the cash flows from a group of government-insured, residential mortgages. The term "NHA" refers to the National Housing Act, the federal legislation that provides for the offering of mortgage insurance.

Each security is backed by a distinct group of mortgages, known as a pool. Investors in an NHA MBS pool receive a blended monthly payment consisting of any principal that is paid by the underlying mortgagors and an interest component that is based on the pool's coupon rate.

Investment Benefits

UNSURPASSED SAFETY

NHA Mortgage-Backed Securities are considered AAA instruments as the timely payment of both principal and interest is guaranteed by the Canada Mortgage and Housing Corporation (CMHC), a federal crown corporation. Thus, NHA MBS are equivalent to Government of Canada Bonds in terms of credit.

ATTRACTIVE YIELDS

Although NHA MBS offer the same safety of principal, they typically provide an annualized yield that is higher than that of equivalent term Treasury Bills or Government of Canada Bonds.

INVESTMENT ELIGIBILITY

MBS are fully eligible for investment in tax sheltered plans such as RRSPs and RRFs.

MONTHLY INCOME

Each month, principal and interest payments flow from mortgages to investors. Thus, NHA MBS are ideal for investors who desire regular monthly income, especially those looking for suitable RRIF investments.

MARKETABILITY

NHA Mortgage-Backed Securities trade in a fashion similar to government bonds. Since inception, the NHA MBS market has grown considerably, both in size and in the number of market participants. Since CIBC World Markets MBS Trading Desk bids on all outstanding NHA MBS issues, you can always sell your investments before maturity if necessary.

Special Features of Mortgage-Backed Securities

There are two basic types of NHA MBS: non-prepayable pools and prepayable pools.

NON-PREPAYABLE MBS

Non-prepayable pools are the most basic form of NHA MBS. In a non-prepayable pool, unscheduled principal payments are not permitted. Thus, principal on the underlying mortgages in a non-prepayable pool can only be repaid according to the original amortization schedule. Such pools are often referred to as closed pools as they are closed to prepayments.

The monthly cash flow from a closed pool consists of a small principal portion and a larger interest component. As prepayments are not permitted, monthly payments are predictable and consistent in size over the life of the pool. As a result, non-prepayable MBS are suitable for investors who require a predictable monthly cash flow. At maturity, any principal that has not been repaid over the life of the pool is then returned to the investor.

PREPAYABLE MBS

Prepayable MBS are composed of mortgages that allow mortgage holders to make unscheduled principal payments under certain conditions. In addition to scheduled principal and interest, investors holding prepayable MBS may also receive unscheduled principal and, in some cases, the penalty interest charged to mortgagors who make early prepayments. Prepayable pools are often called open pools as they are open to early principal repayments.

The potential for prepayments can cause the cash flows from prepayable pools to vary on a monthly basis. Although the original principal is guaranteed by the federal government, the timing of principal payments is somewhat uncertain. Prepayable MBS are better suited for investors looking for yield enhancement because they are compensated for the variability in cash flow by yields that are higher than on comparable non-prepayable MBS.

Pool Numbers and RPB Factors

Individual MBS pools are identified by a unique eight digit number known as a pool number. The first three digits of a pool number give an indication as to the pool type of a given issue. Pool numbers beginning with 990 and 966 are given to non-prepayable pools while pool numbers beginning with 967 and 964 indicate prepayable pools.

In order to keep track of the principal that has been returned for individual pools, a statistic known as the RPB factor is used (RPB is short for Remaining Principal Balance). The RPB factor is an eight digit decimal number that indicates the amount of original principal remaining for the mortgage pool after the current months payments.

As an example, consider an MBS with a pool factor of 0.98350000. For every \$10,000 of original principal, approximately \$9,835 remains outstanding and \$165 has been repaid. The RPB factor is often referred to as the pool factor (not to be confused with the pool number which is used to identify specific pools).

Answers to Commonly Asked Questions

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WHEN DO I RECEIVE MBS PAYMENTS?

The payment date for NHA MBS is the 15th of the month. Payments are made on the 15th for any and all principal and interest due at the end of the previous month. If the 14th or 15th fall on a non-business day, payment will be made the second business day following the 14th. This payment date is also used for any balloon payment of principal due at maturity.

WHAT TERMS ARE AVAILABLE?

Although most NHA MBS are issued in terms of 3 or 5 years, some pools are issued with terms of 10 years or longer. The large number of issues outstanding also provides for an active secondary market that offers a variety of terms, coupons and yields.

WHAT ARE THE TAX IMPLICATIONS OF INVESTING IN MBS?

Monthly payments from MBS are comprised of both interest and principal. As per the CMHC MBS Information Circulars, Canadian residents are taxed (as income) on only the interest portion of their payment. Capital gains are realized at disposition or maturity and will be taxed under normal capital gains rules.

CAN I OBTAIN PHYSICAL CERTIFICATES FOR MY MBS INVESTMENT?

All NHA MBS are available on the **book based system**, which means there is no need for physical delivery. If you require physical delivery, MBS certificates can be issued in certificate form.

IS THERE A MINIMUM SIZE FOR AN MBS INVESTMENT?

NHA MBS are available for minimum face value amounts of \$5,000 and in \$5,000 multiples thereof.

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CIBC
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**NHA Mortgage-
Backed
Securities**

MULTI
CALLABLE
NOTES
EQUITY INDEX
LINKED NOTES

STRIP
BONDS

COUPON
ANNUITY
PACKAGES

CORPORATE
BONDS

FOREIGN
BONDS

EUROBONDS

FOREIGN
EXCHANGE

RETIREMENT
SAVINGS
PLANS

MONEY
MARKET

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will be pleased to demonstrate how
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fixed income returns.**