

Perpetual knowledge bank series: RMBS

By Perpetual Asset Management

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Residential Mortgage-Backed Securities or RMBS are a specific type of bond that is secured against a large pool of residential mortgages. While home loans are typically private transactions between a lender and an individual borrower that stay on the lender's balance sheet for the duration of the mortgage, an RMBS is a debt security that is typically acquired by

institutional investors and financial institutions. While home lenders have to pay interest, RMBS investors earn interest.

RMBS are best thought of as a collection of interrelated bonds that are secured against a large pool of residential mortgages. Instead of just two or three home loans, RMBS notes typically group together hundreds if not thousands of home loans. The key feature of RMBS structures is 'tranching', which transforms the mortgage pool into a range of securities (the RMBS notes), each with a different risk and maturity profile. Interest on RMBS notes is paid in [coupons similar to bonds](#). A coupon is an interest payment promised to the investor at regular intervals for the term of the bond. Payments of interest and principal – and allocations of losses – to the RMBS notes are made at regular intervals (typically monthly) on pre-set payment dates.

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