



## U.S. STRUCTURED FINANCE NEWSLETTER

ISSUE 46. FEBRUARY 22, 2005

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### U.S. Student Loan ABS Criteria

In this newsletter, Dominion Bond Rating Service (DBRS) provides guidance to originators, lenders, or facilitators as they prepare new securitizations, as well as institutional investors as they evaluate their portfolio allocations.

Student loan securitizations fall into two categories: U.S. Government-Backed Student Loan Securitizations and Private (or "Alternative") Student Loan Securitizations. Some securitizations include private and alternative loan portfolios. The demand for student loan monies, especially non-government-backed alternative loans, is growing, and DBRS expects continued expansion.

A comparison of student loan funding and securitization statistics indicates the majority of alternative student loans are ultimately financed through the capital markets via the use of securitization vehicles. Accordingly, the increasing volume of student loan ABS has intensified institutional investor preferences for objective measures of their creditworthiness, such as a DBRS rating.

### Government Loan Programs: Program Compliance-Driven Servicing

The government offers two basic student loan programs to students and/or their parents: (1) direct, and (2) guaranteed loans. It exclusively funds Federal Direct Student Loan Programs. Consequently, capital markets do not play a role in these programs, except indirectly through the U.S. Treasury market. Federally guaranteed loans, however, are almost always funded by the non-government capital markets. These programs are closely monitored for servicer compliance by the Department of Education (DOE). Non-compliance can jeopardize the government's guaranty, potentially compromising securitizations backed by student loans pools serviced by these servicers.

The primary risk to the recoverability of invested funds lies with the servicer's ability to precisely satisfy the requirements set forth by the DOE. Understanding the government review methodologies is a key facet of due diligence.

### Alternative Student Loans: Collateral Performance-Driven Servicing

Alternative student loans are provided by private lenders and do not benefit from ultimate government guarantees. The critical underwriting criteria for these loans are driven by individual obligors' creditworthiness. Credit risk can be partially or wholly mitigated at the:

- (1) Individual loan level through guarantees issued by private guarantors,
- (2) Security level by one of the monoline financial guarantee insurers, or
- (3) Structural level through a multi-class, senior/subordinated cash flow.

Student borrowers' lack of credit history challenges originators of student loans. As with government programs, the servicing process is a critical component of the private student industry. For alternative loan originators/lenders successful servicing is defined by the servicer's ability to collect on the loan as opposed to its administrative aptitude for satisfying the government's guarantees rules.

### Conclusion

While there are substantial differences between government and private student loan markets, most of the analytical characteristics for both collateral segments overlap. DBRS has therefore created a single list of required information, including pool and loan/obligor-level statistics, to evaluate credit risk.