defaqto

Fund review

Architas

Passive Intermediate Fund

April 2020

architas

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Defaqto fund reviews

This document is designed to provide the reader with a quantitative overview of the fund reviewed.

The review then goes on to examine information of a more qualitative nature, which has been obtained through an interview process with the fund manager/s.

The qualitative information covers specific areas including the fund manager's philosophy, their people, and the processes they employ.

Additional information is also provided on their research capability, the resources they have at their disposal and how they manage risk.

All of this information goes towards creating this comprehensive Fund Review.

Defaqto Ratings

Ratings to help advisers and their clients make better informed decisions

The Defaqto experts have created a range of ratings to help advisers find the best product or proposition for their clients.

Show at a glance how a fund or fund family performs in comparison to the rest of the market.

Demonstrate the comprehensiveness of products across a range of areas, from pensions to DFMs.

An overall assessment of service – by advisers for advisers.

Suitability ratings to support compliant advice

Defaqto have created a set of ten Risk Profiles, and four Income Risk Profiles with corresponding ratings to which funds are mapped using a robust process. This helps advisers to evidence suitability for their clients in both the accumulation and decumulation phase:

Fund review

Architas

Passive Intermediate Fund

Nancy Mills, Insight Analyst.

Executive summary

Architas was established in 2008 as a specialist boutique within the global AXA Group to focus solely on providing multi-asset and multi-manager portfolio solutions to institutional and retail clients. 100% AXA-owned, it operates autonomously within its chosen field, with no connection to AXA IM.

Architas' multi-asset offering comprises passive, blended and active fund of fund products. Within each style, the risk profile ranges from lowest (2) to highest (7). This risk mapping is determined by Evalue, an external tool which also provides the strategic asset allocation output on which portfolio construction is based; it does not necessarily align with other systems' rankings. Evalue determines the appropriate asset allocation and fixed volatility bands for each fund given its risk/return objectives.

This 'Passive Intermediate' fund aims to generate returns on a long-term basis by a combination of capital growth and income, with a median level of volatility. Its Evalue risk profile of 4 (Defaqto 5) lies in the middle of the passive range (hence the name 'Intermediate'); it will typically have the majority of its exposure to developed market equities, but the balance will comprise bonds, government issues, property (capped at 5%) and cash. There is minimal exposure to emerging markets. It invests via index trackers wherever possible and is hence called 'Passive'.

This portfolio of passive vehicles is actively co-managed by the highly experienced Sheldon Macdonald and Alex Burn. They, along with 16 further analyst/managers, seek out the 'best of breed' fund in the discrete asset class for which they are responsible. The selection process is well defined and appears to be applied in a disciplined manner by a team with good levels of experience. Risk oversight looks robust, with the risk team reporting independently to CEO Hans Georgeson (Matthieu Andre from 1st March 2020).

A 'Super clean' share class (S) have been widely available since August 2018, with an AMC of 25bp. The data in this document has been created using that share class.

About Architas

Architas was established in 2008 as a specialist boutique within the global AXA Group. It is 100% owned by AXA and its board executives report directly into the AXA Group. Hans Georgeson, who has over 20 years' financial industry experience, has been company CEO since 2010. Georgeson has very recently announced his decision to step aside as CEO and has been succeeded by Matthieu Andre with effect from 1st March 2020. Andre has significant experience of the AXA Group having previously held the posts of CEO of AXA Global Life and Savings and Deputy CEO and Chief Strategic Development Officer for European Markets. Headquartered in London, Architas employs around 280 people around the world, including the 18 investment professionals most closely associated with the fund reviewed in this report.

Architas designs multi-asset and multi-manager fund solutions; within this, its ranges include risk profiled funds (passive, active and blended funds), income generating funds and specialist equity and bond funds. As at end December 2019, assets under management and advice for external clients (both retail and institutional) and also various AXA group entities, totalled £23.8bn.

In terms of operations and fund selection, it is important to note that Architas operates independently of AXA IM and that there is no crossover between Architas and the AXA IM MACS (Multi-Asset Client Solutions) division led by renowned veteran investor Serge Pizem. Additionally, Architas' fund of funds products are completely unfettered; there is no requirement to hold AXA vehicles, and AXA funds must undergo the same selection process as any other fund and compete on the same terms as any other fund provider.

Defaqto Ratings

Quantitative review

Investment objective

All analysis using Morningstar data to 31 March 2020

The fund aims for a medium to long-term return, combining capital growth and income, by investing in a diversified range of asset classes, with median levels of volatility. There is no specific stated target return. The fund can invest in cash, equities, bonds and property; it may also use warrants, derivatives, money market instruments, borrowings and deposits, and engage in hedging and stock lending. In implementing the strategic asset allocation set by Evalue (see 'asset allocation' below), the fund utilises - wherever possible and practical - 'Passive' instruments i.e. vehicles that seek to track the performance of indices. 'Intermediate' refers to the risk level in the asset allocation. Fund selection is actively managed.

Fund information and classification

Launch Date	Oct 23 2012
Fund Manager	Sheldon MacDonald & Alex Burn
Domicile	GBR
Assets	Passive
Approach	Risk Targeted
Type	OEIC

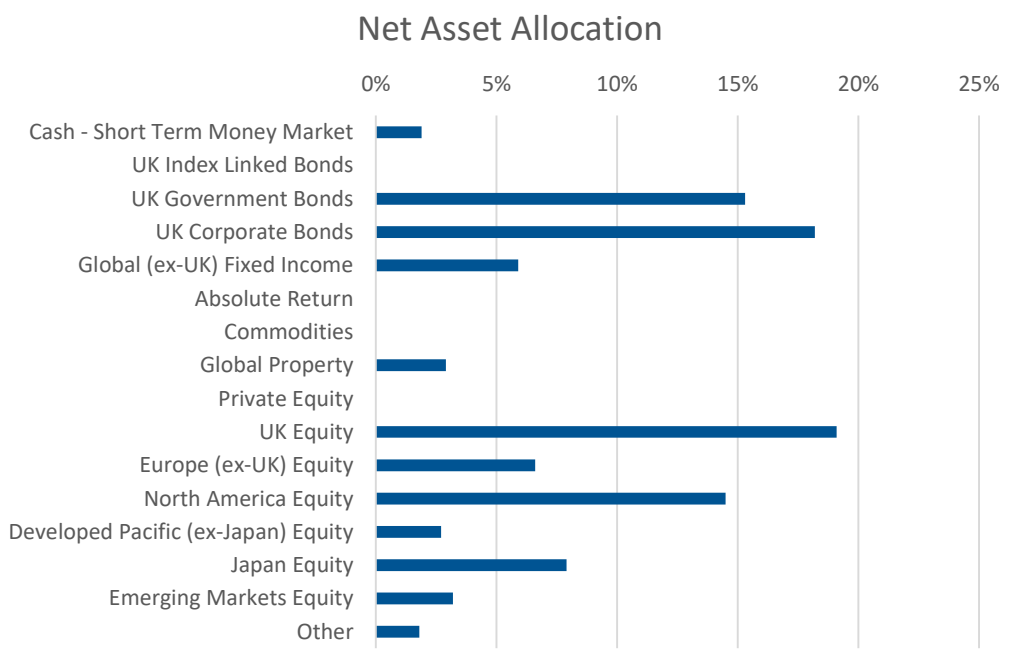
IA Sector	Volatility Managed
Morningstar Category	Moderate Allocation
Defaqto Diamond Rating Type	Not rated
Diamond Rating	Not rated

*Note: The Morningstar Category is used in all comparative analysis, over the following pages.

Asset allocation

The strategic asset allocation for this fund is set by Evalue, an external tool which models asset behaviour and correlations in hypothetical scenarios over varying time periods- indicating the optimum allocation for the desired long-term risk/return profile of the fund. Essentially, it is a forward-looking model indicating potential risk and returns. However, that allocation is subject to Architas-imposed constraints to ensure both diversification and its suitability currency-wise for UK-based investors. Property exposure is capped at 5% due to its illiquid nature. The tolerance level (i.e. permitted deviation from the allocation) for any asset class with a weighting of more than 10% is +/-2%. For an asset class below 10%, the tolerance limits are +/-1%.

In the 'Intermediate' fund, the majority of the fund is in developed market equities (emerging markets' exposure is negligible) but there will be sizeable bond positions in both government and corporate issues.



Note

This asset allocation chart is drawn using the 16 asset classes (including 'other') that we use in our modelling.

This may differ slightly from the asset allocation described by the fund manager, due to various asset class roll-up and mapping variances.

Top 10 holdings

This is a fund of funds, which explains the zero numbers for the equity and bond holdings. The top 10 holdings make up over 80% of the overall fund.

The four largest holdings, making up around 45% of the portfolio combined, are two bond funds and two UK Equity funds.

This fund is truly unfettered, which is evident in the holdings data below.

Date	31/03/2020
Total Number of Equity Holdings	0
Total Number of Bond Holdings	0
Assets in Top 10 Holdings (%)	79.61

Name	Sector	Country	% of assets
Vanguard FTSE U.K. All Shr Idx UT Acc		United Kingdom	11.25
iShares UK Equity Index (UK) L Acc		United Kingdom	11.01
Vanguard UK Inv Grd Bd Idx GBP Acc		Ireland	10.98
iShares Corporate Bond Index (UK) L Acc		United Kingdom	10.80
Vanguard US Equity Index Acc		United Kingdom	7.48
iShares US Equity Index (UK) L Acc		United Kingdom	6.99
iShares UK Gilts All Stks Idx (UK) L Acc		United Kingdom	6.34
Vanguard UK Govt Bd Idx GBP Acc		Ireland	6.25
iShares Japan Equity Index (UK) L Acc		United Kingdom	4.35
Vanguard Japan Stock Index GBP Acc		Ireland	4.15

Liquidity

The assets held within this fund are extremely liquid, with 100% being able to be liquidated within 7 days.

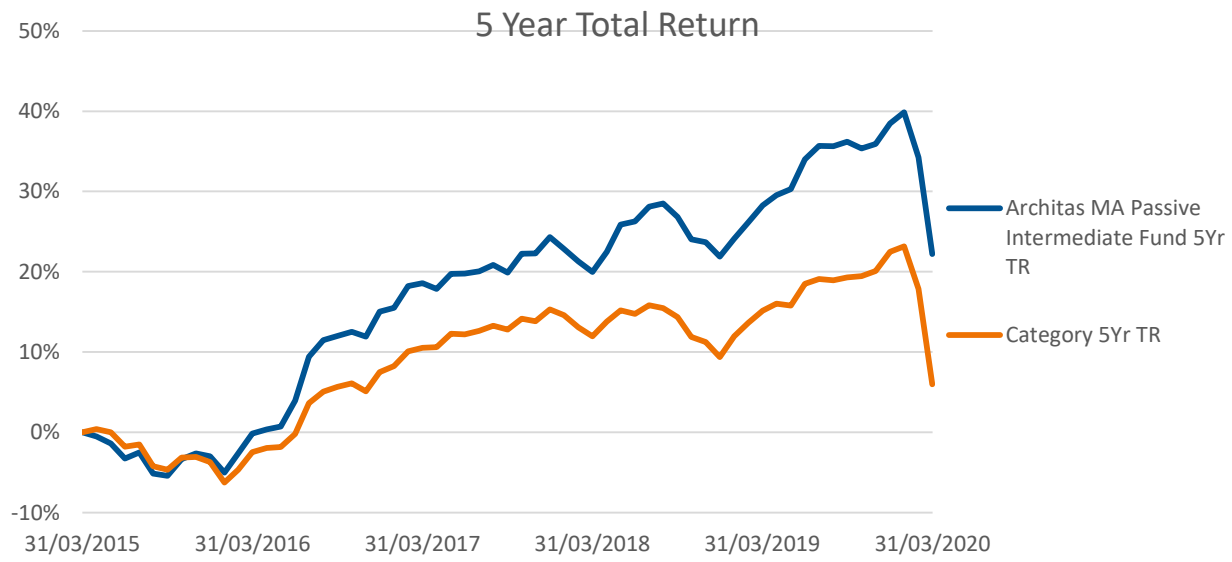
Days to liquidate holdings	% of portfolio
1 - 7 days (%)	100.00
8 - 30 days (%)	
31 - 180 days (%)	
181 - 365+ days (%)	

Source: Architas February 2020

Performance - total returns

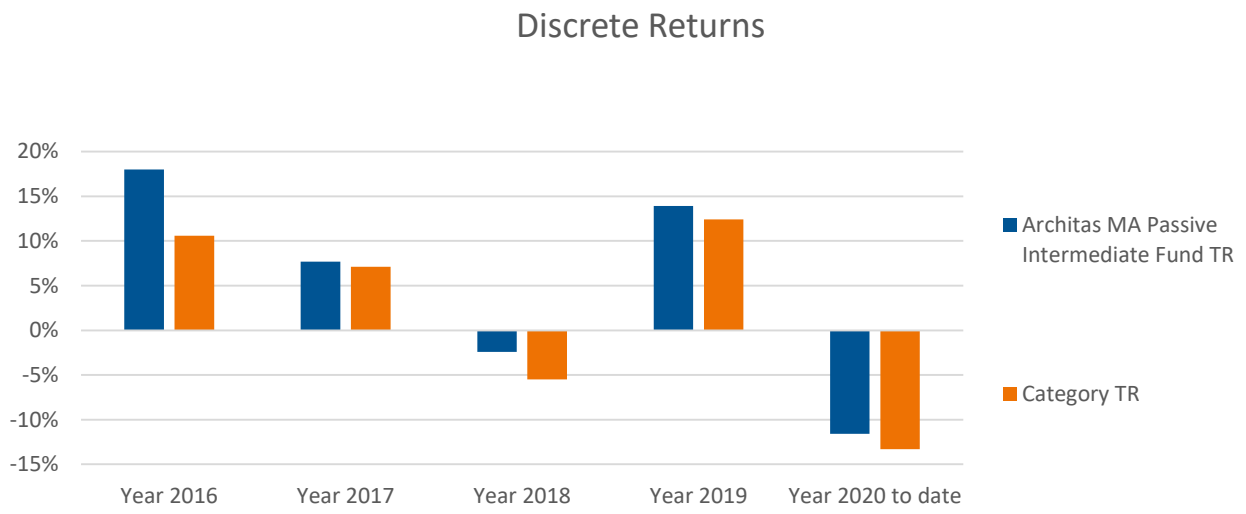
The fund has shown a very strong performance and has consistently outperformed the category average over the last five years.

The last couple of years, the gap between the performance of the fund and the category average has continued to widen despite the downturn in markets we are seeing in early 2020.



Performance - discrete returns

Peer-relative and absolute performance has been consistently strong across the five discrete time periods shown in the chart below. The fund has outperformed the category average in every discrete year noted below, on the upside and on the downside. The fund continues to perform better than the category average in early 2020, demonstrating Architas' desire to protect the fund on the downside.

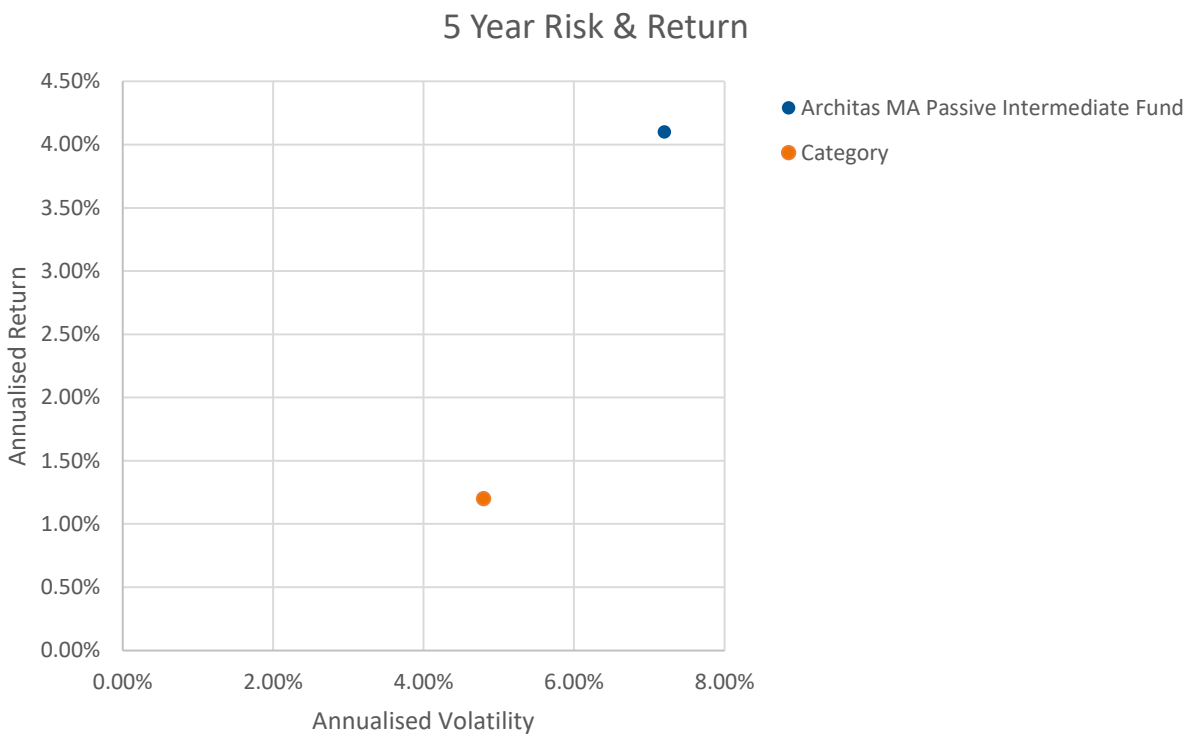


Risk

The fund has had a higher volatility level than the category median fund on a five-year view but returns have been better over that period.

In terms of risk profile, the fund sits in the middle of the passive range (ranked 4 on Evalue's forward looking model). This fund has a Defaqto 5 risk rating.

Actual levels of volatility going forward may differ from expected levels of volatility. We have seen an increased level of volatility during the first part of 2020, due to the Coronavirus pandemic.



Drawdown

As might be expected of a fund with a median risk profile, drawdowns are more moderate in nature. Positive months have outweighed negative months over the last five years. Both the max drawdown and worst month figures were during 2020.

Last 60 Months	
Max Drawdown	-17.6%
Positive Months	38
Negative Months	22
Worst Month	-9.4%

Fund size and fees

This fund has AUM of £669m and is one of the larger funds in the Passive range. It is worth re-emphasising that the multi-asset and multi-manager styles are Architas's specialism, and total AUM as at end December 2019 was £23.8bn.

All share classes are available in 'clean' and 'super clean'. The 'clean' remains available to direct investors, whilst the 'super clean' has been widely available on all platforms since 1 August 2018. The AMC on the 'super clean' class is reduced by 20bp to 25bp in this fund.

AUM	£669M
OCF Estimated	0.42%
OCF Actual	0.42%
Transaction Fee Actual	0.03%
Performance Fee (Yes/No)	No
Performance Fee Actual	n/a

Qualitative review

Defaqto analysts met members of the Architas fund team at their offices in London in December 2018 and February 2020.

Philosophy

Architas aims to provide a simple, understandable approach to investment. It offers a range of multi-asset and multi-manager portfolios tailored to investors' differing risk tolerances and preferences.

The Architas approach blends top-down and bottom-up elements. In the multi-asset fund ranges (passive, blended and active), the strategic asset allocation and volatility parameters appropriate for each fund's risk/reward profile is set using the output of a 15-year forward looking model, from external model provider Evalue. These parameters are strictly observed in the Passive range, with the funds sitting in the mid-point of their volatility range; in the Blended and Active ranges there is leeway for shorter-term tactical allocation tilts (which may be regional or stylistic in nature), although they are still managed within their volatility parameters. The asset allocation framework is then populated bottom-up by the investment team's fund choices. The in-house fund selection process, intended to be both detailed and thorough, is viewed as a cornerstone of the process and integral to the company's investment philosophy.

Since the arrival of CIO Jamie Arguello in 2016, there has been a move to make portfolios more focused (i.e. in terms of number of holdings) and also a renewed emphasis on downside protection. Stylistically, the Architas investment approach has become more 'evidence-based' than 'flair- based'.

With respect to this specific fund, the name 'Passive Intermediate' requires clarification. 'Intermediate' refers to the style and type of asset allocation allied to this fund's specific expected risk/return profile (i.e. it combines equities and bonds) whilst 'Passive' refers to the actual fund vehicles used to populate that allocation i.e. they will be index trackers and/or ETFs, providing beta but not generating alpha. Whilst 'passive' instruments are used, the fund is actively monitored and managed.

As is usual with 'passive' fund ranges, the emphasis is on transparency, superior index replication and low cost.

Architas prefers to look at its own funds' performance on a market-relative basis i.e. how they would expect funds to outperform at any given stage of a market cycle, or in certain style-based market phases. They also tend to monitor peers that they consider their nearest competition.

Architas are clear on their desire to participate in the upside of market performance while protecting in the downside. They do not expect their funds to be at the top of category average in rising markets but do consider their strategies are better at capital preservation during downward markets than others.

People

The 18-strong Architas team of investment professionals is headed by CIO Jaime Arguello who succeeded Caspar Rock, who left the group in 2016. Since taking over, Arguello has looked for a more focused approach in portfolio construction (in terms of numbers of holdings) and has also prioritised a more evidenced based investment approach to investment. The team averages 15 years' financial industry experience.

There has been some change over the last 12 months or so within the team, with the departure of COO Anna O'Donoghue and the hiring of two new Investment Analysts, Shayan Ratnasingam and Asim Qadri. It has recently been announced that Solomon Nevins will be leaving Architas in the next few months.

The team works in a collaborative and collegial fashion. Most of the funds are co-managed – an equitable relationship, with 'co' rather than 'individual' ownership of fund track records. Each team member has analytical as well as fund managerial responsibilities, by either asset type and/or geography, meaning that their input is relevant and crucial to all funds, not just the ones for which they have named co-responsibility.

The Passive fund range is co-managed by Sheldon MacDonald and Alex Burn.

Jaime Arguello (Engineering, Ecole Nationale des Ponts et Chaussees) – joined Architas in 2016, after seven years as CIO of Barclays' multi-manager and alternatives business. He has over 30 years' experience in markets.

Sheldon MacDonald (BComm, Financial Accounting and Economics, CFA), joined Architas in 2010. As well as co-managing the Architas Blended range the Architas Passive range, he is Deputy CIO, has oversight on fund selection and leads fund manager research on a number of strategies. He previously held similar roles at Nedgroup Investments.

Alex Burn (BA Hons Corporate Management, CFA) – joined Architas in 2013. As well as his co-manager role on the Passive range, he researches Asian and Japanese equity funds.

The investment team

The fund managers

Sheldon MacDonald, CFA
Deputy Chief Investment Officer

Sheldon co-manages the Architas Multi-Asset Passive Fund range, as well as the Architas Global Equity Income fund. He oversees fund selection and manages the products' asset allocation and investment strategies. He also leads fund manager research on global equity strategies.

Before joining Architas in 2010, Sheldon was a fund of funds manager at Nedgroup Investments, part of Old Mutual plc. As well as running a variety of long only multi-asset strategies, Sheldon has extensive experience in the hedge fund space and, prior to joining Nedgroup Investments, was Head of Derivative Trading at Old Mutual Asset Managers in South Africa.

Sheldon has a BComm in Financial Accounting and Economics and holds the IMC and is a CFA charterholder. He has over 25 years of investment experience.

Alex Burn, CFA
Investment Manager

Alex leads research on Asian and Japanese equity funds as well as due diligence on passive strategies and co-manages the Global Equity Income fund and Multi Asset Passive range.

Alex joined Architas in 2013 from the AXA UK graduate scheme. He has a BA (Hons) in Corporate Management and is IMC qualified. He has also been a CFA charterholder since May 2017.

Source: Architas February 2020

Process

The strategic asset allocation for the Passive funds is provided and updated quarterly by Evalue, an external asset allocation tool.

The Evalue tool does not officially exclude any asset class but Architas does impose its own in-house constraints, even for this passive range of funds. It does not like to invest in asset classes that it (and advisers) might find opaque, such as global absolute return funds (GARS); it is also wary of liquidity issues in property and notes that some areas in property are uninvestable and hence impossible to replicate and implement fully. For that reason, property exposure is capped at 5%. This has recently been reduced from 10% due to liquidity concerns at present. Architas were clear that they would favour liquidity over return when it came to choosing a property fund. Architas must also ensure sufficient diversification and also the allocation's suitability currency-wise for UK-based investors. Once these asset allocation constraints are implemented, passive funds must adhere strictly to the subsequent Evalue allocation output.

The Evalue tool incorporates a wide range of economic and asset class variables into its 15-year forward looking model, which is designed to forecast returns and the probability of returns of the various asset classes over that time period. Incorporating the Architas constraints explained above, Evalue determines the appropriate asset allocation and fixed volatility bands for each fund given its risk/return objectives.

Funds in the multi-asset passive range are managed to the mid-point of their prescribed volatility parameters. Unlike the other Architas multi-asset ranges, there is no tactical allocation. Adjustments to the strategic asset allocation are carried out as required when the updated quarterly data is received from Evalue, with rebalancing executed gradually to minimise costs. A shift in asset allocation may require the sale of a holding and/or the addition of a new name. Within this quarterly cycle, regular weekly meetings and the monthly Investment Committee meeting monitor asset allocation (to handle any portfolio rebalancing made necessary by market movements within the quarter).

Fund selection for the passive range is an active process, as not all passive funds are the same. The selection process considers the fund structure, the composition and calculation of the benchmark that it aims to replicate (its breadth, depth and usefulness), the replication methodology and its tracking error over time (to identify any deviation from benchmark). The analyst looks at the size, quality and experience of the investment team running the fund, though, rather surprisingly, there is no explicit requirement for managers to have a track record. Essentially, the analyst looks for the 'best of breed' in each asset class to produce a very focused portfolio. Any new addition has to fit the prescribed asset allocation and ideally should provide an element of risk diversification.

Funds are monitored on an ongoing basis, and at least quarterly for style drift. The lead analyst for each asset class/sector is required to review the buy list formally every six months and to have contact with the manager at least once a year, with conclusions presented at the subsequent portfolio team meeting. A major area of focus for this range is on any change in tracking errors and charges.

A fund may be sold if there are meaningful changes to its process, philosophy or team that the manager deems significant. Divestment may also occur if performance deviates from expectations, or if the analyst identifies a better vehicle in the same asset class.

INVESTMENT PROCESS

STEPS

architas

STRATEGIC ASSET ALLOCATION (SAA)

EValue model input

TACTICAL ASSET ALLOCATION (TAA)

Based on short-term market views

Aims to add alpha

PORTFOLIO MANAGEMENT

Allocation within asset classes

MANAGER SELECTION

Looking for consistent alpha generation

Source: Architas February 2020

Risk management

An investment risk team of seven looks at holdings and portfolio risk on a daily basis.

Independent risk monitoring and oversight is provided by a quite separate risk team of six, led by Massimiliano Zorza, who has been Global Head of Risk since June 2009. There is no crossover in terms of personnel between the two risk teams.

Zorza has almost 20 years' experience in financial operations. He has a separate reporting line to the CEO of Architas and his team operates autonomously of the investment team, providing independent challenge on key metrics.

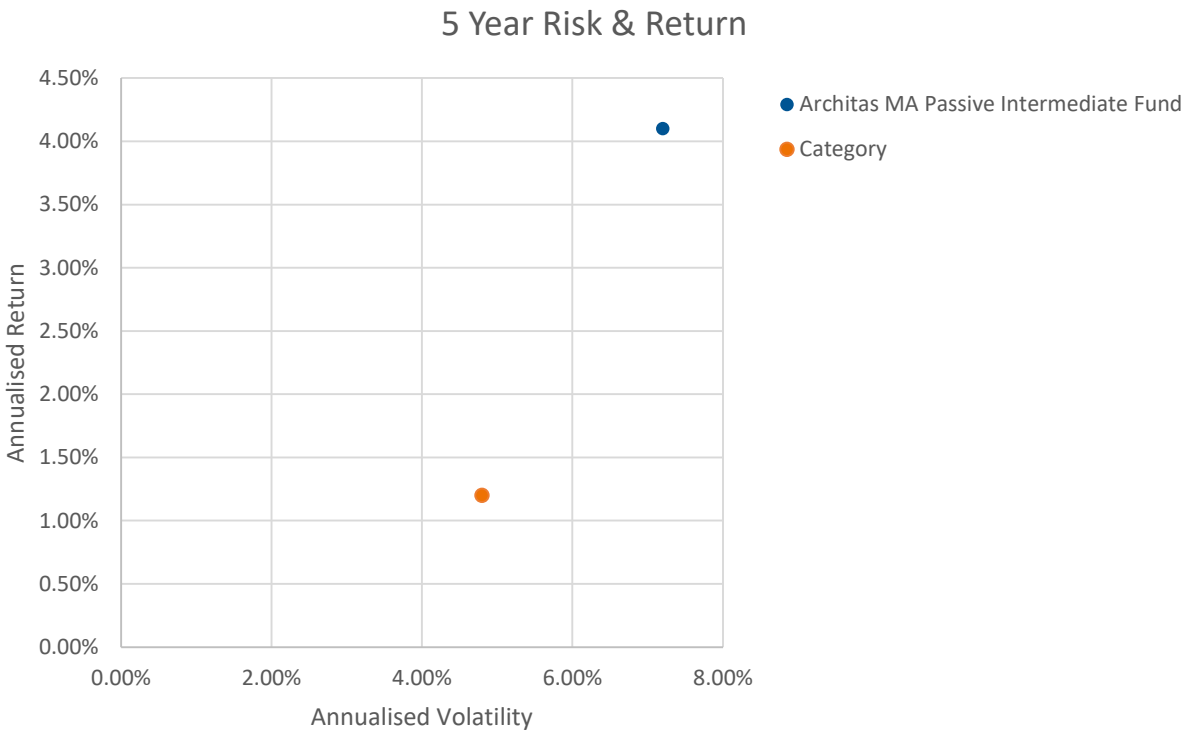
Risk monitoring and management follows a clearly defined schedule. The risk team monitors specific holding risk, liquidity and top down asset allocation on a daily basis, as well as underlying exposures on a look-through basis. The team also looks at statistical and qualitative outputs in order to identify potential risks, and flag these to the portfolio team.

The risk team is also tasked with ensuring that portfolio requirements and investment regulations are adhered to on a consistent basis. This is particularly important for this passive range of funds as the funds are required to be at the mid-point of their volatility bands (within predetermined tolerance limits).

The risk team's findings are more formally reviewed weekly. Zorza attends the monthly investment committee, chaired by CIO Jaime Arguello, and can raise questions on matters such as holdings and position sizes. We are also given to understand that he has veto power over fund selection. The monitoring of tracking errors and risk/return analysis are an integral feature of these meetings. The team also provides detailed performance attribution to the CIO and portfolio management team.

A full report is made to the Architas Board on a quarterly basis.

Risk and return profile



Research process

The strategic asset allocation, provided by Evalue and updated quarterly, with asset allocation and volatility ranges fixed. There is no tactical asset allocation in the passive fund range.

Each team member has research responsibility for a specific area and asset class, with the brief to seek out the 'best of breed' therein. The fund selection process blends quantitative and qualitative analysis, is clearly defined, and would seem to be consistently applied.

The Passive range is truly unfettered (with only around 5% of the range invested in AXA IM funds) allowing the managers complete freedom to pick the funds they believe are best.

Using Morningstar data, the analyst screens the asset class to identify potential opportunities. Liquidity screens also feature; typically funds below £100m in size are not considered, but this is not a hard and fast rule.

Key considerations with passive funds include the fund structure, the composition and calculation of the benchmark that it aims to replicate (its breadth, depth and usefulness), the replication methodology and its tracking error over time (to identify any deviation from benchmark).

Interviewing fund managers is an integral part of the process; normally there will be more than one visit before any recommendation is made. Thanks to its size, Architas has good access to fund managers. To date, it has never invested in an underlying fund without meeting the fund manager first. The analyst forms a qualitative assessment of the team, process and fund performance. Team-wise, he/she looks at the size, quality and experience of the investment team running the fund, though interestingly (and rather surprisingly), there is no explicit requirement for managers to demonstrate a previous track record on the asset class.

Resources available

Evalue, an external asset allocation tool, is key to the process as it is the reference point for the strategic asset allocation for the passive range of funds. It formulates volatility parameters for each fund appropriate to its risk/return characteristics.

The fund selection process utilises Morningstar data universes for its initial screening and proprietary screens and filters facilitate deeper analysis. Other systems available include Bloomberg Port (risk and scenario analysis, as well as performance attribution), Style Research and Morningstar portfolio performance attribution systems.

Architas also pay for research from Goldman Sachs and JP Morgan.

The investment process should be consistent and repeatable. Even with passive funds, the analyst will also look at the underlying assets of the fund to ensure he/she is comfortable with its composition. There is also an assessment of operational areas such as risk controls and risk management. Performance-wise, the fund being reviewed is required to provide attribution. Each area is then scored out of five and weighted to produce a composite score (also out of five); the fund must score at least three to go further in the process (but this by no means guarantees approval). The three attributes are not equally weighted; the team is considered the most important criterion.

The analyst then puts forward the investment case for the fund at the Fund Approval Forum, where it meets peer group challenge. The analyst can only submit ideas in his/her area of specialisation. Any approval decision must be unanimous; if not, CIO Jaime Arguello has the final decision-making power. Given the focused nature of portfolios, approved funds need to be high conviction ideas. Each analyst creates a list of approved funds which the portfolio manager can use in portfolio construction. The portfolio managers cannot invest in any fund that has not been approved by the forum.

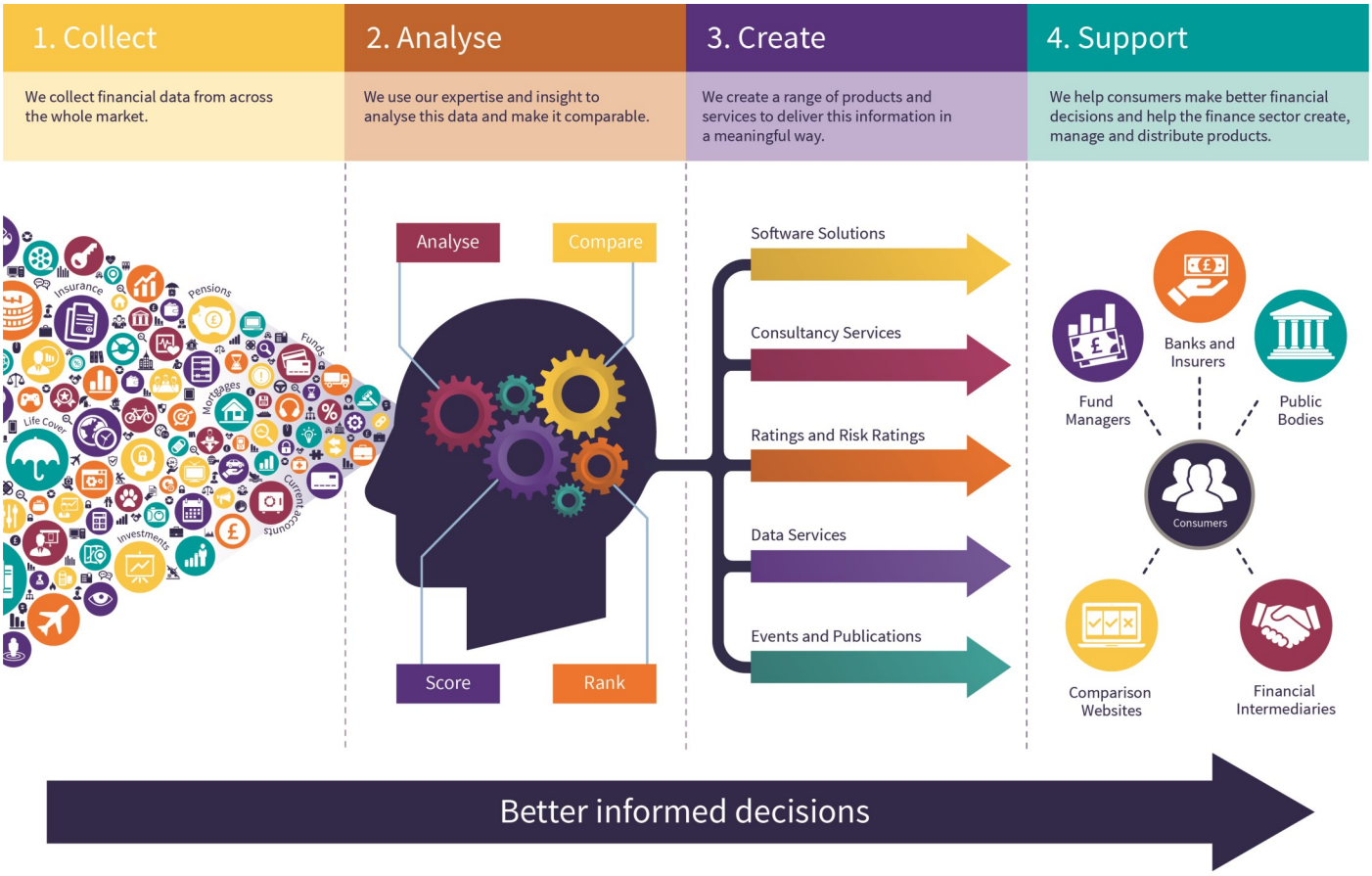
Funds are monitored on an ongoing basis, and at least quarterly for style drift. For passive funds in particular, the analyst keeps watch on benchmarks' composition. Funds are reviewed more formally at least twice a year. Throughout the process, there is ongoing dialogue between analyst and fund manager as required.

Glossary

Defaqto Diamond Rating	A quality rating based upon a range of key attributes, including performance, cost, size, and manager tenure.
Defaqto Risk Rating	A suitability rating that applies to solutions, which have been mapped and aligned to the ten Defaqto Risk Profiles.
Defaqto Income Risk Rating	A suitability rating that applies to solutions, which have been mapped and aligned to the four Defaqto Income Risk Profiles.
Launch Date	The launch date for the share class being reviewed.
Assets	Refers to the asset types that the fund managers uses, being either 'active' or 'passive'.
Approach	Refers to the management focus adopted by the manager.
Investment Association (IA) sector	The Investment Association peer group that the fund/s are classified within. See www.investmentassociation.org for details.
Morningstar Category	Funds are grouped into categories according to their actual investment style, not merely their stated investment objectives, nor their ability to generate a certain level of income. To ensure homogeneous groupings, Morningstar normally allocates funds to categories on the basis of their portfolio holdings. Several portfolios are taken into account to ensure that the fund´s real investment stance is taken into account. Source: Morningstar Inc.
Defaqto Diamond Rating Type	Created by Defaqto to determine the Defaqto Diamond Ratings.
Asset allocation chart	Created using Defaqto's 16 asset classes including 'other'.
Total returns chart	Displays the percentage return, over the specified period, compared to Morningstar category, with gross income reinvested.
Discrete returns chart	Based on 5 discrete 12 month periods (if available), working backwards from the stated month-end. Displays the percentage returns, compared to the Morningstar category, with gross income reinvested.
Risk-return chart	Displays the annualised standard deviation of daily log returns and the annualised percentage return of the solution, compared to the Morningstar category.
Drawdown and positive/negative months table	Displays the maximum peak to trough loss, within the period stated, using daily pricing data, together with the number of positive and negative months of performance, and the percentage fall in value in the worst month.
Fund size and fees	Displays assets under management (AUM), for the solution, together with a range of MIFID II compliant fees. It should be noted that, for technical reasons, negative transaction fees can occur. Its also possible that negative performance fees can be displayed and these represent fee rebates.
Historic income chart	If displayed, shows the net distribution history declared by the solution, on a £ per unit basis.
Yield table	If displayed, shows the current income yield, calculated on a trailing percentage basis, together with the distribution frequency.

Data source: Morningstar Inc. Please note that some solutions may have simulated/extended track records, in accordance with Morningstar's Extended Performance Methodology paper.

About Defaqto



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Our independent fund and product information helps banks, insurers and fund managers with designing and promoting their propositions. We analyse more than 41,000 financial products in the UK. These products change on a daily basis, and our customers need help with keeping track of this.

We have been doing this for over 20 years, and we have 60 analysts spending 400 hours a day monitoring the market. They ensure that the information we provide is accurate and up to date. Our experts have done all the hard work so that financial institutions and consumers can make better informed decisions

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