

Media

Company Update

June 22, 2018

(Maintain) **Buy**

Target Price (12M, W) **▲ 150,000**

Share Price (06/21/18, W) **116,100**

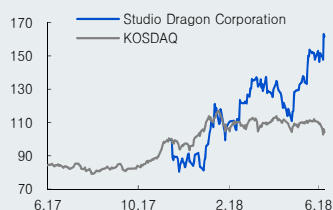
Expected Return **29%**

OP (18F, Wbn) 67
Consensus OP (18F, Wbn) 67

EPS Growth (18F, %) 74.2
Market EPS Growth (18F, %) 12.9
P/E (18F, x) 63.5
Market P/E (18F, x) 9.1
KOSDAQ 826.22

Market Cap (Wbn) 3,255
Shares Outstanding (mn) 28
Free Float (%) 23.9
Foreign Ownership (%) 1.9
Beta (12M) 0.73
52-Week Low 57,800
52-Week High 117,100

(%) **1M 6M 12M**
Absolute 20.7 86.7 0.0
Relative 27.5 67.2 0.0



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Studio Dragon Corporation

(253450 KQ)

Mr. Sunshine is coming to Netflix

Netflix deal for *Mr. Sunshine* worth at least W28.7bn

After yesterday's market close, Studio Dragon announced in a regulatory filing that it signed a licensing contract with Netflix for its upcoming drama *Mr. Sunshine*. While the exact size of the deal (recognized as licensing revenue) was not revealed, we believe the deal is worth at least W28.7bn, given disclosure regulations. At the low end, the figure represents more than 70% of the drama's production costs and a sharp increase from the prices of previous Netflix deals (50% of production costs). Given the rising value of content worldwide, we think it is likely the latest contract is worth more than the low-end figure.

Considering that the latest deal does not include China, we could see additional licensing sales once exports to China resume. Following the recent IPO of iQiyi, the battle for content among China's three biggest OTTs has been intensifying. There is also significant pent-up demand for Korean content. While the timing is not certain, we see potential for a deal worth over W10bn within the next year.

Raising earnings estimates and target price; risks skew to upside

We expect higher pricing of large-scale content to generate earnings leverage. We believe price gains are the result of: 1) the execution of a content business model (i.e., expanding beyond domestic ad sales to global content rights); 2) the emergence of streaming giants (Netflix, Amazon, etc.); and 3) the scarcity of Korean big-budget content. As such factors continue to play out and drive industry changes, we expect the rise in prices to continue going forward.

Reflecting higher pricing and earnings leverage, we are raising our earnings estimates and target price (from W110,000 to W150,000). We forecast operating profit at W67.3bn (+104% YoY) for 2018 and W116.1bn (+73% YoY) for 2019. Our estimates assume: 1) licensing sales of one tentpole title (with additional upside) to Netflix per quarter; 2) resumption of China exports in 1Q19; and 3) the production of two originals in 2019.

Content key to platform competitiveness; rising bid for 21st Century Fox is telling

As the use of content expands across borders, the value of content companies is skyrocketing. The content market, which previously was fragmented by country and relied heavily on broadcast ad sales, is becoming more globally integrated (and larger in size) and turning to direct licensing to streaming services. The rising value of content companies is illustrated by the ongoing bidding war between Comcast and Disney for 21st Century Fox's assets (bid price went up from US\$52.4bn to US\$65bn and then US\$71.3bn). We also highlight the record-breaking share prices of video platforms Netflix (W194tr) and iQiyi (W36tr). In this context, we think the share price rally of Studio Dragon, one of the top Asian content production companies, is well-deserved.

Seller's market; launch of CJ ENM also positive

We believe the content industry will remain seller-driven for years to come, given the aggressive expansion of platforms and the significant time it takes to build content competitiveness. We think Studio Dragon's latest Netflix deal also validates the scarcity value of Korean-made "blockbusters." Companies with strong production capabilities and blockbuster-level financial ability are best-positioned in today's environment. Against this backdrop, Studio Dragon's parent company (CJ ENM) is set to become a massive player valued at well over W5tr through its latest merger (July 1st). Having a company with formidable assets and stable profits as not only its parent but also its largest customer is undeniably positive to Studio Dragon. We believe Studio Dragon will gain more room for programming and financing, leading to increased blockbuster productions and earnings leverage.

FY(Dec.)	12/14	12/15	12/16	12/17	12/18F	12/19F
Revenue (Wbn)	0	0	196	287	380	528
OP (Wbn)	0	0	0	33	67	116
OP margin (%)	-	-	0.0	11.5	17.6	22.0
NP (Wbn)	0	0	0	24	51	90
EPS (W)	0	0	0	1,050	1,829	3,195
ROE (%)	0.0	0.0	0.0	9.5	13.0	19.3
P/E (x)	-	-	-	61.9	63.5	36.3
P/B (x)	-	-	-	4.9	7.8	6.4
Dividend yield (%)	-	-	-	0.0	0.0	0.0

Note: All figures are based on consolidated K-IFRS; NP refers to net profit attributable to controlling interests
Source: Company data, Mirae Asset Daewoo Research estimates

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Upward revisions to earnings forecasts and our target price

The lower bound of the license contract value for *Mr. Sunshine*, the most eagerly anticipated drama of 2018, has been confirmed. We have raised our 2018 and 2019 operating profit forecasts for Studio Dragon to W67.3bn (+104% YoY) and W116.1bn (+73% YoY), respectively, to reflect the potential for increases in both content selling prices and operating leverage. Our key earnings forecast assumptions are as follows:

- 1) Programming: Increase in the number of titles aired (quantity; 26 in 2018, 30 in 2019) to drive up both production costs and license fees from broadcasting networks (prices)
- 2) Sales: Simultaneous increases in the number of titles aired, customers (Q), as well as selling prices (P)
 - Licensing sales of *Mr. Sunshine* (slated to premiere in 3Q18) and *Memories of the Alhambra* (4Q), as well as one tentpole title (with additional upside) to Netflix per quarter (2019).
 - With licensing sales to China expected to resume in 1Q19, we conservatively estimate China-bound licensing sales value at just 80% of Netflix-bound sales value, and did not incorporate sales of existing titles (e.g., *Goblin*, *The Legend of the Blue Sea*)
- 3) Original content production: Studio Dragon will produce one original-content title for Netflix in 1H and 2H19 each
- 4) Upside catalysts for shares
 - Additional increases in content selling prices (W10bn-level for each tentpole title and W5bn for other titles)
 - Additional original content production for global OTTs (e.g., Netflix and Chinese OTTs)
 - Lump-sum recognition of China-bound sales of existing titles (upon confirmation of China-bound content sale resumption)
 - Increases in selling prices of titles broadcast simultaneously in Korea and China (currently estimated at 80% the prices for those offered to Netflix)

Table 1. Target price calculation

(Wbn, x)

	2019F	Note
EBITDA	184	
Target EV/EBITDA	22.2	Based on China peers
Fair EV	4,095	
Net debt (net cash)	-34.6	
Fair market cap	4,130	
Target price (W)	147,306	
Target price (W)	150,000	Rounded
Upside potential (%)	29.2	

Source: Mirae Asset Daewoo Research

Table 2. Major TV drama lineups for 2H18: Focus on tentpoles slated for release in 2H

Title	Genre	No. of episodes	Air date	Air date	Distributor	Writer	Stars
What's Wrong with Secretary Kim	Romance/drama	16	June-July	Wed/Thurs	tvN	Jung Eun-young	Park Seo-joon, Park Min-young
Life On Mars	Crime	16	June-July	Sat/Sun	OCN	Lee Dae-il	Jung Kyung-ho, Park Sung-woong, Go Ah-sung
Mr. Sunshine	Romance/history	24	July-Sept.	Sat/Sun	tvN	Kim Eun-sook	Lee Byung-hun, Kim Tae-ri
Wife That I know	Drama	16	Aug.-Sept.	Wed/Thurs	tvN	Yang Hui-seung	Ji Sung, Han Ji-min
Player	Drama	-	Aug.~	-	OCN	Shin Jae-hyeong	Song Seung-hun, Jung Soo Jung, Lee Si-eon
Dear Husband of 100 Days	Drama	-	Sept.~	-	tvN	No Ji-sul	Do Kyung-soo, Nam Ji-hyun
The Guest (tentative title)	-	-	Sept.~	-	OCN	Seo Jae-won, Kwon So-ra	Jung Eun-chae, Kim Jae-wook
Memories of the Alhambra	Drama	16	Nov.~	Sat/Sun	tvN	Song Jae-jeong	Hyun Bin, Park Shin-hye
Hundred Million Stars From the Sky	Drama	-	2H18	-	tvN	Song Hye-jin	Seo In-guk, Jung So-min

Source: Mirae Asset Daewoo Research

Table 3. Earnings and forecasts

(Wbn, %, no)

	1Q17	2Q17	3Q17	4Q17	1Q18	2Q18F	3Q18F	4Q18F	2017	2018F	2019F
Revenue	75	62	77	72	80	73	129	99	287	380	528
Programming	26	24	42	39	41	32	44	38	131	154	173
Licensing	36	26	23	26	32	32	69	48	112	181	244
Other	13	12	12	7	7	10	15	13	44	45	51
Original production contracting	0	0	0	0	0	0	0	0	0	0	60
Costs	59	50	67	64	66	61	92	77	240	295	390
Production costs (excl. originals)	24	25	36	39	39	32	48	39	125	157	181
Commission fees	7	5	5	5	6	6	14	10	22	36	40
Depreciation expenses on tangible/intangible assets	9	9	10	11	12	14	14	16	39	56	68
Other	19	10	16	9	8	9	16	13	54	46	54
Production costs for originals	0	0	0	0	0	0	0	0	0	0	48
SG&A	3	3	4	4	3	4	6	5	14	18	21
EBITDA	23	18	17	15	23	22	45	33	72	124	184
Operating profit	14	9	7	3	11	9	31	17	33	67	116
OP margin	18.5	14.3	8.6	4.8	13.3	11.9	24.0	17.3	11.5	17.7	22.0
Pretax profit	13	9	6	2	11	8	31	17	30	67	115
Net profit	13	3	6	2	8	7	24	13	24	51	90
Net margin	17.8	4.5	7.3	2.8	9.8	8.9	18.5	13.3	8.3	13.5	17.0
YoY											
Revenue	-	-	-	-	6.0	17.9	65.9	37.3	46.7	32.6	38.7
Programming	-	-	-	-	54.5	31.8	5.7	-3.6	49.5	17.5	12.1
Licensing	-	-	-	-	-12.0	20.7	196.5	87.3	48.3	62.0	34.7
Other	-	-	-	-	-43.4	-17.4	23.5	80.2	35.3	2.8	12.7
EBITDA	-	-	-	-	2.1	23.4	172.0	126.1	-	71.3	49.4
Operating profit	-	-	-	-	-23.7	-2.1	363.6	393.3	56.1	103.5	72.5
Net profit	-	-	-	-	-41.3	133.5	320.3	556.1	83.8	115.1	74.6
Major assumptions											
No. of titles aired	4.0	4.5	6.5	6.5	7.0	6.0	6.5	6.5	21.5	26.0	30.0
No. of titles licensed to Netflix	0.0	1.0	1.0	1.1	2.0	0.5	1.0	1.0	3.1	4.5	6.0

Source: Mirae Asset Daewoo Research

Table 4. Earnings forecast revisions

(Wbn %, %p)

	Previous		Revised		Change		Notes
	18F	19F	18F	19F	18F	19F	
Revenue	361	480	380	528	5.5	9.9	- Reflected higher drama ASP (from 2018F) and China-bound sales resumption (from 2019F)
Operating profit	59	72	67	116	14.2	61.8	
Net profit	45	55	51	90	14.5	63.0	
OP margin	16.3	14.9	17.7	22.0	1.3	7.1	
Net margin	12.4	11.5	13.5	17.0	1.1	5.5	

Note: All figures are based on consolidated K-IFRS; NP refers to net profit attributable to controlling interests

Source: Mirae Asset Daewoo Research

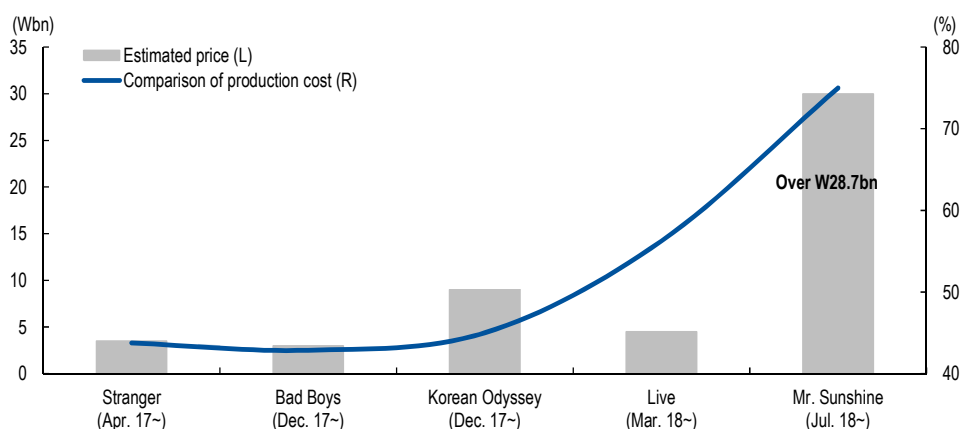
Netflix deal for *Mr. Sunshine* worth at least W28.7bn

After yesterday's market close, Studio Dragon announced in a regulatory filing that it had signed a 10-year licensing contract with Netflix for its upcoming drama, *Mr. Sunshine* (with holdback periods differing by country). While the exact size of the deal (recognized as licensing revenue) was not revealed, we believe the deal is worth at least W28.7bn, in light of the required disclosures. At the low end, the figure represents more than 70% of the drama's production costs and a sharp increase from the prices of previous Netflix deals (50% of production costs). Given the rising value of content worldwide, we think it is likely that the latest contract is worth more than the low-end figure.

Considering that the latest deal does not include China, we could see additional licensing sales once exports to China resume. Following the recent IPO of iQiyi, the battle for content among China's three biggest OTTs has been intensifying. In addition, there is also significant pent-up demand for Korean content. While the timing may vary, we see potential for an over-W10bn deal within the next year.

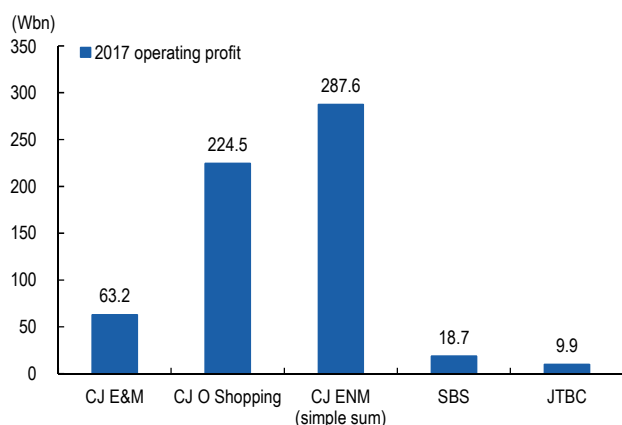
Our estimated value of W28.7bn represents over 70% of production costs for *Mr. Sunshine*, and is higher than the levels of previous deals. Indeed, Studio Dragon's past deals with Netflix (e.g., *Stranger*, *A Korean Odyssey*, *Live*, etc.) were estimated at W4-9bn each (about 50% of production costs). The company can be expected to see greater earnings leverage from the sharp increase in the licensing contract value. We believe that the growth in content licensing prices is attributable to: 1) the shift in the company's business model from domestic advertising to global sales; 2) the emergence of global media platform giants (e.g., Netflix, Amazon, etc.); and 3) the rarity of blockbuster Korean dramas.

Figure 1. Netflix-bound content prices on the rise



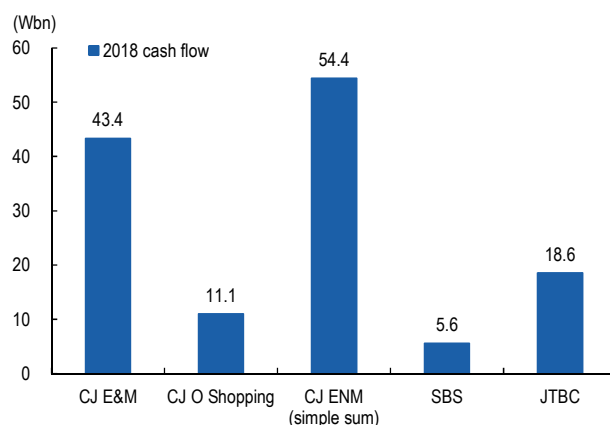
Note: The terms of licensing deals (e.g., country, exclusivity, holdback, etc.) differ by contract
Source: Mirae Asset Daewoo Research

Figure 2. OP of CJ and other major broadcasters

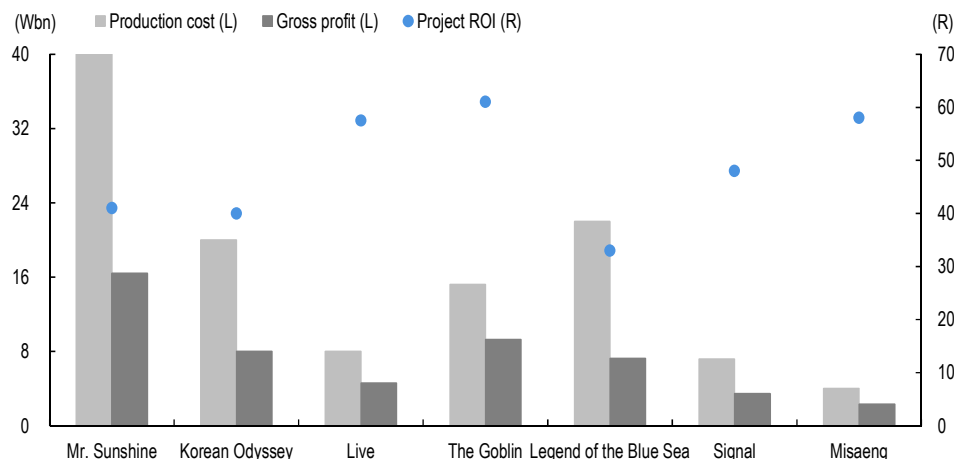


Source: Each company, Mirae Asset Daewoo Research

Figure 3. Cash flow of CJ and other major broadcasters

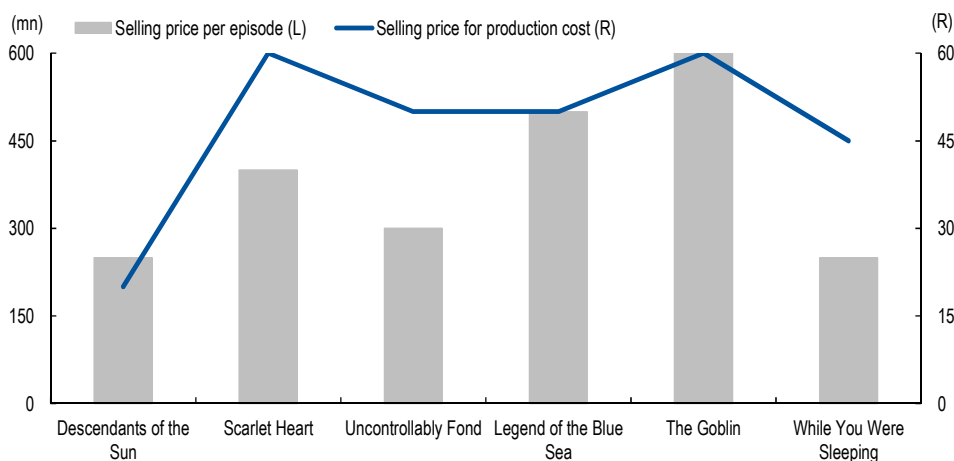


Source: Each company, Mirae Asset Daewoo Research

Figure 4. Estimated gains from major dramas

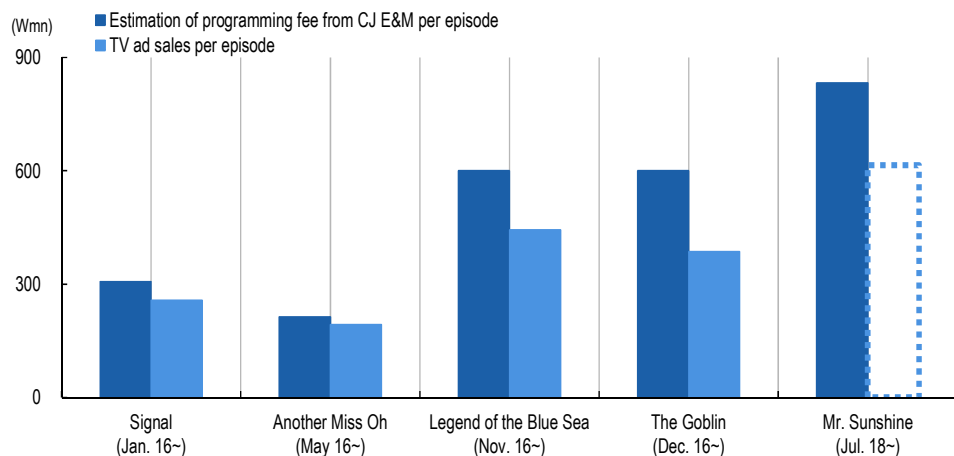
Note: Some data are based on media reports and our estimates

Source: Company data, Mirae Asset Daewoo Research

Figure 5. China-bound content export prices are also correlated with production costs

Note: Production costs and sales prices are based on media reports and our estimates.

Source: Media reports, Mirae Asset Daewoo Research

Figure 6. Studio Dragon is capable of producing large-scale content that can generate greater revenue from licensing than from TV ads

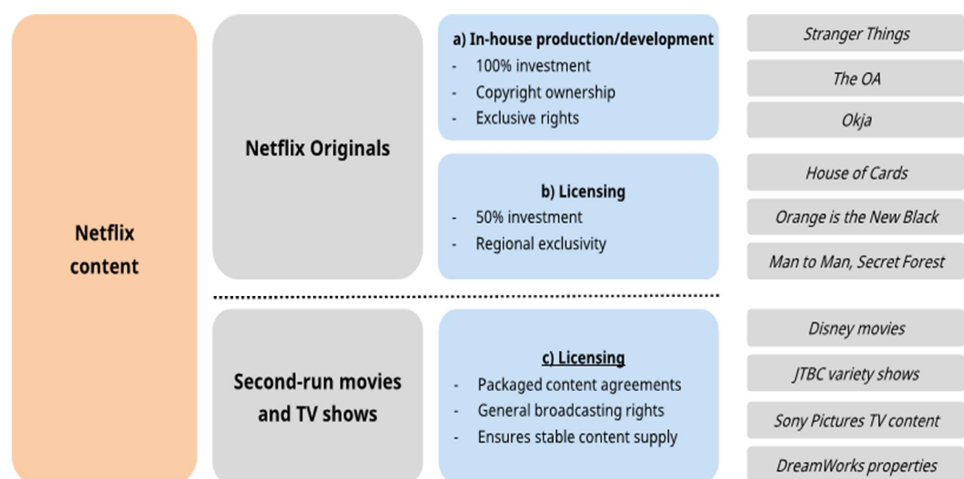
Note: Production costs are based on media reports; TV ad revenue is based on our estimates

Source: CJ E&M, Mirae Asset Daewoo Research

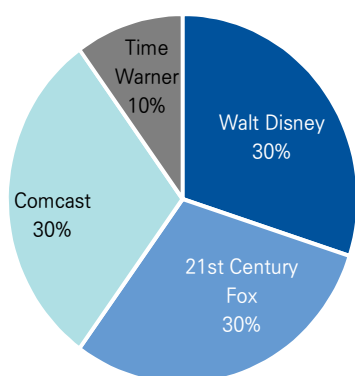
Table 4. Co-production expected with global firms

	Company	Plans
Asia	Amazon	Distribute TV dramas in Japan
	True CJ Creations	Remake of TV drama based on IP (targeting the Thai market)
	CJ Blue	Remake of TV drama based on IP (targeting the Vietnamese market)
	Other	Sign JV and M&A deals with local producers
North America	Warner Bros.	Signed co-production MOU Co-produce global TV dramas
	Netflix	Distribute new dramas <i>Black</i> , <i>A Korean Odyssey</i> and <i>Live</i> Co-produce global TV dramas
	AMC	Co-produce global TV dramas
	iTV	Co-produce global TV dramas
	Other	Sign JV and M&A deals with local producers

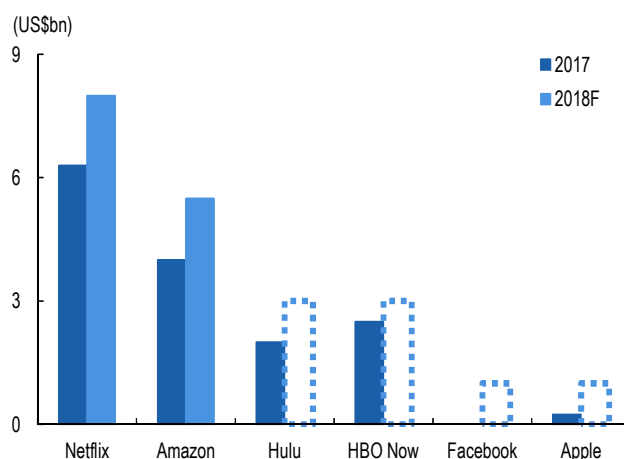
Source: Company data, Mirae Asset Daewoo Research

Figure 7. Studio Dragon to expand original content production for global platforms

Source: Mirae Asset Daewoo Research

Figure 8. Hulu ownership breakdown: Walt Disney to beef up Hulu

Source: Each company, Mirae Asset Daewoo Research

Figure 9. Global OTT content players are expanding content investments

Source: Each company, Mirae Asset Daewoo Research

Content is key to platform competitiveness; rising bid for 21st Century Fox is telling

The content market, which previously was fragmented by country and relied heavily on broadcast ad sales, is becoming more globally integrated (and larger in size) and turning to direct licensing to streaming services. As the use of content expands across borders, the value of content companies is skyrocketing. The rising value of content companies is illustrated by: 1) the ongoing bidding war between Comcast and Disney for 21st Century Fox's assets (bid price went up from US\$52.4bn to US\$65bn, and then US\$71.3bn); 2) a US federal judge's recent approval for AT&T's acquisition of Time Warner; and 3) Verizon's plan to acquire CBS. We also highlight the record-breaking share prices of video platforms Netflix (W194tr) and iQiyi (W36tr). In this context, we think the share price rally of Studio Dragon, one of the top Asian content production companies, is well-deserved.

Table 5. Bidding war between Comcast and Disney for 21st Century Fox's assets

Timeline	Details
11/17	After negotiations with Disney started in August 2017, Verizon and Comcast also joined the competition Comcast proposed a deal to acquire 21st Century Fox's assets for US\$27.1bn (vs. Disney's proposed acquisition price of US\$23.3bn); however, negotiations with Comcast broke down, due to concerns over monopoly regulations stemming from the Justice Department's lawsuit against the merger between AT&T and Time Warner Verizon proposed an acquisition deal at market price; negotiations fell apart
12/17	Comcast reconsidered a bid for the acquisition, but decided to withdraw from the competition
End-2017	Disney proposed an acquisition price of US\$52.4bn
4/19/18	21st Century Fox decided to sell its media business to Disney, in light of monopoly regulations and a positive outlook for Disney shares
6/13/18	Comcast reconsidered the acquisition and proposed a bid price of US\$65bn in cash
6/19/18	Disney announced its plan to propose a higher bid price than that of Comcast
6/20/18	Disney proposed a bid price of US\$71.3bn

Source: Mirae Asset Daewoo Research

Figure 10. Likelihood of AT&T acquiring Time Warner has increased (CNN report from June 18th)



AT&T-Time Warner deal approved

The decision allowing AT&T to buy Time Warner could reshape the media industry. It's unknown if government will appeal. CNN's Jessica Schneider reports. Source: CNNMoney



Source: CNN, Mirae Asset Daewoo Research

Studio Dragon Corporation (253450 KQ/Buy/TP: W150,000)

Comprehensive Income Statement (Summarized)

(Wbn)	12/16	12/17	12/18F	12/19F
Revenue	196	287	380	528
Cost of Sales	100	240	295	390
Gross Profit	96	47	85	138
SG&A Expenses	0	14	18	21
Operating Profit (Adj)	0	33	67	116
Operating Profit	0	33	67	116
Non-Operating Profit	-17	-3	0	-1
Net Financial Income	-1	-1	4	5
Net Gain from Inv in Associates	0	0	0	0
Pretax Profit	-17	30	67	115
Income Tax	0	6	15	25
Profit from Continuing Operations	8	24	51	90
Profit from Discontinued Operations	0	0	0	0
Net Profit	0	24	51	90
Controlling Interests	0	24	51	90
Non-Controlling Interests	0	0	0	0
Total Comprehensive Profit	8	24	51	90
Controlling Interests	8	24	51	90
Non-Controlling Interests	0	0	0	0
EBITDA	22	74	123	184
FCF (Free Cash Flow)	-13	-7	88	143
EBITDA Margin (%)	11.2	25.8	32.4	34.8
Operating Profit Margin (%)	0.0	11.5	17.6	22.0
Net Profit Margin (%)	0.0	8.4	13.4	17.0

Statement of Financial Condition (Summarized)

(Wbn)	12/16	12/17	12/18F	12/19F
Current Assets	81	290	317	438
Cash and Cash Equivalents	12	51	78	51
AR & Other Receivables	39	55	55	90
Inventories	0	1	1	2
Other Current Assets	30	183	183	295
Non-Current Assets	161	170	184	203
Investments in Associates	0	0	0	0
Property, Plant and Equipment	1	1	1	1
Intangible Assets	124	128	139	156
Total Assets	242	459	501	641
Current Liabilities	84	91	81	131
AP & Other Payables	20	32	32	51
Short-Term Financial Liabilities	8	10	0	0
Other Current Liabilities	56	49	49	80
Non-Current Liabilities	21	0	0	1
Long-Term Financial Liabilities	20	0	0	0
Other Non-Current Liabilities	1	0	0	1
Total Liabilities	106	91	81	131
Controlling Interests	136	368	420	509
Capital Stock	11	14	14	14
Capital Surplus	115	320	320	320
Retained Earnings	8	32	83	173
Non-Controlling Interests	0	0	0	0
Stockholders' Equity	136	368	420	509

Cash Flows (Summarized)

(Wbn)	12/16	12/17	12/18F	12/19F
Cash Flows from Op Activities	-12	-7	88	143
Net Profit	0	24	51	90
Non-Cash Income and Expense	25	46	69	89
Depreciation	0	0	0	0
Amortization	22	41	56	68
Others	3	5	13	21
Chg in Working Capital	-46	-73	-17	-10
Chg in AR & Other Receivables	-27	-14	0	-34
Chg in Inventories	0	-2	0	-1
Chg in AP & Other Payables	11	9	-2	4
Income Tax Paid	-2	-10	-14	-25
Cash Flows from Inv Activities	-70	-141	-51	-170
Chg in PP&E	-1	0	0	0
Chg in Intangible Assets	0	0	-55	-85
Chg in Financial Assets	-2	-142	0	-90
Others	-67	1	4	5
Cash Flows from Fin Activities	93	188	-10	0
Chg in Financial Liabilities	28	-18	-10	0
Chg in Equity	126	208	0	0
Dividends Paid	0	0	0	0
Others	-61	-2	0	0
Increase (Decrease) in Cash	12	40	27	-27
Beginning Balance	0	12	51	78
Ending Balance	12	51	78	51

Source: Company data, Mirae Asset Daewoo Research estimates

Forecasts/Valuations (Summarized)

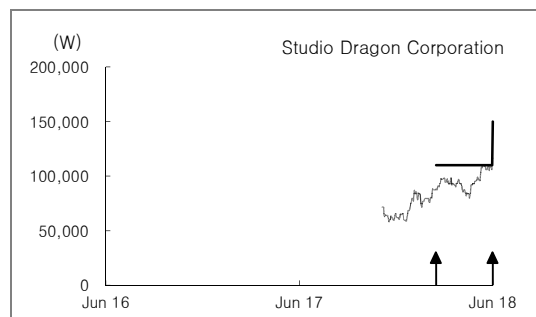
	12/16	12/17	12/18F	12/19F
P/E (x)	-	61.9	63.5	36.3
P/CF (x)	-	21.2	27.2	18.3
P/B (x)	-	4.9	7.8	6.4
EV/EBITDA (x)	-	22.1	24.6	16.1
EPS (W)	0	1,050	1,829	3,195
CFPS (W)	1,735	3,068	4,276	6,359
BPS (W)	6,176	13,141	14,977	18,172
DPS (W)	0	0	0	0
Payout ratio (%)	0.0	0.0	0.0	0.0
Dividend Yield (%)	-	0.0	0.0	0.0
Revenue Growth (%)	-	46.4	32.4	38.9
EBITDA Growth (%)	-	236.4	66.2	49.6
Operating Profit Growth (%)	-	-	103.0	73.1
EPS Growth (%)	-	-	74.2	74.7
Accounts Receivable Turnover (x)	5.3	6.2	6.9	7.3
Inventory Turnover (x)	0.0	443.0	293.8	310.8
Accounts Payable Turnover (x)	17.3	40.5	48.7	49.1
ROA (%)	0.0	6.8	10.7	15.7
ROE (%)	0.0	9.5	13.0	19.3
ROIC (%)	0.0	15.6	27.3	43.3
Liability to Equity Ratio (%)	77.8	24.7	19.3	25.8
Current Ratio (%)	96.4	319.6	392.4	334.4
Net Debt to Equity Ratio (%)	12.1	-49.4	-52.2	-54.8
Interest Coverage Ratio (x)	0.0	19.0	1,378.0	9,582.5

APPENDIX 1

Important Disclosures & Disclaimers

2-Year Rating and Target Price History

Company (Code)	Date	Rating	Target Price
Studio Dragon Corporation (253450)	06/22/2018	Buy	150,000
	03/06/2018	Buy	110,000



Stock Ratings

Buy	: Relative performance of 20% or greater
Trading Buy	: Relative performance of 10% or greater, but with volatility
Hold	: Relative performance of -10% and 10%
Sell	: Relative performance of -10%

Industry Ratings

Overweight	: Fundamentals are favorable or improving
Neutral	: Fundamentals are steady without any material changes
Underweight	: Fundamentals are unfavorable or worsening

Ratings and Target Price History (Share price (—), Target price (—), Not covered (—), Buy (▲), Trading Buy (■), Hold (●), Sell (◆))

* Our investment rating is a guide to the relative return of the stock versus the market over the next 12 months.

* Although it is not part of the official ratings at Mirae Asset Daewoo Co., Ltd., we may call a trading opportunity in case there is a technical or short-term material development.

* The target price was determined by the research analyst through valuation methods discussed in this report, in part based on the analyst's estimate of future earnings.

* The achievement of the target price may be impeded by risks related to the subject securities and companies, as well as general market and economic conditions.

Equity Ratings Distribution & Investment Banking Services

	Buy	Trading Buy	Hold	Sell
Equity Ratings Distribution	74.13%	15.92%	9.95%	0.00%
Investment Banking Services	75.00%	11.11%	13.89%	0.00%

* Based on recommendations in the last 12-months (as of March 31, 2018)

Disclosures

We managed the IPO of Studio Dragon Corporation with one year.

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