

Studio Dragon (253450 KS)

Shares on a rebound, with reason

BUY (Maintain)

CP (Sep. 11)	KRW70,200
TP (6 months)	KRW93,000
Upside	32.5%

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KOSPI	2,049.20p
KOSDAQ	630.37p
Market cap	KRW1,972.3bn/USD1,730.1mn
Par value	KRW500
Outstanding shares	28.1mn
Free float	7.1mn (25.2%)
52-week high/low	KRW116,300/KRW 54,000
60-day avg. trading volume	113,714shrs
60-day avg. turnover	KRW7,375mn
Foreign ownership	2.53%
Major shareholders	
	CJ ENM and 5 others 74.37%
Absolute performance	3M -2.0%
	6M -23.9%
	12M -33.8%
Relative performance	3M 13.4%
to KOSDAQ	6M -10.8%
	12M -13.8%

◆ 3Q19 consolidated OP forecast at KRW10bn (-53.3% YoY)

◆ Standing out among China plays

◆ Retain BUY and raise target price by 9.4% to KRW93,000

3Q19 consolidated OP forecast at KRW10bn (-53.3% YoY)

Our 3Q19 earnings forecasts for Studio Dragon remain unchanged at consolidated sales of KRW135bn (+9.2% YoY) and operating profit of KRW10bn (-53.3% YoY). We believe a YoY decline in operating profit is inevitable in 3Q19 with the comparison base significantly raised by the success of the Mr. Sunshine series in 3Q18. In 4Q19, consolidated operating profit should jump to KRW14.9bn (+1,475% YoY) on seasonal demand for VOD (video on demand).

Standing out among China plays

China is still a key factor for Studio Dragon as the company's profitability would surge once the Chinese government relaxes restrictions on Korean media content. Due to the absence of China sales, market focus turned to the decline in operating profit margin from the rise in production costs this year. Instead of waiting around for an upturn in China sales, Studio Dragon has been preparing for expansion into the bigger market in the Americas.

For Studio Dragon shares to rally further, we believe the company needs to secure original drama production deals in the Americas from major platforms other than Netflix (refer to our report on September 2). Negotiations are currently underway with various platforms such as Apple and order intake is expected to start within the remainder of 2019 at the earliest. Once the company seals new deals, Studio Dragon should take another step up from its current status as a key beneficiary of Netflix's content shortages to a major beneficiary of intensifying content competition among global platforms. We thus believe Studio Dragon deserves to trade at higher valuation multiples vs. other China plays.

Earnings visibility is also clearer for 2020, with operating profit expected to rise more than 50% YoY to KRW70bn-75bn even in the absence of an upturn in China earnings. Earnings from Arthdal Chronicles Season 2, The King: Eternal Monarch, Signal Season 2, and at least three original drama production deals should emerge as key drivers of growth going forward.

Retain BUY and raise target price by 9.4% to KRW93,000

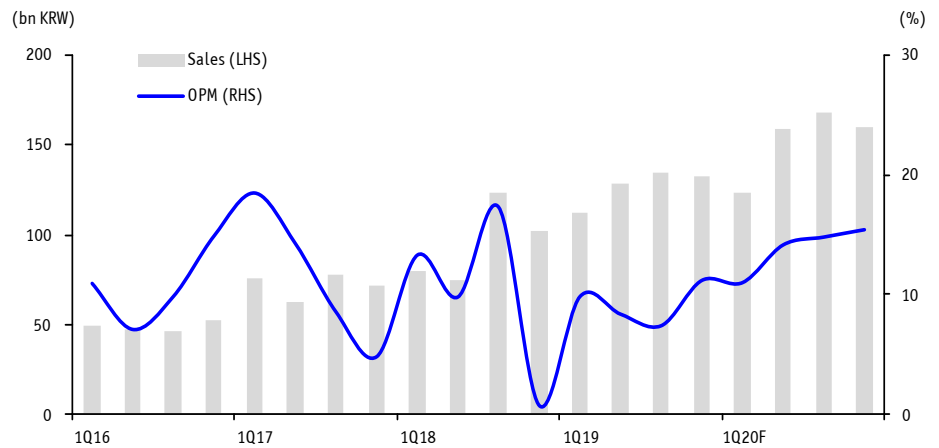
We raise our target price for Studio Dragon from KRW85,000 to KRW93,000. Our revised target is based on 2020F operating profit of KRW75bn excluding China earnings (net profit of KRW64bn) and a target PER of 40x. We maintain our BUY rating in light of: 1) forecasts for 20%-level YoY top-line growth in 2020; 2) expectations for over-50% YoY growth in operating profit in 2020; and 3) lowered share valuations. All in all, we expect Studio Dragon shares to continue on a steady uptrend in the near term.

Year to December	Sales (bn KRW)	OP (bn KRW)	Pre-tax (bn KRW)	NP (bn KRW)	EPS (KRW)	Growth (%)	BPS (KRW)	PER (x)	EV/EBITDA (x)	PBR (x)	ROE (%)	Net debt ratio (%)
2017	286.8	33.0	30.3	23.8	1,050	84.5	13,141	61.9	22.1	4.9	9.5	(49.5)
2018	379.6	39.9	45.6	35.8	1,278	21.7	14,305	72.3	21.2	6.5	9.3	(38.2)
2019F	507.8	46.7	55.8	41.7	1,486	16.3	15,791	47.2	7.9	4.4	9.9	(43.4)
2020F	609.7	85.8	96.7	73.5	2,620	76.3	18,411	26.8	6.6	3.8	15.3	(47.9)
2021F	688.4	110.8	122.8	93.4	3,328	27.0	21,739	21.1	5.7	3.2	16.6	(53.6)

Source: Company data, Shinhan Investment Corp. / Note: TB = turn black, TR = turn red, RR = remain red

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Sales and operating profit margin



Source: Company data, Shinhan Investment Corp.

Earnings trend and outlook (K-IFRS consolidated)

(bn KRW)	1Q18	2Q18	3Q18	4Q18	1Q19	2Q19	3Q19F	4Q19F	1Q20F	2Q20F	3Q20F	4Q20F	2017	2018	2019F	2020F
<Earnings forecasts>																
Total revenue	79.9	74.3	123.7	101.7	111.8	128.2	135.0	132.7	123.2	159.1	167.7	159.7	286.8	379.5	507.8	609.7
Production revenue	40.7	34.1	48.9	54.4	44.1	58.1	54.1	58.7	48.1	62.5	58.7	63.2	131.2	178.1	215.0	232.4
- Global platforms	0.0	0.0	0.0	0.0	0.0	0.0	1.0	1.5	0.0	2.3	2.3	2.3	0.0	0.0	2.5	6.8
Distribution revenue	32.1	28.8	63.4	37.8	56.2	60.3	59.4	53.5	63.2	70.6	82.0	70.5	111.8	162.1	229.4	286.3
Other (PPL) revenue	7.1	11.4	11.4	9.5	11.5	9.8	11.4	10.5	12.0	11.0	12.1	11.0	43.7	39.4	43.3	46.1
<Overseas operations>																
Overseas distribution revenue	22.7	16.5	46.2	24.8	42.6	42.2	39.1	38.1	48.5	50.0	58.2	52.9	67.2	110.2	162.0	209.7
Share in distribution revenue (%)	70.8	57.2	72.9	65.7	75.9	70.0	65.7	71.3	76.7	70.8	71.1	75.1	60.1	68.0	70.6	73.2
Japan	3.5	4.5	3.4	4.2	10.3	5.9	5.8	6.2	11.6	7.5	7.5	8.0	18.7	15.6	28.2	34.6
Asia including China	8.9	10.5	10.4	13.9	21.3	12.7	16.6	17.3	24.6	16.8	26.0	28.1	39.9	43.8	68.3	95.5
China	0.0	0.0	0.0	1.5	1.8	0.0	0.0	0.0	0.0	0.0	10.0	10.0	0.0	1.5	1.8	20.0
Americas	0.2	0.3	0.3	1.1	0.4	0.5	0.5	0.5	0.6	0.6	0.6	0.7	8.2	1.9	1.9	2.5
Others	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.2	0.1	0.1	0.1	0.4	0.4	0.4	0.5
COGS	66.2	63.7	98.9	95.2	96.8	112.8	120.9	111.9	105.1	131.0	137.9	128.3	239.8	324.0	442.5	502.4
SG&A	3.0	3.3	3.3	6.0	4.0	4.6	4.1	5.9	4.5	5.5	4.9	6.6	14.1	15.7	18.6	21.5
OP	10.7	7.3	21.5	0.4	11.0	10.8	10.0	14.9	13.6	22.6	24.9	24.7	33.0	39.9	46.7	85.8
Pre-tax profit	10.8	11.0	22.0	1.7	13.2	11.9	12.9	17.7	15.9	24.9	27.9	28.1	30.3	45.6	55.8	96.7
NP	7.9	8.9	17.3	1.7	9.2	7.3	10.6	14.5	12.1	18.9	21.2	21.3	23.8	35.8	41.7	73.5
<% YoY growth>																
Sales	6.0	19.6	59.6	41.5	40.0	72.6	9.2	30.0	10.2	24.1	24.2	20.3	46.7	32.3	33.7	20.1
OP	(23.7)	(17.8)	223.0	(87.3)	3.5	47.4	(53.3)	1,874.6	23.4	109.8	148.6	65.9	55.4	20.9	16.2	83.7
NP	(41.3)	216.8	206.3	(12.5)	17.2	(17.3)	(38.8)	605.0	30.9	157.6	99.8	46.9	83.3	50.2	15.4	76.3
<Margin, %>																
OPM	13.3	9.8	17.4	0.4	9.9	8.4	7.4	11.2	11.0	14.2	14.9	15.5	11.5	10.5	9.2	14.1
NPM	9.8	11.9	14.0	1.7	8.2	5.7	7.9	10.9	9.8	11.9	12.6	13.4	8.3	9.4	8.2	12.1

Source: Company data, Shinhan Investment Corp.

Note: Distribution rights revenue from Netflix included in overseas distribution revenue; China revenue assumed to be booked from 3Q20

PER valuation: Target price of KRW93,000

(bn KRW)	Value	(bn KRW)	Value	(bn KRW)	Value
2019F NP	41.7	2020F NP	73.5	2021F NP	93.4
EPS (KRW)	1,486	EPS (KRW)	2,620	EPS (KRW)	3,328
Target price (KRW)	52,000	Target price (KRW)	93,000	Target price (KRW)	117,000
Target PER (x)	35	Target PER (x)	35	Target PER (x)	35
		Current price	70,200		
		Current PER	26.8		

Source: Shinhan Investment Corp.

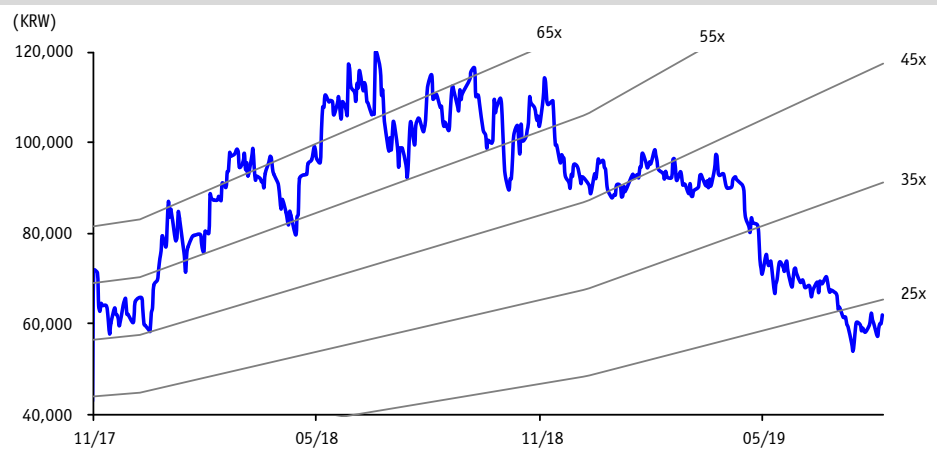
Note: Target PER based on a 20% discount to past 2-year average PER (low) in view of uncertainty in China earnings and decline in profitability from increasing production costs. Studio Dragon continues to see steady distribution revenue growth from Netflix and should be able to deliver sharp profit growth once China eases restrictions on Korean media content

PER trend

(x)	2017	2018	Past 2-year average
PER (high)	77.4	96.6	87.0
PER (low)	52.7	45.4	49.0
PER (average)	60.3	75.9	68.1

Source: Shinhan Investment Corp.

12-month forward PER band



Source: Bloomberg, Shinhan Investment Corp.

3Q19 forecast

(bn KRW)	3Q19F	2Q19	% QoQ	3Q18	% YoY	Previous	Consensus
Sales	135.0	128.2	5.3	123.7	9.2	135.0	133.0
OP	10.0	10.8	(7.4)	21.5	(53.3)	10.0	14.3
NP	10.6	7.3	45.2	17.3	(38.8)	10.6	12.7
OPM (%)	7.4	8.4		17.4		7.4	10.8
NPM (%)	7.9	5.7		14.0		7.9	9.5

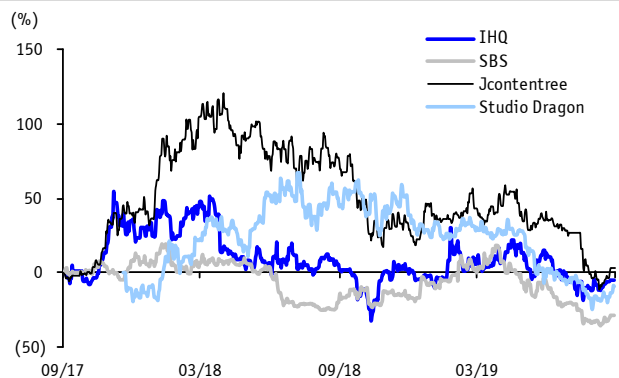
Source: Company data, FnGuide, Shinhan Investment Corp.

Peer group valuation

Ticker		253450 KS	036420 KS	003560 KS	160550 KS	DIS US	300027 CH	300133 CH
Company		Studio Dragon	Jcontentree	IHQ	NEW	Walt Disney	Huayi Brothers Media	Zhejiang Huace Film & TV
Market cap (bn KRW)		1,972.3	541.0	111.8	105.5	293,309.5	13.1	12.9
Sales	2018	379.6	511.3	161.2	161.2	65,093.4	644.7	959.5
(bn KRW)	2019F	502.3	568.6	170.7	170.7	82,860.3	704.1	879.3
	2020F	603.6	637.4	186.9	186.9	97,160.9	815.0	1,023.3
OP	2018	40.2	34.7	(10.6)	(10.6)	16,249.8	63.4	80.8
(bn KRW)	2019F	48.8	60.7	1.8	1.8	16,063.8	95.2	65.7
	2020F	74.0	69.3	8.7	8.7	18,322.9	124.0	104.6
OPM	2018	10.6	6.8	(6.6)	(6.6)	25.0	9.8	8.4
(%)	2019F	9.7	10.7	1.1	1.1	19.4	13.5	7.5
	2020F	12.3	10.9	4.7	4.7	18.9	15.2	10.2
NP	2018	36.2	23.1	(9.5)	(9.5)	11,477.9	(6.6)	39.0
(bn KRW)	2019F	40.7	29.8	4.0	4.0	11,372.2	64.4	56.8
	2020F	60.2	34.9	7.2	7.2	11,359.8	93.7	83.0
Sales growth	2018	32.4	21.6	70.5	70.5	3.2	(1.9)	9.7
(% YoY)	2019F	32.3	11.2	5.9	5.9	27.3	9.2	(8.4)
	2020F	20.2	12.1	9.5	9.5	17.3	15.7	16.4
EPS growth	2018	19.7	170.9	39.5	39.5	16.7	(110.4)	(59.4)
(% YoY)	2019F	12.5	7.5	(146.9)	(146.9)	(11.6)	(1,499.3)	80.7
	2020F	48.5	14.6	58.0	58.0	2.0	27.5	36.9
PER	2018	72.3	29.3	N/A	N/A	16.8	N/A	70.2
(x)	2019F	48.4	18.3	24.7	23.3	24.1	23.8	28.9
	2020F	32.6	16.0	15.6	14.8	23.6	18.6	21.1
PBR	2018	6.5	1.9	1.0	1.0	3.6	1.5	2.1
(x)	2019F	4.5	1.5	0.9	0.9	2.7	1.4	1.8
	2020F	4.0	1.4	0.9	0.8	2.4	1.4	1.7
EV/EBITDA	2018	21.1	9.7	N/A	N/A	11.1	37.1	30.4
(x)	2019F	12.5	8.0	22.0	20.3	18.1	21.0	28.5
	2020F	10.7	7.5	11.7	10.8	16.0	16.3	21.0
ROE	2018	9.4	9.3	(7.7)	(7.7)	23.3	(0.4)	3.4
(%)	2019F	9.6	8.8	4.7	4.7	14.2	4.8	4.6
	2020F	12.9	9.6	5.6	5.6	11.8	5.9	5.9

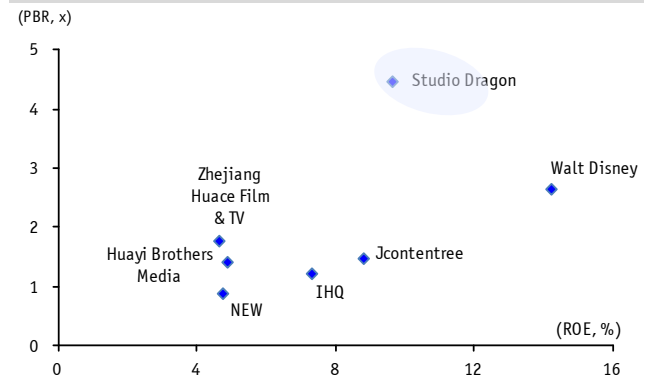
Source: Bloomberg, Shinhan Investment Corp.

Relative share performance vs. domestic peers



Source: Bloomberg, Shinhan Investment Corp.

2019F PBR and ROE vs. global peers



Source: Bloomberg, Shinhan Investment Corp.

Statement of financial position

Year to December (bn KRW)	2017	2018	2019F	2020F	2021F
Total assets	459.5	512.4	584.5	671.0	775.8
Current assets	289.8	247.2	305.5	390.5	487.5
Cash and equivalents	51.3	153.0	192.0	246.9	326.2
Accounts receivable	54.9	68.8	86.0	111.8	126.2
Inventories	1.3	0.6	0.8	0.9	1.0
Non-current assets	169.6	265.2	279.0	280.5	288.4
Tangible assets	1.1	1.0	0.8	0.8	0.6
Intangible assets	127.5	198.5	211.4	212.0	219.4
Investment assets	3.8	3.7	4.8	5.7	6.4
Other financial assets	0.0	0.0	0.0	0.0	0.0
Total liabilities	91.0	111.1	141.5	154.5	166.0
Current liabilities	90.7	108.2	138.4	151.2	162.6
Short-term borrowings	0.0	0.0	0.0	0.0	0.0
Accounts payable	6.1	19.6	20.5	21.5	22.5
Current portion of long-term debt	10.0	0.0	0.0	0.0	0.0
Non-current liabilities	0.3	2.9	3.1	3.3	3.5
Bonds	0.0	0.0	0.0	0.0	0.0
Long-term borrowings	0.0	2.1	2.1	2.1	2.1
Other financial liabilities	0.0	0.0	0.0	0.0	0.0
Total shareholders' equity	368.4	401.3	443.0	516.5	609.8
Capital stock	14.0	14.0	14.0	14.0	14.0
Capital surplus	319.6	320.1	320.1	320.1	320.1
Other capital	2.7	0.3	0.3	0.3	0.3
Accumulated other comprehensive income	0.0	(0.8)	(0.8)	(0.8)	(0.8)
Retained earnings	32.1	67.6	109.3	182.8	276.2
Controlling interest equity	368.4	401.3	443.0	516.5	609.8
Non-controlling interest equity	0.0	0.0	0.0	0.0	0.0
*Total debt	10.1	2.1	2.1	2.1	2.1
*Net debt (cash)	(182.5)	(153.4)	(192.4)	(247.5)	(326.9)

Statement of cash flow

Year to December (bn KRW)	2017	2018	2019F	2020F	2021F
Cash flow from operations	(7.2)	(29.1)	224.8	225.4	256.8
Net profit	23.8	35.8	41.7	73.5	93.4
Depreciation expense	0.3	0.3	0.4	0.3	0.3
Amortization expense	41.0	75.0	177.7	175.7	177.8
FX translation loss (gain)	0.8	(0.5)	0.0	0.0	0.0
Asset disposal loss (gain)	(0.0)	0.0	0.0	0.0	0.0
Equity method loss (gain)	0.0	0.0	0.0	0.0	0.0
Change in working capital	(72.9)	(139.4)	8.6	(19.6)	(8.7)
(Payment of income tax)	(10.4)	(9.7)	(14.1)	(23.2)	(29.5)
Others	10.2	9.4	10.5	18.7	23.5
Cash flow from investments	(141.0)	140.6	(188.4)	(173.0)	(180.1)
Increase in tangible assets	(0.1)	(0.2)	(0.3)	(0.4)	(0.1)
Decrease in tangible assets	0.1	0.0	0.1	0.1	0.1
Change in intangible assets	(0.2)	(0.1)	(190.6)	(176.3)	(185.2)
Change in investment assets	0.0	0.0	(1.1)	(0.9)	(0.7)
Others	(140.8)	140.9	3.5	4.5	5.8
Free cash flow	44.0	143.7	223.7	223.7	255.9
Cash flow from financing	188.1	(9.7)	(0.0)	(0.0)	(0.0)
Change in borrowings	(18.1)	(10.0)	0.0	0.0	0.0
Change in treasury stock	0.0	0.0	0.0	0.0	0.0
Dividends	0.0	0.0	0.0	0.0	0.0
Others	206.2	0.3	0.0	0.0	0.0
Other cash flow	0.0	0.0	2.6	2.6	2.6
Change in consolidated scope	0.0	0.0	0.0	0.0	0.0
Change in FX rates	(0.1)	(0.1)	0.0	0.0	0.0
Change in total cash	39.8	101.7	39.0	55.0	79.2
Beginning cash	11.5	51.3	153.0	192.0	246.9
Ending cash	51.3	153.0	192.0	246.9	326.2

Source: Company data, Shinhan Investment Corp.

Statement of comprehensive income

Year to December (bn KRW)	2017	2018	2019F	2020F	2021F
Sales	286.8	379.6	507.8	609.7	688.4
Growth (%)	85.7	32.4	33.8	20.1	12.9
COGS	239.7	324.0	442.5	502.4	554.2
Gross profit	47.1	55.6	65.3	107.4	134.2
GPM (%)	16.4	14.6	12.9	17.6	19.5
SG&A	14.2	15.7	18.6	21.5	23.4
Operating profit	33.0	39.9	46.7	85.8	110.8
Growth (%)	98.3	21.0	17.1	83.7	29.2
OPM (%)	11.5	10.5	9.2	14.1	16.1
Non-operating profit	(2.7)	5.7	9.1	10.9	12.0
Financial profit	(2.5)	6.1	8.7	9.6	11.0
Other non-operating profit	(0.2)	(0.3)	0.4	1.3	1.0
Equity method gain (loss)	0.0	0.0	0.0	0.0	0.0
Pre-tax profit	30.3	45.6	55.8	96.7	122.8
Income tax	6.4	9.8	14.1	23.2	29.5
Continuing operations	23.8	35.8	41.7	73.5	93.4
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Net profit	23.8	35.8	41.7	73.5	93.4
Growth (%)	192.9	50.3	16.3	76.3	27.0
NPM (%)	8.3	9.4	8.2	12.1	13.6
Controlling interest	23.8	35.8	41.7	73.5	93.4
Non-controlling interest	0.0	0.0	0.0	0.0	0.0
Comprehensive income	23.8	34.7	41.7	73.5	93.4
Controlling interest	23.8	34.7	41.7	73.5	93.4
Non-controlling interest	0.0	0.0	0.0	0.0	0.0
EBITDA	74.3	115.2	224.8	261.9	288.8
Growth (%)	91.4	55.1	95.2	16.5	10.3
EBITDA margin (%)	25.9	30.3	44.3	42.9	42.0

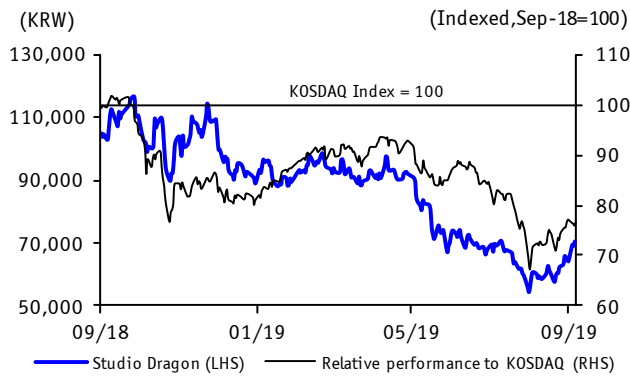
Key ratios

Year to December	2017	2018	2019F	2020F	2021F
EPS (KRW)	1,050	1,278	1,486	2,620	3,328
EPS of controlling interest (KRW)	1,050	1,278	1,486	2,620	3,328
BPS (KRW)	13,141	14,305	15,791	18,411	21,739
BPS of controlling interest (KRW)	13,141	14,305	15,791	18,411	21,739
DPS (KRW)	0	0	0	0	0
PER (x)	61.9	72.3	47.2	26.8	21.1
PER of controlling interest (x)	61.9	72.3	47.2	26.8	21.1
PBR (x)	4.9	6.5	4.4	3.8	3.2
PBR of controlling interest (x)	4.9	6.5	4.4	3.8	3.2
EV/EBITDA (x)	22.1	21.2	7.9	6.6	5.7
Dividend payout ratio (%)	0.0	0.0	0.0	0.0	0.0
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0
Profitability					
EBITDA margin (%)	25.9	30.3	44.3	42.9	42.0
OPM (%)	11.5	10.5	9.2	14.1	16.1
NPM (%)	8.3	9.4	8.2	12.1	13.6
ROA (%)	6.8	7.4	7.6	11.7	12.9
ROE (%)	9.5	9.3	9.9	15.3	16.6
ROIC (%)	18.0	14.8	19.4	34.4	41.1
Stability					
Debt to equity ratio (%)	24.7	27.7	31.9	29.9	27.2
Net debt ratio (%)	(49.5)	(38.2)	(43.4)	(47.9)	(53.6)
Cash ratio (%)	56.6	141.4	138.7	163.4	200.7
Interest coverage ratio (x)	19.0	343.0	1,143.4	2,100.7	2,713.3
Activity (%)					
Working capital turnover (times)	57.1	(183.6)	(19.3)	(26.3)	(60.1)
Inventory turnover (days)	0.8	0.9	0.5	0.5	0.5
Receivable turnover (days)	58.5	59.5	55.6	59.2	63.1

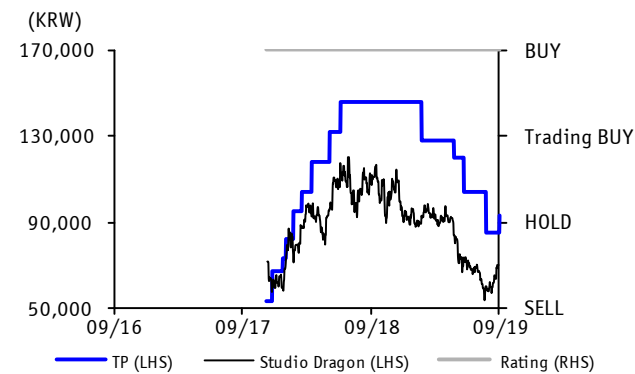
Source: Company data, Shinhan Investment Corp.

Studio Dragon (253450 KS)

Share performance



Target price



Date	Rating	Target price (KRW)	Target price gap (%)	
			Average	Max/Min
2017.11.23	BUY	53,000	20.8	35.5
2017.12.10	BUY	67,000	(6.9)	(1.8)
2018.01.09	BUY	73,000	(6.2)	1.9
2018.01.18	BUY	82,000	(2.2)	6.1
2018.02.08	BUY	95,000	(15.1)	(6.7)
2018.03.04	BUY	104,000	(9.9)	(5.3)
2018.04.01	BUY	118,000	(23.0)	(16.4)
2018.05.22	BUY	132,000	(19.3)	(11.3)
2018.06.22	BUY	146,000	(28.3)	(17.9)
2018.12.23		6M later	(37.5)	(34.0)
2019.02.07	BUY	128,000	(27.6)	(23.2)
2019.05.10	BUY	120,000	(36.9)	(30.6)
2019.06.07	BUY	104,000	(35.8)	(29.0)
2019.08.09	BUY	85,000	-	-

Note: Calculation of target price gap based on past 6 months

Rating Distribution - SHIC Universe (as of 10 September 2019)

BUY (BUY)	97.49%	Trading BUY (HOLD)	0.50%	HOLD (HOLD)	2.01%	SELL (SELL)	0%
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Rating Distribution - SHIC Investment Banking Clients (as of 10 September 2019)

BUY (BUY)	100%	Trading BUY (HOLD)	0%	HOLD (HOLD)	0%	SELL (SELL)	0%
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SHIC Ratings (as of 1 April 2017)

Stock	Sector
<ul style="list-style-type: none"> ◆ BUY: Expected 6-month gain of 10% or more ◆ Trading BUY: Expected 6-month gain of 10% to loss of 10% ◆ HOLD: Expected 6-month loss of 10% to 20% ◆ SELL: Expected 6-month loss of 20% or more 	<ul style="list-style-type: none"> ◆ OVERWEIGHT: Based on market cap, largest share of sector stocks under coverage is rated BUY ◆ NEUTRAL: Based on market cap, largest share of sector stocks under coverage is rated Trading BUY or HOLD ◆ UNDERWEIGHT: Based on market cap, largest share of sector stocks under coverage is rated SELL

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