

Yum China (YUMC US)

Key takeaways from YUMC 2023 Investor Day

During the 2023 YUMC Investor Day in Xian (last time was in Shanghai in 2019), its management raised the FY23E target and gave a time frame for its mid-term target of 20,000 stores in China (by FY26E). We believe such acceleration in growth during FY24E-26E is based on YUMC's years of refinement in unit economics and a confident answer to the speeding up in industry consolidation. Hence, we maintain BUY and lift TP to US\$ 78.66, based on 27x FY24E P/E (unchanged).

- Revised up and provided more details about its FY23E target.** Management is now targeting a 90% SSS recovery rate (vs 2019), which is actually implying 5%-10% SSSG in FY23E and that is roughly inline with CMBI est. They also revised up store opening target to 1,400-1,600 (from 1,100-1,300), lifting the YoY store count growth to 12% (from 10%). However, this is just inline with our view (we did mention twice in 1Q23 and 1H23, that the original plan was too conservative, where the growth rate was even slower than in FY22 and 1H23 mix was just too high at 50%-60%). We estimated that the mix for KFC/ Pizza Hut will be about 1,000-1,100/400-500. While the Company is keeping its capex target of US\$ 700mn-900mn, the spending per store can be lower and resulted in lower D&A expenses and higher OP margin.
- Putting down a time frame for its 20,000 stores target.** Management finally provided a concrete timeline for its mid-term target of 20,000 stores in China, that is by FY26E, which is effectively implying roughly 1,800+ stores per year (perhaps 1,200/600 for KFC/ Pizza Hut) and a round 12% CAGR. We are reasonably confident on this goal, because: 1) KFC/ Pizza Hut had only tapped into 1,900+/ 650+ cities, still far below the 3,000 addressable cities that YUMC thinks are suitable, 2) the addressable market is now larger since smaller store model was invented, where the capex and breakeven point are far lower, 3) the franchising mix was raised to 15%-20% of new stores and more local resources can be leveraged.
- Franchising has been modernized and becomes more useful for expansion.** Management did mention that the network effect is stronger in urban cities (but not in rural cities), and therefore, having a capable partner can certainly be useful when expanding to the remote areas. Moreover, local partners can often penetrate into various sites such as the hospitals, universities, transportation hubs, etc.. More importantly, thanks to advancement of digitalization and management know-how, the franchised stores, nowadays, are much easier to be managed and monitored, therefore the food safety issues should be solved with ease.
- Maintain BUY and raise TP to US\$ 78.66.** Our new TP is based on 27x FY24E P/E (unchanged), at par with 5 years avg. and supported by industry turnaround and the accelerated store expansions. We revised up FY23E/24E/ 25E NP by 1%/ 6%/ 7% to factor in faster expansion and higher OP margin. YUMC is currently trading at 19x FY24E P/E, not at all demanding.

Earnings Summary

(YE 31 Dec)	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue (US\$ mn)	9,853	9,569	11,262	12,979	15,085
YoY growth (%)	19.2	(2.9)	17.7	15.2	16.2
Operating profit (US\$ mn)	1,386	629	1,315	1,651	2,142
Net profit (US\$ mn)	990.0	442.0	908.6	1,232.4	1,590.4
EPS (Reported) (US\$)	2.28	1.04	2.20	2.91	3.76
YoY growth (%)	17.0	(54.2)	110.8	32.3	29.0
P/E (x)	24.6	53.6	25.4	19.2	14.9
P/B (x)	3.1	3.1	3.0	2.6	2.3
Yield (%)	0.8	1.1	1.2	1.6	2.0
ROE (%)	13.8	5.9	12.0	14.6	16.5

Source: Company data, Bloomberg, CMBIGM estimates

BUY (Maintain)

Target Price	US\$78.66
(Previous TP)	US\$74.47)
Up/Downside	40.3%
Current Price	US\$56.08

China Consumer Discretionary

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Stock Data

Mkt Cap (US\$ mn)	23,497.5
Avg 3 mths t/o (US\$ mn)	50.2
52w High/Low (US\$)	64.36/38.84
Total Issued Shares (mn)	419.0

Source: FactSet

Shareholding Structure

JPMorgan Chase & Co.	10.5%
Invesco Advisers, Inc.	8.0%

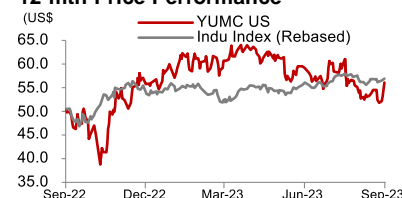
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	3.0%	3.1%
3-mth	-5.2%	-6.5%
6-mth	-7.2%	-15.3%

Source: FactSet

12-mth Price Performance



Source: FactSet

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- **Management also laid down the FY24E-26E outlook.** They are now targeting HSD-DD system sales CAGR, HSD-DD operating profit CAGR and DD EPS CAGR during FY24E-26E. Since FY26 target of 20,000 stores had already implied a 12% store count CAGR, therefore, even if we take into account of the potentially lower sales for smaller/ satellite store model vs the regular ones (by about 25%), these growth targets are all quite achievable.
- **Competition did intensify but YUMC is still highly competitive.** It is totally true that the market has become more promotional, esp. when the economic growth and recovery trend was not as good as expected, and new players have been expanding in an extremely rapid speed in FY23E. However, we still think YUMC has all its takes to compete and win more market share, supported by its: 1) accelerated store opening plan, 2) delicious and innovative food (new products like Chinese style burger will be introduced in 4Q23E), 3) widened price range, as it has launched more affordable products like the RMB 20 combo meal (the GP margin is still high, thanks to value engineering).
- **Store economic has become way more profitable (vs 2019) and improvements may continue.** Given more collaboration and innovation in the supply chain, unit cost for many products (e.g. a typical chicken product), vs 2019, has gone down a lot since FY20, this had given YUMC a large buffer to face potential cost inflation as well as price war. Thanks to improved labour capability through more investments in technology and process design (including sharing of managers between stores and centralized recruitment and staff training functions), as well as the greater use of smaller size store model (D&A and rental expenses are lower), we believe the restaurant level OP margin can continue to improve. Noted that restaurant level OP margin for smaller store for KFC/ satellite store for Pizza Hut have already increased to 21%/ 16% (vs 19%/ 13% for regular store).

Earnings revision

Figure 1: Earnings revision

US\$ mn	New			Old			Diff (%)		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Revenue	11,262	12,979	15,085	11,217	12,576	14,120	0.4%	3.2%	6.8%
Gross profit	7,959	9,203	10,705	7,927	8,920	10,025	0.4%	3.2%	6.8%
Operating Profit	1,315	1,651	2,142	1,301	1,552	1,923	1.1%	6.4%	11.4%
Net profit	909	1,232	1,590	899	1,167	1,448	1.1%	5.6%	9.8%
EPS (US\$ cents)	2.203	2.913	3.760	2.179	2.758	3.423	1.1%	5.6%	9.8%
Gross margin	70.7%	70.9%	71.0%	70.7%	70.9%	71.0%	0ppt	0ppt	0ppt
EBIT margin	11.7%	12.7%	14.2%	11.6%	12.3%	13.6%	0.1ppt	0.4ppt	0.6ppt
Net profit att. margin	8.1%	9.5%	10.5%	8.0%	9.3%	10.3%	0.1ppt	0.2ppt	0.3ppt

Source: Company data, CMBIGM estimates

Figure 2: CMBIGM estimates vs consensus

US\$ mn	CMBIGM			Consensus			Diff (%)		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Revenue	11,262	12,979	15,085	11,242	12,713	14,042	0.2%	2.1%	7.4%
Gross profit	7,959	9,203	10,705	7,370	8,683	9,175	8.0%	6.0%	16.7%
Operating Profit	1,315	1,651	2,142	1,252	1,520	1,731	5.0%	8.6%	23.7%
Net profit	909	1,232	1,590	909	1,096	1,263	-0.1%	12.4%	25.9%
EPS (US\$ cents)	2.203	2.913	3.760	2.169	2.639	3.073	1.5%	10.4%	22.3%
Gross Margin	70.7%	70.9%	71.0%	65.6%	68.3%	65.3%	5.1ppt	2.6ppt	5.6ppt
Operating Margin	11.7%	12.7%	14.2%	11.1%	12.0%	12.3%	0.5ppt	0.8ppt	1.9ppt
Net Margin	8.1%	9.5%	10.5%	8.1%	8.6%	9.0%	0ppt	0.9ppt	1.5ppt

Source: Company data, CMBIGM estimates

Assumptions

Figure 3: CMBIGM's assumptions

Major assumptions	FY21A	FY22A	FY23E	FY24E	FY25E
Sales by segment (US\$ mn)					
KFC - dine in sales	4,818	4,457	5,197	5,875	6,788
KFC - delivery sales	2,185	2,762	3,354	3,938	4,545
PH - dine in sales	1,340	1,125	1,330	1,606	2,007
PH- delivery sales	769	835	977	1,143	1,315
Others	741	390	404	416	430
Total	9,853	9,569	11,262	12,979	15,085
Sales by segment growth (%)					
KFC - dine in sales	16.0%	-7.5%	16.6%	13.1%	15.5%
KFC - delivery sales	34.7%	26.4%	21.4%	17.4%	15.4%
PH - dine in sales	17.0%	-16.1%	18.3%	20.8%	24.9%
PH- delivery sales	19.8%	8.6%	17.0%	17.0%	15.0%
Others	5.7%	-47.4%	3.7%	3.0%	3.3%
Total	19.2%	-2.9%	17.7%	15.2%	16.2%
Sales network by brand					
KFC	8,168	9,094	10,134	11,374	12,614
Pizza Hut	2,590	2,903	3,323	3,963	4,603
Others	1,030	950	990	1,040	1,120
Total	11,788	12,947	14,447	16,377	18,337
Restaurant profit margin by brand					
KFC	14.5%	15.5%	19.0%	19.7%	21.3%
Pizza hut	10.6%	9.1%	13.8%	15.1%	16.1%
Others	-1.3%	-4.6%	-0.2%	0.4%	0.5%
Total	13.7%	14.1%	18.0%	18.8%	20.2%
Costs breakdown					
Food and paper/ sales	28.5%	29.6%	29.3%	29.1%	29.0%
Payroll and employee benefits/ sales	22.9%	25.0%	24.2%	23.8%	23.1%
Rental and other operating expenses/ sales	27.0%	27.2%	25.1%	25.3%	25.1%
G & A expenses/ sales	5.7%	6.2%	6.0%	5.8%	5.6%
Franchisees expenses/ sales	6.6%	2.9%	2.5%	2.2%	1.8%
Effective tax rate	26.5%	30.4%	30.0%	25.0%	25.0%
NP att. margin	10.0%	4.6%	8.1%	9.5%	10.5%
NP att. growth (%)	26.3%	-55.4%	105.6%	35.6%	29.0%

Source: Company data, CMBIGM estimates

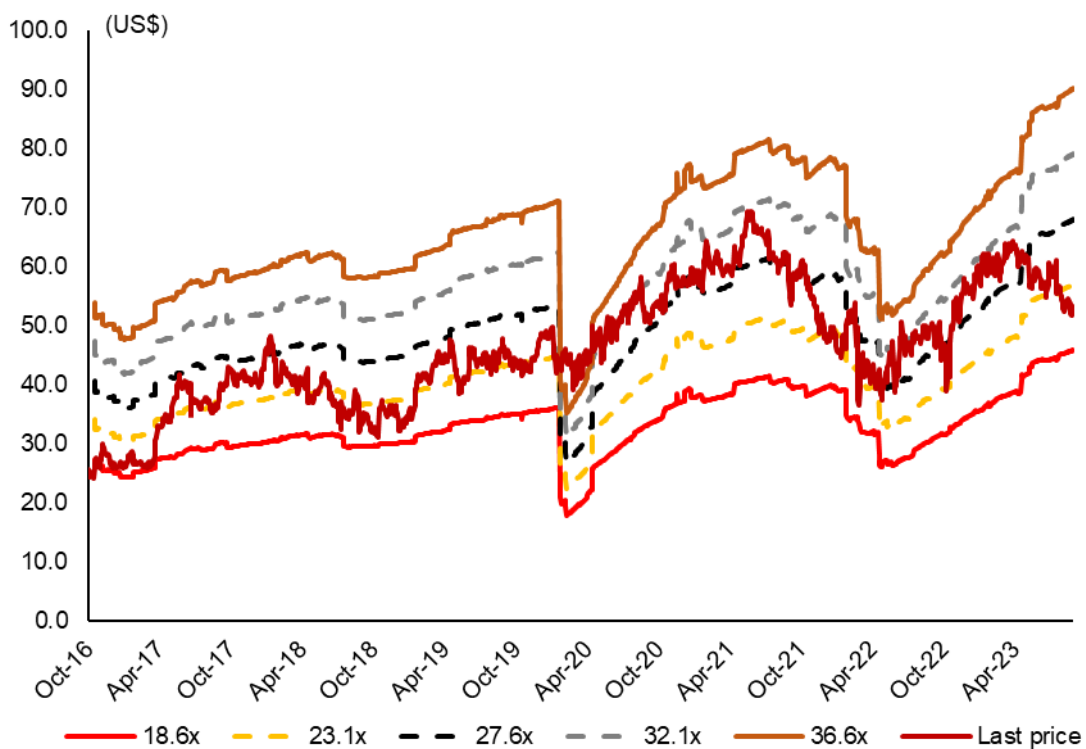
Valuation

Figure 4: Peers valuation table

Company	Ticker	Rating	12m TP (LC)	Price (LC)	Up/Down-side	Mkt. Cap (HK\$m)	Year End	P/E (x)		P/B (x)	ROE (%)	3yrs PEG (x)	Yield (%)	YTD perf.	
								FY1E	FY2E	FY2E	FY2E	FY1E	FY1E	FY1E	
Leading Greater China Catering															
Yum China	YUMC US	BUY	78.66	56.08	40%	180,139	Dec-22	25.4	19.2	2.6	5.9	0.5	1.2	(1.1)	
Jiumaojiu	9922 HK	BUY	15.46	11.90	30%	17,309	Dec-22	29.7	18.2	3.6	6.6	0.2	0.8	(42.9)	
Haidilao	6862 HK	BUY	24.76	20.90	18%	116,497	Dec-22	24.6	21.1	7.0	46.0	0.4	1.1	(6.7)	
Nayuki	2150 HK	BUY	7.53	4.60	64%	7,890	Dec-22	30.1	14.1	1.2	(9.7)	(0.1)	0.0	(38.9)	
Helens	9869 HK	NR	n/a	7.18	n/a	9,096	Dec-22	24.5	17.7	3.3	(68.1)	(0.1)	1.5	(51.6)	
Tam Jai	2217 HK	NR	n/a	1.58	n/a	2,119	Mar-23	14.4	9.9	1.3	9.1	0.6	2.1	(39.9)	
Cafe De Coral	341 HK	BUY	12.32	9.15	35%	5,359	Mar-23	17.2	12.6	1.8	3.9	0.2	5.6	(38.6)	
Xiabuxiabu	520 HK	NR	4.89	3.44	42%	3,736	Dec-22	28.8	11.8	2.1	(4.7)	(0.1)	1.6	(61.0)	
Yihai	1579 HK	BUY	n/a	13.96	n/a	14,472	Dec-22	14.9	13.1	2.3	20.5	1.3	1.9	(48.9)	
Gourmet Master	2723 TT	NR	n/a	112.00	n/a	4,947	Dec-22	18.7	14.9	1.6	7.6	0.4	3.7	(26.1)	
								Avg.	22.8	15.3	2.7	1.7	0.3	2.0	(35.6)
								Med.	24.6	14.5	2.2	6.2	0.3	1.6	(39.4)
International Catering															
Yum! Brands	YUM US	NR	n/a	129.07	n/a	283,147	Dec-22	24.6	21.8	n/a	n/a	1.9	1.9	0.8	
Mcdonald's	MCD US	NR	n/a	281.77	n/a	1,607,615	Dec-22	24.4	22.7	n/a	n/a	1.4	2.2	6.9	
Starbucks Corp	SBUX US	NR	n/a	96.93	n/a	869,193	Oct-22	28.1	23.8	n/a	n/a	1.5	2.2	(2.3)	
Rest' Brands	QSR US	NR	n/a	67.59	n/a	241,413	Dec-22	21.0	19.6	6.7	40.2	3.7	3.3	4.5	
Chipotle	CMG US	NR	n/a	1933.0	n/a	417,499	Dec-22	44.5	36.7	15.1	45.3	1.8	0.0	39.3	
Darden	DRI US	NR	n/a	148.81	n/a	140,820	May-23	17.0	15.4	7.2	44.6	1.8	3.5	7.6	
Domino's Pizza	DPZ US	NR	n/a	396.46	n/a	108,927	Jan-23	29.0	25.2	n/a	n/a	2.5	1.2	14.5	
Wendy's Co	WEN US	NR	n/a	19.94	n/a	32,672	Jan-23	20.3	17.8	16.9	47.0	1.4	5.0	(11.9)	
Shake Shack	SHAK US	NR	n/a	61.24	n/a	20,279	Dec-22	226.0	149.7	5.8	(1.8)	(1.1)	n/a	47.5	
Wingstop Inc	WING US	NR	n/a	168.76	n/a	39,607	Dec-22	77.4	66.6	n/a	n/a	4.0	0.5	22.6	
Jollibee Foods	JFC PM	NR	n/a	232.40	n/a	35,929	Dec-22	32.6	26.8	3.1	9.3	2.1	1.3	1.0	
								Avg.	49.5	38.7	9.1	30.8	1.9	2.1	11.9
								Med.	28.1	23.8	7.0	42.4	1.8	2.0	6.9
H-shares Consumer Staples															
UPC	220 HK	NR	n/a	5.45	n/a	23,540	Dec-22	13.5	12.1	1.6	11.8	0.8	7.7	(30.2)	
Tingyi	322 HK	NR	n/a	10.74	n/a	60,513	Dec-22	16.1	13.3	4.0	21.7	0.9	6.3	(20.4)	
Want Want	151 HK	NR	n/a	5.00	n/a	59,397	Mar-23	13.7	12.6	3.1	21.6	1.4	5.5	(4.2)	
China Mengniu*	2319 HK	BUY	36.50	27.25	34%	107,364	Dec-22	16.8	14.5	2.0	11.3	1.5	1.8	(21.9)	
Nongfu Spring*	9633 HK	BUY	56.90	44.50	28%	500,468	Dec-22	45.1	38.9	14.3	45.6	3.2	1.6	0.9	
Vitasoy	345 HK	NR	n/a	9.88	n/a	10,599	Mar-23	58.1	28.5	3.1	1.5	0.5	1.1	(38.5)	
Budweiser*	1876 HK	BUY	18.60	16.88	10%	223,549	Dec-22	27.3	22.7	2.4	8.3	1.7	1.6	(31.2)	
Tsingtao*	168 HK	BUY	88.90	64.45	38%	110,944	Dec-22	18.6	15.8	2.6	16.7	1.4	2.9	(15.8)	
CR Beer*	291 HK	BUY	73.10	44.30	65%	143,717	Dec-22	24.9	20.5	3.8	17.9	1.4	1.6	(18.8)	
Dali Foods	3799 HK	NR	n/a	3.73	n/a	51,079	Dec-22	14.8	13.5	2.1	15.8	3.4	3.9	6.6	
								Avg.	24.9	19.2	3.9	17.2	1.6	3.4	(17.3)
								Med.	17.7	15.1	2.9	16.3	1.4	2.3	(19.6)

Source: Bloomberg, Company data, CMBIGM estimates, *covered by Joseph Wong

Figure 5: Forward 12M P/E valuation band



Source: Bloomberg, CMBIGM estimates

Financial Summary

INCOME STATEMENT	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (US\$ mn)						
Revenue	8,263	9,853	9,569	11,262	12,979	15,085
Cost of goods sold	(2,342)	(2,812)	(2,836)	(3,303)	(3,776)	(4,381)
Gross profit	5,921	7,041	6,733	7,959	9,203	10,705
Operating expenses	(5,245)	(6,298)	(6,010)	(6,666)	(7,591)	(8,608)
Selling expense	0	0	0	0	0	0
Admin expense	(591)	(663)	(704)	(800)	(896)	(1,011)
Staff costs	(1,730)	(2,258)	(2,389)	(2,720)	(3,085)	(3,483)
Other rental related expenses	(814)	(968)	(957)	(1,079)	(1,225)	(1,402)
Others	(1,660)	(1,893)	(1,358)	(1,493)	(1,733)	(1,944)
Operating profit	961	1,386	629	1,315	1,651	2,142
Other income	285	643	(94)	23	39	45
Share of (losses)/profits of associates/JV	0	0	0	0	0	0
EBITDA	1,411	1,902	1,231	1,889	2,303	2,911
Depreciation	(431)	(505)	(582)	(514)	(595)	(729)
Other amortisation	(19)	(11)	(20)	(60)	(57)	(40)
Interest income	43	60	84	113	145	171
Interest expense	0	0	0	0	0	0
Net Interest income/(expense)	43	60	84	113	145	171
Other income/expense	104	(54)	(26)	(31)	(35)	(41)
Pre-tax profit	1,108	1,392	687	1,398	1,761	2,272
Income tax	(295)	(369)	(209)	(419)	(440)	(568)
After tax profit	813	1,023	478	979	1,320	1,704
Minority interest	(29)	(33)	(36)	(70)	(88)	(114)
Net profit	784	990	442	909	1,232	1,590

BALANCE SHEET	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (US\$ mn)						
Current assets	4,936	4,716	3,940	5,329	6,322	7,373
Cash & equivalents	1,158	1,136	1,130	2,374	3,230	4,108
Restricted cash	3,105	2,860	2,022	2,022	2,022	2,022
Account receivables	99	67	64	77	89	103
Inventories	398	432	417	494	565	656
Prepayment	176	221	307	361	416	484
Other current assets	0	0	0	0	0	0
Non-current assets	5,939	8,507	7,886	7,511	7,808	8,398
PP&E	1,765	2,251	2,118	2,336	2,909	3,537
Right-of-use assets	2,164	2,612	2,219	2,219	2,219	2,219
Investment in JVs & assos	85	292	266	266	266	266
Intangibles	246	272	159	99	42	2
Goodwill	832	2,142	1,988	1,455	1,237	1,237
Other non-current assets	847	938	1,136	1,136	1,136	1,136
Total assets	10,875	13,223	11,826	12,840	14,130	15,770
Current liabilities	2,067	2,383	2,166	2,403	2,643	2,945
Short-term borrowings	0	0	0	0	0	0
Account payables	708	830	830	967	1,105	1,282
Tax payable	72	51	68	68	68	68
Other current liabilities	1,287	1,502	1,268	1,369	1,470	1,595
Non-current liabilities	2,337	2,918	2,500	2,500	2,500	2,500
Long-term borrowings	0	0	0	0	0	0
Other non-current liabilities	2,337	2,918	2,500	2,500	2,500	2,500
Total liabilities	4,404	5,301	4,666	4,903	5,143	5,445
Share capital	4,829	4,967	4,291	4,291	4,291	4,291
Retained earnings	2,105	2,892	2,191	2,628	3,494	4,612
Other reserves	(463)	63	678	1,018	1,202	1,422
Total shareholders equity	6,471	7,922	7,160	7,937	8,987	10,325
Minority interest	0	0	0	0	0	0
Total equity and liabilities	10,875	13,223	11,826	12,840	14,130	15,770

CASH FLOW	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (US\$ mn)						
Operating						
Profit before taxation	1,108	1,392	687	1,398	1,761	2,272
Depreciation & amortization	450	516	602	574	652	769
Tax paid	111	160	(20)	(419)	(440)	(568)
Change in working capital	69	53	0	92	103	130
Others	(624)	(990)	144	533	218	0
Net cash from operations	1,114	1,131	1,413	2,178	2,293	2,602
Investing						
Capital expenditure	(419)	(689)	(679)	(732)	(1,168)	(1,358)
Acquisition of subsidiaries/ investments	(288)	(115)	(23)	0	0	0
Others	(2,402)	(51)	180	0	0	0
Net cash from investing	(3,109)	(855)	(522)	(732)	(1,168)	(1,358)
Financing						
Dividend paid	(95)	(203)	(202)	(202)	(270)	(366)
Net borrowings	0	0	0	0	0	0
Proceeds from share issues	2,195	0	0	0	0	0
Share repurchases	(8)	(75)	(466)	0	0	0
Others	(34)	(35)	(176)	0	0	0
Net cash from financing	2,058	(313)	(844)	(202)	(270)	(366)
Net change in cash						
Cash at the beginning of the year	1,046	1,158	1,136	1,130	2,374	3,230
Exchange difference	40	15	(53)	0	0	0
Others	72	(37)	47	1,244	855	878
Cash at the end of the year	1,158	1,136	1,130	2,374	3,230	4,108
GROWTH	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec						
Revenue	(5.8%)	19.2%	(2.9%)	17.7%	15.2%	16.2%
Gross profit	(6.0%)	18.9%	(4.4%)	18.2%	15.6%	16.3%
Operating profit	6.7%	44.2%	(54.6%)	109.1%	25.5%	29.7%
EBITDA	6.2%	34.8%	(35.3%)	53.5%	21.9%	26.4%
Net profit	10.0%	26.3%	(55.4%)	105.6%	35.6%	29.0%
PROFITABILITY	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec						
Gross profit margin	71.7%	71.5%	70.4%	70.7%	70.9%	71.0%
Operating margin	11.6%	14.1%	6.6%	11.7%	12.7%	14.2%
EBITDA margin	17.1%	19.3%	12.9%	16.8%	17.7%	19.3%
Return on equity (ROE)	16.3%	13.8%	5.9%	12.0%	14.6%	16.5%
GEARING/LIQUIDITY/ACTIVITIES	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec						
Current ratio (x)	2.4	2.0	1.8	2.2	2.4	2.5
Receivable turnover days	4.1	3.1	2.5	2.5	2.5	2.5
Inventory turnover days	60.6	53.9	54.6	54.6	54.6	54.6
Payable turnover days	103.7	99.8	106.8	106.8	106.8	106.8
VALUATION	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec						
P/E	28.7	24.6	53.6	25.4	19.2	14.9
P/E (diluted)	28.7	24.6	53.6	25.4	19.2	14.9
P/B	3.5	3.1	3.1	3.0	2.6	2.3
P/CFPS	18.1	22.9	14.1	10.6	10.3	9.1
Div yield (%)	0.5	0.8	1.1	1.2	1.6	2.0

Source: Company data, CMBIGM estimates. Note: The calculation of net cash includes financial assets.

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