

Downgrade to SELL

Next Games Q3 results were weak and highlighted the volatility in earnings stability when developing and launching new games. The company's cash assets have taken a big dent and with the existing games not being able to finance the development of new games Next Games is looking into other funding options. With the financing situation overshadowing the long-term potential we downgrade to SELL with a target price of EUR 1.8 (8.5).

Our World launch burdened results

Next Games Q3 results were weak, with EBIT at EUR -10.7m. Profitability was significantly affected by user acquisition and marketing costs relating to Our World, released in mid-July, along with development costs. Revenue in Q3 was EUR 13.4m (NML 5.6m, Our World 7.8m). Our World saw a good start after release, but a growing number of active users lead to technical issues and a weaker second half of the quarter. The technical issues have decreased, and key metrics saw stabilization towards the end of the quarter. A new license agreement was signed during the quarter and Next Games now has four games in development.

Financial situation in focus

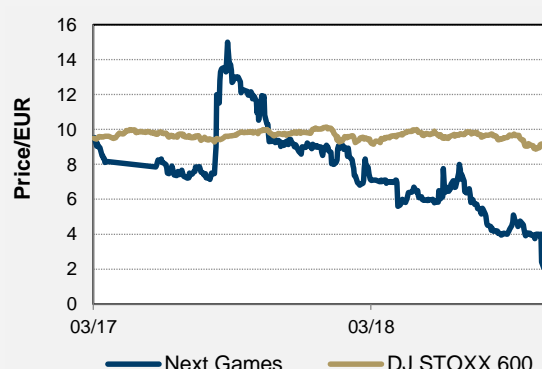
With the larger than anticipated loss in Q3, impacted by the weaker sales of Our World, Next Games is looking into options for securing its financing. The company's cash balance at the end of the quarter was EUR 8.8m along with an unused credit limit of EUR 5m. Next Games did not comment further on the types of financing sought, but we note that the effect of dilution in the case of a share emission at current share prices could be significant.

SELL (BUY) with a target price of EUR 1.8 (8.5)

At the current development pace and with only two live games the need for financing in the near future appears evident. We now expect clearly deeper losses and we emphasize the financing risk. We downgrade to SELL (BUY) with a TP of EUR 1.8 (8.5).

Rating

SELL



Share price, EUR (Last trading day's closing price) 2.06

Target price, EUR 1.8

Latest change in recommendation 06-Nov-18

Latest report on company 06-Nov-18

Research paid by issuer: YES

No. of shares outstanding, '000's 18,459

No. of shares fully diluted, '000's 18,459

Market cap, EURm 38

Free float, % 48.6

Exchange rate 0.000

Reuters code NXTGMS.HE

Bloomberg code NXTGMS FH

Average daily volume, EURm 0.0

Next interim report 15-Feb-19

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BUY HOLD SELL

KEY FIGURES

	Sales EURm	EBIT EURm	EBIT %	Ptx profit EURm	EPS EUR	P/E (x)	EV/Sales (x)	P/CF (x)	EV/EBIT (x)	DPS EUR
2016	31	-2	-5.1%	-2	-0.49	0.0	-0.1	0.0	1.8	0.00
2017	32	-6	-19.6%	-7	-0.35	-28.8	4.4	-25.2	-22.3	0.00
2018E	36	-23	-63.5%	-24	-1.14	-1.8	0.9	-2.0	-1.5	0.00
2019E	73	-11	-14.7%	-11	-0.48	-4.3	0.5	-5.1	-3.7	0.00
2020E	95	3	3.4%	2	0.11	19.2	0.4	12.5	12.4	0.00
Market cap, EURm			38	BV per share 2018E, EUR		0.8	CAGR EPS 2017-20, %			0.0
Net debt 2018E, EURm			-4	Price/book 2018E		2.4	CAGR sales 2017-20, %			42.9
Enterprise value, EURm			34	Dividend yield 2018E, %		0.0	ROE 2018E, %			-80.4
Total assets 2018E, EURm			21	Tax rate 2018E, %		12.7	ROCE 2018E, %			-84.8
Goodwill 2018E, EURm			1	Equity ratio 2018E, %		73.8	PEG, P/E 18/CAGR			0.0

All the important disclosures can be found on the last pages of this report.

VALUATION RESULTS	BASE CASE DETAILS	VALUATION ASSUMPTIONS	ASSUMPTIONS FOR WACC	
Current share price	2.06 PV of Free Cash Flow	32 Long-term growth, %	2.5 Risk-free interest rate, %	2.25
DCF share value	8.01 PV of Horizon value	90 WACC, %	10.6 Market risk premium, %	5.8
Share price potential, %	289.0 Unconsolidated equity	0 Spread, %	0.5 Debt risk premium, %	2.8
Maximum value	8.6 Marketable securities	26 Minimum WACC, %	10.1 Equity beta coefficient	1.40
Minimum value	7.5 Debt - dividend	-1 Maximum WACC, %	11.1 Target debt ratio, %	20
Horizon value, %	73.5 Value of stock	148 Nr of shares, Mn	18.5 Effective tax rate, %	20

DCF valuation, EURm	2017	2018E	2019E	2020E	2021E	2022E	2023E	2024E	2025E	2026E	2027E	Horizon
Net sales	32	36	73	95	109	122	134	145	152	159	163	167
<i>Sales growth, %</i>	<i>4.5</i>	<i>11.2</i>	<i>101.9</i>	<i>30.0</i>	<i>15.0</i>	<i>12.0</i>	<i>10.0</i>	<i>7.5</i>	<i>5.0</i>	<i>5.0</i>	<i>2.5</i>	<i>2.5</i>
Operating income (EBIT)	-6	-23	-11	3	16	18	20	20	21	22	23	23
<i>EBIT margin, %</i>	<i>-19.6</i>	<i>-63.5</i>	<i>-14.7</i>	<i>3.4</i>	<i>14.5</i>	<i>15.0</i>	<i>15.0</i>	<i>14.0</i>	<i>14.0</i>	<i>14.0</i>	<i>14.0</i>	<i>14.0</i>
+ Depreciation+amort.	2	2	2	1	1	1	1	1	1	1	1	
- Income taxes	0	3	2	-1	-3	-4	-4	-4	-4	-4	-5	
- Change in NWC	-2	-1	-1	-1	0	0	0	0	0	0	0	
<i>NWC / Sales, %</i>	<i>0.6</i>	<i>3.0</i>	<i>3.0</i>	<i>3.0</i>	<i>3.0</i>	<i>3.0</i>	<i>3.0</i>	<i>3.0</i>	<i>3.0</i>	<i>3.0</i>	<i>3.0</i>	
+ Change in other liabs	0	0	0	0	0	0	0	0	0	0	0	
- Capital Expenditure	-8	-1	1	-2	-2	-2	-2	-1	-1	-2	-1	-1
<i>Investments / Sales, %</i>	<i>23.9</i>	<i>4.1</i>	<i>-2.0</i>	<i>2.2</i>	<i>1.6</i>	<i>1.5</i>	<i>1.2</i>	<i>1.0</i>	<i>1.0</i>	<i>1.0</i>	<i>0.9</i>	<i>0.9</i>
- Other items	0	0	0	0	0	0	0	0	0	0	0	
= Unlevered Free CF (FCF)	-14	-20	-6	1	11	13	15	15	16	17	18	227
= Discounted FCF (DFCF)		-20	-5	1	8	9	9	8	8	8	7	90
= DFCF min WACC		-20	-5	1	8	9	9	9	8	8	7	100
= DFCF max WACC		-20	-5	1	8	9	9	8	8	7	7	81

INTERIM FIGURES

EVLI ESTIMATES, EURm	2017Q1	2017Q2	2017Q3	2017Q4	2017	2018Q1	2018Q2	2018Q3	2018Q4E	2018E	2019E	2020E
Net sales	11	9	6	7	32	5	6	13	12	36	73	95
EBITDA	1	0	-2	-4	-5	-3	-4	-10	-4	-21	-8	4
<i>EBITDA margin (%)</i>	<i>4.9</i>	<i>1.3</i>	<i>-30.4</i>	<i>-53.1</i>	<i>-14.9</i>	<i>-70.6</i>	<i>-68.4</i>	<i>-74.4</i>	<i>-29.6</i>	<i>-57.8</i>	<i>-11.6</i>	<i>4.6</i>
EBIT	0	0	-2	-4	-6	-4	-4	-11	-4	-23	-11	3
<i>EBIT margin (%)</i>	<i>3.4</i>	<i>-2.6</i>	<i>-35.6</i>	<i>-63.9</i>	<i>-19.6</i>	<i>-78.0</i>	<i>-74.8</i>	<i>-79.8</i>	<i>-34.7</i>	<i>-63.5</i>	<i>-14.7</i>	<i>3.4</i>
Net financial items	0	0	0	0	0	0	-1	0	0	-1	0	-1
Pre-tax profit	0	0	-2	-4	-7	-4	-5	-11	-4	-24	-11	2
Tax	0	0	0	0	0	1	-1	2	1	3	2	0
<i>Tax rate (%)</i>	<i>0.0</i>	<i>-5.4</i>	<i>0.0</i>	<i>10.8</i>	<i>6.8</i>	<i>20.0</i>	<i>-15.5</i>	<i>19.9</i>	<i>20.0</i>	<i>12.7</i>	<i>20.0</i>	<i>20.0</i>
Net profit	0	0	-2	-4	-6	-3	-6	-9	-4	-21	-9	2
EPS	0.02	-0.02	-0.13	-0.22	-0.35	-0.17	-0.31	-0.47	-0.19	-1.14	-0.48	0.11
EPS adjusted (diluted no. of shares)	0.05	-0.02	-0.13	-0.22	-0.32	-0.17	-0.31	-0.47	-0.19	-1.14	-0.48	0.11
Dividend per share	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
SALES, EURm												
Next Games	11	9	6	7	32	5	6	13	12	36	73	95
Total	11	9	6	7	32	5	6	13	12	36	73	95
SALES GROWTH, Y/Y %												
Next Games	95.7	18.3	-7.9	-41.5	4.5	-56.2	-33.2	110.4	83.7	11.2	101.9	30.0
Total	95.7	18.3	-7.9	-41.5	4.5	-56.2	-33.2	110.4	83.7	11.2	101.9	30.0
EBIT, EURm												
Next Games	0	0	-2	-4	-6	-4	-4	-11	-4	-23	-11	3
Total	0	0	-2	-4	-6	-4	-4	-11	-4	-23	-11	3
EBIT margin, %												
Next Games	3.4	-2.6	-35.6	-63.9	-19.6	-78.0	-74.8	-79.8	-34.7	-63.5	-14.7	3.4
Total	3.4	-2.6	-35.6	-63.9	-19.6	-78.0	-74.8	-79.8	-34.7	-63.5	-14.7	3.4

INCOME STATEMENT, EURm	2013	2014	2015	2016	2017	2018E	2019E	2020E
Sales	0	0	10	31	32	36	73	95
<i>Sales growth (%)</i>	<i>0.0</i>	<i>0.0</i>	<i>242,600.0</i>	<i>220.5</i>	<i>4.5</i>	<i>11.2</i>	<i>101.9</i>	<i>30.0</i>
Costs	0	-4	-16	-32	-37	-57	-81	-91
Reported EBITDA	0	-4	-7	-1	-5	-21	-8	4
Extraordinary items in EBITDA	0	0	0	0	0	0	0	0
<i>EBITDA margin (%)</i>	<i>0.0</i>	<i>-98,825.0</i>	<i>-68.5</i>	<i>-3.7</i>	<i>-14.9</i>	<i>-57.8</i>	<i>-11.6</i>	<i>4.6</i>
Depreciation	0	0	0	0	-2	-2	-2	-1
EBITA	0	-4	-7	-2	-6	-23	-11	3
Goodwill amortization / writedown	0	0	0	0	0	0	0	0
Reported EBIT	0	-4	-7	-2	-6	-23	-11	3
<i>EBIT margin (%)</i>	<i>0.0</i>	<i>-98,825.0</i>	<i>-72.5</i>	<i>-5.1</i>	<i>-19.6</i>	<i>-63.5</i>	<i>-14.7</i>	<i>3.4</i>
Net financials	0	0	0	0	0	-1	0	-1
Pre-tax profit	0	-4	-7	-2	-7	-24	-11	2
Extraordinary items	0	0	0	0	0	0	0	0
Taxes	0	0	0	0	0	3	2	0
Minority shares	0	0	0	0	0	0	0	0
Net profit	0	-4	-7	-2	-6	-21	-9	2
BALANCE SHEET, EURm								
Assets								
Fixed assets	0	1	1	2	7	7	3	4
<i>% of sales</i>	<i>0</i>	<i>24,975</i>	<i>9</i>	<i>6</i>	<i>22</i>	<i>18</i>	<i>4</i>	<i>4</i>
Goodwill	0	0	0	0	1	1	1	1
<i>% of sales</i>	<i>0</i>	<i>0</i>	<i>0</i>	<i>0</i>	<i>3</i>	<i>2</i>	<i>1</i>	<i>1</i>
Inventory	0	0	0	0	0	0	0	0
<i>% of sales</i>	<i>0</i>	<i>0</i>	<i>0</i>	<i>0</i>	<i>0</i>	<i>0</i>	<i>0</i>	<i>0</i>
Receivables	0	0	3	7	6	5	11	14
<i>% of sales</i>	<i>0</i>	<i>0</i>	<i>34</i>	<i>21</i>	<i>18</i>	<i>15</i>	<i>15</i>	<i>15</i>
Liquid funds	0	2	5	4	26	5	11	14
<i>% of sales</i>	<i>0</i>	<i>56,825</i>	<i>48</i>	<i>12</i>	<i>81</i>	<i>15</i>	<i>15</i>	<i>15</i>
Total assets	0	3	9	15	43	21	28	36
Liabilities								
Equity	0	2	5	5	37	16	7	9
<i>% of sales</i>	<i>0</i>	<i>59,025</i>	<i>48</i>	<i>17</i>	<i>113</i>	<i>43</i>	<i>9</i>	<i>9</i>
Deferred taxes	0	0	0	0	0	0	0	0
<i>% of sales</i>	<i>0</i>	<i>0</i>	<i>0</i>	<i>0</i>	<i>0</i>	<i>0</i>	<i>0</i>	<i>0</i>
Interest bearing debt	0	0	0	1	1	1	13	16
<i>% of sales</i>	<i>0</i>	<i>3,825</i>	<i>4</i>	<i>2</i>	<i>2</i>	<i>3</i>	<i>18</i>	<i>17</i>
Non-interest bearing current liabilities	0	1	4	8	5	4	9	11
<i>% of sales</i>	<i>0</i>	<i>18,875</i>	<i>37</i>	<i>27</i>	<i>17</i>	<i>12</i>	<i>12</i>	<i>12</i>
Other interest free debt	0	0	0	0	0	0	0	0
<i>% of sales</i>	<i>0</i>	<i>0</i>	<i>2</i>	<i>0</i>	<i>1</i>	<i>0</i>	<i>0</i>	<i>0</i>
Total liabilities	0	3	9	15	43	21	28	36
CASH FLOW, EURm								
+ EBITDA	0	-4	-7	-1	-5	-21	-8	4
- Net financial items	0	0	0	0	0	-1	0	-1
- Taxes	0	0	0	-2	0	3	2	0
- Increase in Net Working Capital	0	1	0	1	-2	-1	-1	-1
+/- Other	0	0	0	1	0	0	0	0
= Cash flow from operations	0	-3	-7	-1	-7	-20	-8	2
- Capex	0	0	-1	0	-8	-1	1	-2
- Acquisitions	0	0	0	0	0	0	0	0
+ Divestments	0	0	0	0	0	0	0	0
= Net cash flow	0	-3	-8	0	-14	-21	-6	0
+/- Change in interest-bearing debt	0	0	0	0	0	0	12	3
+/- New issues/buybacks	0	6	9	2	38	0	0	0
- Paid dividend	0	0	0	0	0	0	0	0
+/- Change in loan receivables	0	0	10	0	0	0	0	0
Change in cash	0	3	11	2	23	-21	6	3

KEY FIGURES	2014	2015	2016	2017	2018E	2019E	2020E
M-cap	0	0	0	168	38	38	38
Net debt	-2	-4	-3	-26	-4	2	2
Enterprise value	-2	-4	-3	143	34	40	40
Sales	0	10	31	32	36	73	95
EBITDA	-4	-7	-1	-5	-21	-8	4
EBIT	-4	-7	-2	-6	-23	-11	3
Pre-tax	-4	-7	-2	-7	-24	-11	2
Earnings	-4	-7	-2	-6	-21	-9	2
Book value	2	5	5	37	16	7	9
Valuation multiples							
EV/sales	-530.0	-0.4	-0.1	4.4	0.9	0.5	0.4
EV/EBITDA	0.5	0.6	2.5	-29.5	-1.6	-4.7	9.2
EV/EBITA	0.5	0.6	1.8	-22.3	-1.5	-3.7	12.4
EV/EBIT	0.5	0.6	1.8	-22.3	-1.5	-3.7	12.4
EV/operating cash flow	0.7	0.6	3.3	-21.4	-1.8	-5.4	13.1
EV/cash earnings	0.6	0.6	0.8	-27.4	-1.8	-6.1	12.7
P/E	0.0	0.0	0.0	-28.8	-1.8	-4.3	19.2
P/E excl. goodwill	0.0	0.0	0.0	-28.8	-1.8	-4.3	19.2
P/B	0.0	0.0	0.0	4.6	2.4	5.6	4.3
P/sales	0.0	0.0	0.0	5.2	1.1	0.5	0.4
P/CF	0.0	0.0	0.0	-25.2	-2.0	-5.1	12.5
Target EV/EBIT	0.0	0.0	0.0	0.0	-1.3	-3.3	10.9
Target P/E	0.0	0.0	0.0	0.0	-1.6	-3.8	16.7
Target P/B	0.0	0.0	0.0	0.0	2.1	4.9	3.8
Per share measures							
Number of shares	2,449	2,449	3,325	18,219	18,459	18,459	18,459
Number of shares (diluted)	2,449	2,449	3,325	18,219	18,459	18,459	18,459
EPS	-1.57	-2.81	-0.49	-0.35	-1.14	-0.48	0.11
EPS excl. goodwill	-1.57	-2.81	-0.79	-0.32	-1.14	-0.48	0.11
Cash EPS	-1.57	-2.65	-1.09	-0.29	-1.03	-0.36	0.17
Operating cash flow per share	-1.31	-2.74	-0.26	-0.37	-1.02	-0.40	0.16
Capital employed per share	-0.24	0.17	0.43	0.54	0.55	0.41	0.50
Book value per share	0.96	1.90	1.63	2.01	0.85	0.37	0.47
Book value excl. goodwill	0.96	1.90	1.63	1.96	0.80	0.32	0.42
Dividend per share	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Dividend payout ratio, %	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Dividend yield, %	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Efficiency measures							
ROE	0.0	-196.2	-32.7	-30.4	-80.4	-79.1	25.6
ROCE	-314.5	-176.2	-28.1	-29.3	-84.8	-58.9	14.5
Financial ratios							
Capex/sales, %	4,300.0	11.2	1.0	23.9	4.1	-2.0	2.2
Capex/depreciation excl. goodwill,%	0.0	277.1	73.2	441.4	71.6	-65.0	189.0
Net debt/EBITDA, book-weighted	0.5	0.6	2.5	5.3	0.2	-0.2	0.4
Debt/equity, market-weighted	0.0	0.0	0.0	0.0	0.0	0.3	0.4
Equity ratio, book-weighted	72.2	52.7	44.8	87.7	73.8	23.7	24.3
Gearing	-0.90	-0.90	-0.53	-0.70	-0.28	0.29	0.19
Number of employees, average	0	0	0	0	0	0	0
Sales per employee, EUR	0	0	0	0	0	0	0
EBIT per employee, EUR	0	0	0	0	0	0	0

COMPANY DESCRIPTION: Next Games Oyj is a Finland-based developer and publisher of licensed mobile games. The Company develops games in cooperation with the license owners of the entertainment products, for instance a television series. It currently has two active games: The Walking Dead: No Man's Land and The Walking Dead: Our World and four new games under development.

INVESTMENT CASE:

OWNERSHIP STRUCTURE	SHARES	EURm	%
Ovaskainen Jari Juhani Rainer	3,093,110	6.372	16.8%
IDG Ventures USA III, L.P.	1,188,306	2.448	6.4%
Hiitola Kalle Johannes	942,896	1.942	5.1%
Achrén Joakim Tomas Johan	940,818	1.938	5.1%
Achrén Mikael Jan Kennet	928,295	1.912	5.0%
Jumisko Jaakko Ensio	924,746	1.905	5.0%
Ilmarinen Mutual Pension Insurance Company	507,520	1.045	2.7%
Varma Mutual Pension Insurance Company	380,000	0.783	2.1%
Nuard Ventures Oy	364,000	0.750	2.0%
Vaah Holdings Oy	266,720	0.549	1.4%
Ten largest	9,536,411	19.645	52%
Residual	8,923,003	18.381	48%
Total	18,459,414	38.026	100%

EARNINGS CALENDAR

February 15, 2019 FY 2018 Results

OTHER EVENTS

May 17, 2018 AGM

COMPANY MISCELLANEOUS

CEO: Teemu Huuhtanen Aleksanterinkatu 9 A, 00100 Helsinki
CFO: Annina Salvén Tel:
IR:

DEFINITIONS

P/E	$\frac{\text{Price per share}}{\text{Earnings per share}}$	EPS	$\frac{\text{Profit before extraordinary items and taxes} - \text{income taxes} + \text{minority interest}}{\text{Number of shares}}$
P/Sales	$\frac{\text{Market cap}}{\text{Sales}}$	DPS	Dividend for the financial period per share
P/BV	$\frac{\text{Price per share}}{\text{Shareholders' equity} + \text{taxed provisions per share}}$	CEPS	$\frac{\text{Gross cash flow from operations}}{\text{Number of shares}}$
P/CF	$\frac{\text{Price per share}}{\text{Operating cash flow per share}}$	EV/Share	$\frac{\text{Enterprise value}}{\text{Number of shares}}$
EV (Enterprise value)	Market cap + net debt + minority interest at market value – share of associated companies at market value	Sales/Share	$\frac{\text{Sales}}{\text{Number of shares}}$
Net debt	Interest bearing debt – financial assets	EBITDA/Share	$\frac{\text{Earnings before interest, tax, depreciation and amortisation}}{\text{Number of shares}}$
EV/Sales	$\frac{\text{Enterprise value}}{\text{Sales}}$	EBIT/Share	$\frac{\text{Operating profit}}{\text{Number of shares}}$
EV/EBITDA	$\frac{\text{Enterprise value}}{\text{Earnings before interest, tax, depreciation and amortisation}}$	EAFI/Share	$\frac{\text{Pretax profit}}{\text{Number of shares}}$
EV/EBIT	$\frac{\text{Enterprise value}}{\text{Operating profit}}$	Capital employed/Share	$\frac{\text{Total assets} - \text{non interest bearing debt}}{\text{Number of shares}}$
Div yield, %	$\frac{\text{Dividend per share}}{\text{Price per share}}$	Total assets	Balance sheet total
Payout ratio, %	$\frac{\text{Total dividends}}{\text{Earnings before extraordinary items and taxes} - \text{income taxes} + \text{minority interest}}$	Interest coverage (x)	$\frac{\text{Operating profit}}{\text{Financial items}}$
Net cash/Share	$\frac{\text{Financial assets} - \text{interest bearing debt}}{\text{Number of shares}}$	Asset turnover (x)	$\frac{\text{Turnover}}{\text{Balance sheet total (average)}}$
ROA, %	$\frac{\text{Operating profit} + \text{financial income} + \text{extraordinary items}}{\text{Balance sheet total} - \text{interest free short term debt} - \text{long term advances received and accounts payable (average)}}$	Debt/Equity, %	$\frac{\text{Interest bearing debt}}{\text{Shareholders' equity} + \text{minority interest} + \text{taxed provisions}}$
ROCE, %	$\frac{\text{Profit before extraordinary items} + \text{interest expenses} + \text{other financial costs}}{\text{Balance sheet total} - \text{non interest bearing debt (average)}}$	Equity ratio, %	$\frac{\text{Shareholders' equity} + \text{minority interest} + \text{taxed provisions}}{\text{Total assets} - \text{interest free loans}}$
ROE, %	$\frac{\text{Profit before extraordinary items and taxes} - \text{income taxes}}{\text{Shareholders' equity} + \text{minority interest} + \text{taxed provisions (average)}}$	CAGR, %	Cumulative annual growth rate = Average growth per year

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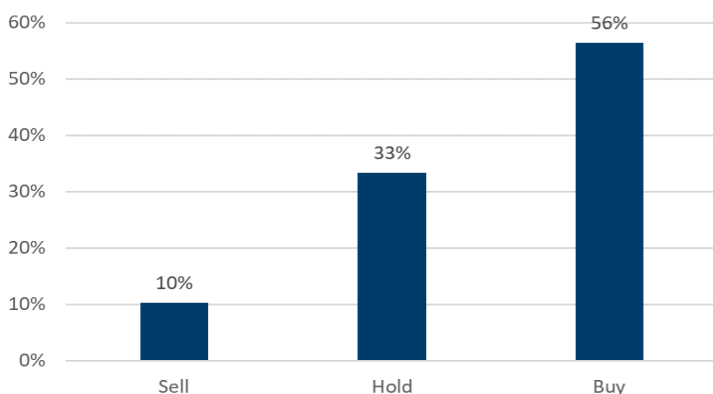
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Investment recommendations are defined as follows:

Target price compared to share price	Recommendation
< -10 %	SELL
-10 – (+10) %	HOLD
> 10 %	BUY

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Name(s) of the analyst(s): Salokivi

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