



Wilson HTM
INVESTMENT GROUP

A Leading Wealth Manager and
Adviser to Emerging Companies

13 May 2014

HILLGROVE RESOURCES LIMITED (HGO)

BUY

HOLD

SELL

ACTION & RECOMMENDATION

We retain our **SPECULATIVE BUY** rating. Hillgrove's April quarter copper production of 5.55 kt (annualised at 22.2 ktpa) was slightly below our estimates – but with copper grades expected to increase over the balance of the year, Hillgrove is on track to achieve full-year guidance of 22.3-24.6 kt of contained copper. Pleasingly, the mine performed above expectations, with record material movements. We forecast commencement of fully franked dividend payments in CY16, offering a modest 5% yield (with capacity to upsize). In our view, Hillgrove remains undervalued by the market. Our share price target of 11.6 cps represents a 12-month total shareholder return of 61%.

Apr-14 quarterly – record mining performance

What's Changed

- **Record mining performance:** HGO has announced its April quarterly production report. The highlights were: 1) record material movements of 5.2 Mt, 17% above our estimates, and 2) process plant throughput of 757 kt (3.28 Mtpa) was within guidance range for the year, and demonstrating its reliability once again.
- **Production was slightly below** – the disappointments were: 1) copper production of 5.55 kt was 5% below our estimates, 2) milled copper grade of 0.80% copper, below full-year guidance of 0.83-0.88% copper, and 3) recoveries of 92.1% were below our estimates, largely a function of the lower copper head grade. The grades of copper should improve over the balance of FY15 (year to Jan-15), as access increases to the higher grade Nugent pit – so we remain confident of HGO achieving guidance of 22.3-24.6 kt of copper.
- **A year of transformation:** We forecast the company's debt position decreasing from \$19.5m (end of the April quarter) to around \$2m by the end of January 2015.

Risks & Catalysts

- **Key risks** around HGO: 1) Consistency in delivering feed to the mill of above 0.80% copper, 2) operational risk at the Kanmantoo mine, especially while it is operating a single open pit with single lane ramp, and 3) future weakness in the copper price.
- **Catalysts:** 1) The July 2014 quarterly report which should demonstrate consistency in delivering grades of 0.80% copper or more to the mill, and 2) an improved copper market or weaker AUD.

Year-end January (AUD)	FY13A	FY14A	FY15E	FY16E	FY17E
Revenue (\$m)	115.4	139.2	185.4	168.8	165.7
EBITDA Margin (%)	12	27	25	21	20
NPAT Norm (\$m)	-10.2	1.7	13.4	8.3	7.2
Consensus NPAT (\$m)			12.1	9.9	23.0
EPS Norm (cps)	-1.2	0.2	1.3	0.8	0.7
EPS Growth (%)	-84	113	684	-38	-13
P/E Norm (x)	-5.9	44.3	5.7	9.2	10.5
EV / EBITDA (x)	7.9	2.9	2.4	3.1	3.3
CFM (x)	3.5	10.7	2.1	2.9	2.9
DPS (cps)	0.0	0.0	0.0	0.4	0.4
Franking (%)	0	0	0	100	100

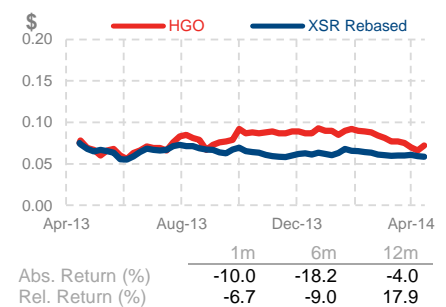
Mkt Cap: \$85m Enterprise Value: \$110m Shares: 1,181m Sold Short: 0.1%

12m Target Price (AUD)	\$0.116
Share Price @ 12-May-14 (AUD)	\$0.072
Fcst 12m Capital Return	60.4%
Fcst 12m Dividend Yield	0.7%
12m Total S'holder Return	61.1%

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12m Share Price Performance



WHTM Return Re-investment Matrix

Return	Re-Investment	
	Low	High
High	Cash Generator	Champion
Low	Challenged	Potential

WHTM Risk Assessment

Risk	Share Price Risk			
	Low	Med	High	Spec
Share Price Risk				
Business Risk				

Key Changes	04-Apr	After	Var %
Revenue FY15	189	185	-1.7%
(\$m) FY16	169	169	0.0%
FY17	166	166	0.0%
EBITDA: FY15	49.0	45.8	-6.6%
(\$m) FY16	35.6	35.6	0.0%
FY17	33.1	33.1	0.0%
EPS: FY15	1.5	1.3	-15.0%
Norm FY16	0.8	0.8	0.3%
(cps) FY17	0.7	0.7	0.1%
Price Target:	0.12	0.12	-2.4%
Rec:	BUY	BUY	
ASX 300 wgt:	0.0%	Median T'over/Day:	\$0.1m

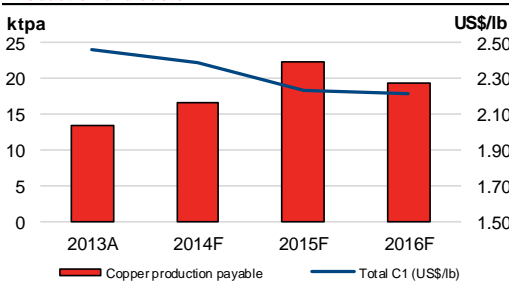
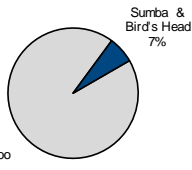
Wilson HTM Equities Research – Hillgrove Resources Limited

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TABLE 1: HGO FINANCIAL SUMMARY

Capital profile				Jan year end					
				2013A	2014F	2015F	2016F	2017F	
Number of shares (m)	1,179			NPAT Reported (A\$m)	-118	15	13.4	8.3	7.2
Market capitalisation (A\$m)	94			NPAT Normalised (A\$m)	-10.2	1.7	13.4	8.3	7.2
Enterprise value (A\$m)	120			EPS (A¢)	-1.1	0.2	1.3	0.8	0.7
Enterprise value (US\$m)	110			CFPS (A¢)	-0.6	-0.5	2.5	2.3	2.5
				DPS (A¢)	0.0	0.0	0.0	0.4	0.4
				P/E (x)	nm	49.3	6.3	10.2	11.7
				P/CF (x)	-12.7	-16.1	3.2	3.4	3.2
				EV/EBITDA (x)	8.4	3.2	2.1	2.2	1.7
				EPS Growth	118%	-15%	684%	-38%	-13%
				Yield (%)	0.0%	0.0%	0.0%	5.0%	5.0%
Resources				Assumptions FY					
Mt	%	Cont	Cu	2013A	2014F	2015F	2016F	2017F	
Resources, incl stockpiles (Mt)	313	@ 0.77%	242 kt	AUD/USD	1.04	0.97	0.91	0.90	0.87
Reserves, incl stockpiles (Mt)	22.1	@ 0.71%	157 kt	Copper price (US\$/lb)	3.70	3.62	3.27	3.21	3.26
EV/t Resource (A\$/t)	A\$492.9	US\$453.5		Gold price (US\$/oz)	1669	1412	1261	1269	1250
EV/t Reserve (A\$/t)	A\$762.5			Silver price (US\$/oz)	31.13	23.87	20.25	20.25	19.75
VALUATION				Total Coal Sales (100%)					
Description	A\$m	A\$ps		2013A	2014F	2015F	2016F	2017F	
Kanmantoo	171	0.14		Copper production payable	13.3	16.6	22.2	19.3	18.1
Sumba & Bird's Head	12	0.01		Gold production payable	4.7	3.6	5.0	9.6	9.8
				Cu. Equiv production payable (kt)	14.2	17.2	23.1	21.0	19.8
Total Operations	183	0.16							
Net (debt) / cash	-20	-0.02		Cash costs @ Kanmantoo	2013A	2014F	2015F	2016F	2017F
Corporate overheads (incl WC)	-26	-0.02		Total C1 (US\$/lb)	2.46	2.38	2.23	2.21	2.24
Franking Credits	0	0.00		Royalties (US\$/lb)	0.05	0.04	0.06	0.07	0.07
Listed investments	0	0.00		Admin (US\$/lb)	0.28	0.24	0.15	0.17	0.15
Exploration	0	0.00		EBITDA costs (US\$/lb)	2.79	2.66	2.44	2.45	2.46
Total Valuation	136	0.116		Sustaining capex (US\$/lb)	0.44	0.08	0.04	0.04	0.04
Premium (Discount)		0.00		All in cash costs (US\$/lb)	2.93	2.74	2.47	2.49	2.50
Target Price		0.116		D&A (US\$/lb)	0.90	0.76	0.54	0.63	0.69
				EBIT costs (US\$/lb)	3.69	3.42	2.98	3.08	3.15
P/NPV		0.69							
Operations NPV split				Margin analysis					
	Valuation inputs			2013A	2014F	2015F	2016F	2017F	
	Rf rate	5.3%		EBITDA (US\$/lb)	0.90	0.96	0.83	0.76	0.80
	MRP	6.0%		All-in cash cost margin (US\$/lb)	0.76	0.88	0.80	0.72	0.75
	Equity beta	1.42		EBIT (US\$/lb)	0.00	0.20	0.29	0.13	0.11
	Ke	14%							
	Kd	7.0%		Profit and Loss (\$m)	2013A	2014F	2015F	2016F	2017F
	Gearing	30%		Revenue	116	140	185	169	166
	Tax rate	30%		Costs	103	102	140	133	133
	WACC	11%		EBITDA	14	38	46	36	33
	DCF (A\$)	0.12		Depreciation & amortisation	26	29	24	24	24
	Prem/disc	0%		EBIT	-13	8	22	12	9
	Target (A\$)	0.12		Interest income	1	0	1	1	1
				Interest expense	7	6	3	0	0
				MRRT	0	0	0	0	0
				Pre tax profit	-18	3	19	12	10
				Tax expense (benefit)	-8	1	6	4	3
				NPAT - underlying	-10	2	13	8	7
				Significant items	2	0	0	0	0
				NPAT - reported	-12	1	13	8	7
Sensitivity (A\$ps/A\$m)				Profitability analysis					
NPV (\$ps)	2015F	2016F		2013A	2014F	2015F	2016F	2017F	
Base Case NPV / NPAT	0.116	13.4	8.3	EBIT margin	-	6%	12%	7%	6%
Copper price +10% increase	+0.04	+4.2	+9.9	EBITDA margin	12%	27%	25%	21%	20%
Copper price +10% increase	+34%	+51%	+137%	Effective tax rate	44%	33%	30%	30%	30%
AUD +10% increase	-0.04	-4.4	59.2	ROA - EBIT / (total assets - cash)	-4%	3%	7%	4%	4%
AUD +10% increase	-33%	-53%	89%	ROE - NPAT / equity	-5%	1%	6%	3%	3%
AUD +1¢ increase	0.00	-0.5	6.8						
AUD +1¢ increase	-4%	-6%	10%						
Production and costs				Cashflow					
ktpa				2013A	2014F	2015F	2016F	2017F	
	25			EBITDA	14	38	46	36	33
	20			Operating cashflow	28	11	42	32	31
	15			Sustaining Capex	-4	-3	-2	-2	-2
	10			Growth Capex	-34	-16	-16	-8	-6
	5			Free cashflow	-10	-8	23	22	24
	0			Investing cashflow	-46	-22	-18	-10	-8
				Financing cashflow	24	0	-28	-15	-4
				Net Change in cash	7	-11	-5	7	19
				Balance Sheet Analysis	2013F	2014F	2015F	2016F	2017F
				Debt	50	42	13	1	1
				Equity	221	229	243	246	248
				Assets	336	322	301	283	281
				Cash	27	16	12	19	38
				Net debt	23	25	2	-18	-37
				Gearing - net debt/equity	10%	11%	1%	-7%	-15%
				Gearing - net debt/ (net debt + equity)	9%	10%	1%	-8%	-18%
				Net debt / EBITDA	16	0.7	0.0	-0.5	-1.1
				EBIT / net interest	-2.2	1.4	8.5	-50.4	-8.0
				EBITDA / net interest	2.4	6.4	17.9	-15.1	-29.1



Source: Wilson HTM, company data

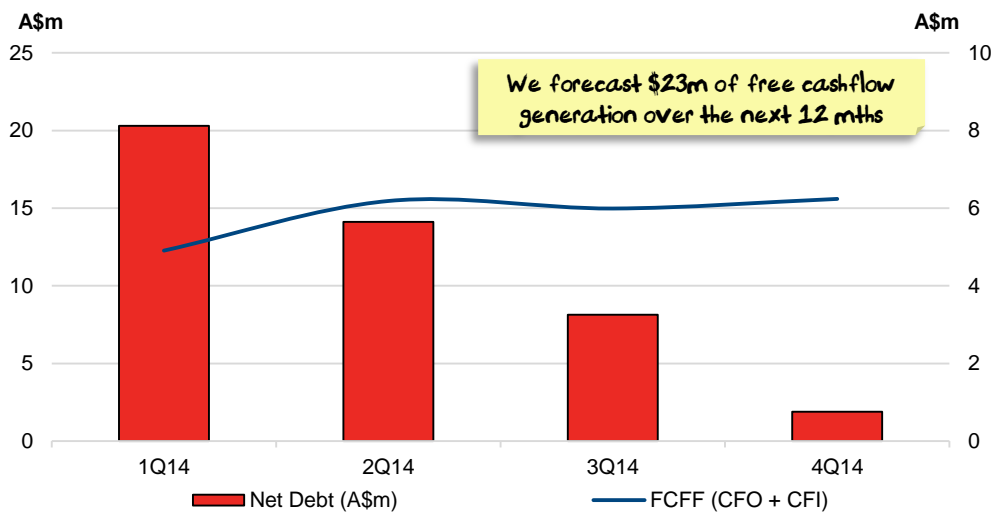


TABLE 2: QUARTERLY PRODUCTION REPORT HIGHLIGHTS

	Jul-13	Oct-13	Jan-14	Apr-14	WilsHTM	QoQ v WilsHTM	
	QTR	QTR	QTR	QTR			
				Actual	Forecast		
Ore to ROM from pit - Mt	0.56	0.77	0.88	0.81	0.80	-8%	1%
Mined waste - Mt	2.16	1.66	3.48	4.45	2.80	28%	59%
Total tonnes mined - Mt	2.71	2.43	4.86	5.26	4.50	8%	17%
Strip ratio	3.89	2.15	3.96	5.48	3.50	38%	56%
Mining grade to ROM - Cu	0.67%	0.63%	0.85%	0.87%	0.83%	2%	5%
Ore milled - Mt	0.72	0.76	0.76	0.76	0.75	-0%	1%
Milled grade - Cu	0.54%	0.63%	0.83%	0.80%	0.84%	-4%	-5%
Recovery - Cu	89.5%	90.7%	92.4%	92.1%	93.0%	-0%	-1%
Cu concentrate produced - dmt	15.82	19.20	25.05	24.34	25.47	-3%	-4%
Contained metal in conc - Cu	3.45	4.31	5.84	5.55	5.86	-5%	-5%
Contained metal in conc - Au - o:	1.27	1.18	1.28	1.33	2.06	4%	-36%
Total concentrate sold (kt)	14.13	18.92	24.81	24.43	25.47	-2%	-4%

Source: Wilson HTM, company data

CHART 1: HGO'S NET DEBT OVER FY15



Source: Wilson HTM, company data

TABLE 3: CHANGES TO FORECASTS

	2014a	2015f	2016f	2017f	NPV (A\$ps)	Target price (A\$ps)
Underlying NPAT (A\$m) - previous	1.7	15.8	8.2	7.2	0.118	0.118
Underlying NPAT (A\$m) - revised	1.7	13.4	8.3	7.2	0.116	0.116
Change (A\$m)	0.0	-2.4	0.0	0.0	0.00	0.0
Change (%)	0%	-15%	0%	0%	-2%	-2%

Source: Wilson HTM, company data



PRICE TARGET		
	Val. A\$m	Val. A\$ps
Kanmantoo	170.716	0.145
Sumba & Bird's Head	12.000	0.010
Total Operations	182.716	0.155
Net (debt) / cash	-20.310	-0.017
Corporate overheads	-26.225	-0.022
Franking Credits	0.000	0.000
Listed investments	0.000	0.000
Exploration	0.000	0.000
Total Valuation	136.180	0.116
Premium (Discount)		0.000
Target Price		0.116

INTERIMS (\$m)				
Half Yr (AUD)	Jul 13	Jan 14	Jul 14	Jan 15
	1HA	2HA	1HE	2HE
Sales	58.6	80.6	93.0	92.4
EBITDA	18.7	18.9	23.9	21.9
EBIT	6.3	2.2	11.8	9.9
Net Profit	1.7	0.0	7.1	6.3
Norm. EPS	0.2	0.0	0.7	0.6
EBIT/Sales	10.7	2.7	12.7	10.7
Dividend (c)	0.0	0.0	0.0	0.0
Franking (%)	0.0	0.0	0.0	0.0

FINANCIAL STABILITY			
Year-end January	FY14A	FY15E	FY16E
Net Debt	25.2	1.9	-17.7
Net Debt / Equity (%)	11.6	0.8	<0
Net Debt / EV (%)	22.9	1.7	<0
Current Ratio (x)	5.0	11.3	18.0
Interest Cover (x)	1.4	8.5	<0
Adj. Cash Int. Cover (x)	2.5	18.7	<0
Debt / CashFlow (x)	4.6	1.0	0.4
Net Debt (cash) / share	0.0	0.0	<0
NTA / share (\$)	0.2	0.2	0.2
Book Value / share (\$)	0.2	0.2	0.2
Payout Ratio (%)	0	0	51
Adj. Payout Ratio (%)	0	0	7

EPS RECONCILIATION (\$m)				
	FY14A		FY15E	
	Rep.	Norm.	Rep.	Norm.
Sales Revenue	139	139	185	185
EBIT	8.7	8.4	21.7	21.7
Net Profit	1.9	1.7	13.4	13.4
Notional Earn.	0.0	0.0	0.0	0.0
Pref./Conv. Div.	0.0	0.0	0.0	0.0
Profit for EPS	1.9	1.7	13.4	13.4
Diluted Shrs(m)	1,052	1,052	1,052	1,052
Diluted EPS (c)	0.2	0.2	1.3	1.3

RETURNS				
	FY14A	FY15E	FY16E	FY17E
ROE (%)	0.8	5.8	3.4	2.9
ROIC (%)	2.4	6.2	3.4	2.9
Incremental ROE	292.9	191.8	-36.9	-42.1
Incremental ROIC	784.8	-211.7	94.7	10.0

KEY ASSUMPTIONS								
Year-end January (AUD)	FY13A	FY14A	FY15E	FY16E	FY17E	FY18E	FY19E	FY20E
AUD/USD	1.0359	0.9684	0.9091	0.8950	0.8727	0.8450	0.8173	
Copper price (US\$/lb)	3.70	3.33	3.07	3.28	3.28	3.20	3.08	
Copper price (US\$/t)	8,150	7,332	6,767	7,220	7,220	7,054	6,779	
Gold price (US\$/oz)	1,669	1,412	1,261	1,269	1,250	1,241	1,216	
Silver price (US\$/oz)	31.1	23.9	20.2	20.3	19.8	19.6	19.9	
Copper Prod Payable (kt)	13.3	16.6	22.2	19.3	18.1	18.1	18.1	
Gold Prod Payable (koz)	4.7	3.6	5.0	9.6	9.8	9.8	9.8	
Cu. Equiv Prod Payable (kt)	14.2	17.2	23.1	21.0	19.8	19.8	19.8	

PROFIT & LOSS (\$m)								
Year-end January (AUD)	FY13A	FY14A	FY15E	FY16E	FY17E	FY18E	FY19E	FY20E
Sales Revenue	115.4	139.2	185.4	168.8	165.7	168.1	167.2	
EBITDA	13.9	37.6	45.8	35.6	33.1	32.4	31.2	
Depn & Amort	26.5	29.2	24.1	24.0	24.0	24.0	24.0	
EBIT	-12.6	8.4	21.7	11.6	9.1	8.4	7.2	
Net Interest Expense	5.7	5.9	2.6	-0.2	-1.1	-1.9	-2.8	
Tax	-8.1	0.8	5.7	3.5	3.1	3.1	3.0	
Minorities / pref divs	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Equity accounted NPAT	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Net Profit pre Sig. Items	-10.2	1.7	13.4	8.3	7.2	7.2	7.0	
Abn's / Ext's / Signif.	1.6	0.2	0.0	0.0	0.0	0.0	0.0	
Reported Net Profit	-8.7	1.9	13.4	8.3	7.2	7.2	7.0	

CASHFLOW (\$m)								
Year-end January (AUD)	FY13A	FY14A	FY15E	FY16E	FY17E	FY18E	FY19E	FY20E
EBITDA	13.9	37.6	45.8	35.6	33.1	32.4	31.2	
Interest & Tax	-3.1	-2.8	-5.1	-3.8	-1.9	-1.4	-0.5	
Working Cap / Other	17.6	-23.8	1.0	0.0	0.0	0.0	0.0	
Operating Cash Flow	28.4	11.0	41.6	31.8	31.2	31.0	30.7	
Maintenance Capex	-4.0	-3.0	-2.0	-2.0	-2.0	-2.0	-2.0	
Free Cash Flow	24.4	8.0	39.6	29.8	29.2	29.0	28.7	
Dividends Paid	0.0	0.0	0.0	-2.1	-4.2	-4.2	-2.1	
Development Capex	-34.1	-16.0	-16.3	-8.1	-5.6	-4.4	-2.4	
Invest. / Disposals	0.3	0.5	0.0	0.0	0.0	0.0	0.0	
Other Inv. Flows	-81.4	-3.7	0.0	0.0	0.0	0.0	0.0	0.0
Cash Flow Pre Financing	-90.8	-11.3	23.3	19.6	19.4	20.4	24.2	
Funded by Equity	97.5	10.2	0.0	0.0	0.0	0.0	0.0	
Funded by Debt	0.0	-9.8	-28.3	-12.5	0.0	0.0	0.0	
Funded by Cash	-6.7	11.0	4.9	-7.0	-19.4	-20.4	-24.2	

BALANCE SHEET SUMMARY (\$m)								
Year-end January (AUD)	FY13A	FY14A	FY15E	FY16E	FY17E	FY18E	FY19E	FY20E
Cash	27.4	16.5	11.5	18.5	37.9	58.3	82.5	
Current Receivables	6.4	5.0	3.3	1.5	0.7	0.4	0.2	
Current Inventories	19.7	26.2	17.4	7.8	3.9	2.0	1.0	
Net PPE	243.5	215.3	219.9	206.1	189.7	172.1	152.4	
Investments	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Intangibles / Capitalised	0.6	0.3	0.3	0.3	0.3	0.3	0.3	
Other	48.7	48.6	48.6	48.6	48.6	48.6	48.6	
Total Assets	346.3	311.8	301.0	282.8	281.1	281.6	285.0	
Current Payables	41.6	23.9	16.4	7.8	4.0	2.0	1.0	
Total Debt	50.3	41.7	13.4	0.9	0.9	0.9	0.9	
Other Liabilities	23.5	28.1	28.1	28.1	28.1	28.1	28.1	
Total Liabilities	115.4	93.7	57.9	36.8	32.9	31.0	30.0	
Minorities / Convertibles	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Shareholder Equity	231.0	218.2	243.2	246.0	248.2	250.6	255.0	
Total Funds Employed	281.2	259.8	256.6	246.9	249.1	251.5	255.9	



RETURN RE-INVESTMENT MATRIX

Return	High	Cash Generator	Champion
	Low	Challenged	Potential
		Low	High
		Re-investment	

Currently progressing a 20 ktpa copper mine in South Australia. Project largely derisked and should provide consistent returns. We also consider ability to grow organically as likely.

RISK MEASURES

	Low	Med	High	Spec
Share Price Risk				
Business Risk				

Share price risk: Earnings subject to copper price exposure and strength of AUD.

Business risk: Main risk is that the project does not deliver forecast copper production profile. Further risk is that exploration potential in South Australia and south-east Asia is not realised.

BUSINESS DESCRIPTION

Hillgrove Resources Limited (HGO) is an Australian mining company focused on the operation of the Kanmantoo copper mine in South Australia, and exploration of its Indonesian tenements. In Indonesia, HGO is targeting the discovery of epithermal gold and porphyry copper/gold deposits. The Kanmantoo copper mine is located less than 55 km from Adelaide. Ramp-up of the open pit mine and processing circuit is progressing to an initial throughput of 2.8 Mtpa producing ~80 kt of concentrate per annum (~20 ktpa of copper metal).

INVESTMENT THESIS

HGO completed a \$19m raising to provide sufficient working capital to allow it to address elevated grade dilution and low mining rates at its Kanmantoo mine. In our base case, operational improvements are achieved and we value the company at \$0.20/sh. The current share price approximately reflects the replacement value of the Kanmantoo mine. While we highlight the near-term operating risks, we do see value should these issues be resolved. We rate HGO a SPECULATIVE BUY.

REVENUE DRIVERS

- Copper and gold prices
- Improved mining rates and copper feed grades to the mill
- Successful exploration at Kanmantoo and Indonesia

BALANCE SHEET

- Equity: 1,180.9m
- Options: 50m
- Market capitalisation: \$96m (at A\$0.080/sh)
- Cash: \$16.4m (31-Jan-14)
- Debt: \$41.7m (31-Jan-14)

KEY ASSETS

The Kanmantoo copper mine (South Australia) is an open-cut mine with throughput of 2.8 Mtpa, producing approximately 80,000 tonnes of concentrate and containing about 20,000 tonnes of copper metal and 10,000 ounces of gold with exploration potential for further copper.

RESERVES & RESOURCES

- Kanmantoo:
 - In-situ resource: 31.2 Mt @ 0.82% copper
 - Long-term stockpile resource: 1.6 Mt @ 0.37% copper

BOARD

- Dean Brown (Chairman)
- John Gooding (Non-Executive Director)
- John Quirke (Non-Executive Director)
- Douglas Snedden (Non-Executive Director)
- Edwin Zemancheff (Non-Executive Director)

KEY ISSUES/CATALYSTS

- Mill feed grades achieving 0.8% by the end of April 2013
- Increased resource at Kanmantoo to increase mine life towards 10 years
- Exploration success in Indonesia provides optionality for HGO

MANAGEMENT

- Mr Greg Hall (Managing Director)
- Russell Middleton (Chief Financial Officer)
- Shanthy Smith (Company Secretary)
- Steven McClare (General Manager, Kanmantoo Copper Mine)

RISK TO VIEW

- Inability to achieve and maintain full production capacity at Kanmantoo

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Return Reinvestment Matrix and Risk Measures

Definitions at <http://www.wilsonhtm.com.au/Disclosures>

Recommendation Structure and Other Definitions

Definitions at <http://www.wilsonhtm.com.au/Disclosures>

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