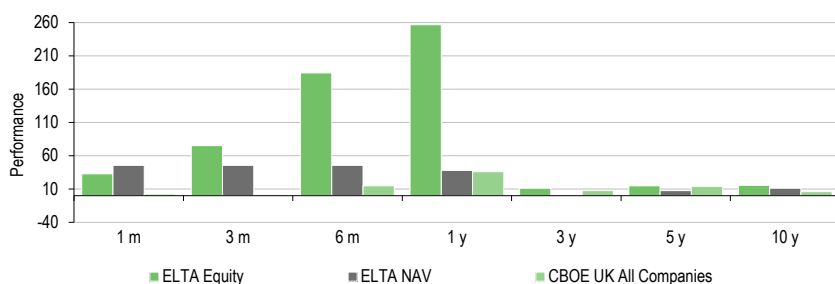


Electra Private Equity

The realisation strategy – further steps

On 21 May, Electra Private Equity (ELTA) announced the board's intention to demerge Fridays – the largest of the two operating businesses (74% of ELTA's NAV) – onto the FTSE Main Market and, subsequently, to bring Hotter Shoes (10% of NAV) to AIM through reclassification of the Electra entity. This followed the 15 April announcement about the disposal of Sentinel for £22.2m (58.1p per share), £11.3m higher than the asset's carrying value on the balance sheet at 30 September 2020. ELTA has been following a realisation strategy since October 2016, when it had a market cap of c £1.7bn, and has since returned c £2bn to shareholders. Since our December 2020 initiation note, the shares have appreciated from a 22% discount to NAV to currently trading at a 7% premium. The share price has almost doubled from 275.5p to 550.5p per share.

ELTA's cumulative and relative performance



Source: ELTA, Edison Investment Research, at 30 April 2021. Note: Three-, five- and 10-year figures are annualised. Please also see our [initiation note](#) on ELTA.

Key points

- As the chart above shows, ELTA's performance over one year and shorter periods has responded very positively to the strategic and operational efforts within the group of the past 24 months, including the ongoing progress of the realisation of assets, with Sentinel sold in April 2021 (proceeds of £22.2m).
- ELTA's management has, over the last six months, realised a lot of the upside we highlighted in the scenario analysis in our [initiation note](#), and the increased NAV of £196.9m on 31 March 2021 reflects its efforts.
- ELTA's strategy remains the realisation of assets in the best possible way for shareholders.
- ELTA's management believes that the TGI Fridays business, with 87 sites now fully open in accordance with government guidance, is well positioned to emerge from lockdown strongly, with a robust pipeline of additional sites due to open in 2021 and beyond.
- Hotter's EBITDA in the seven months to end April 2021 is 8% ahead of pro forma EBITDA for the continuing business in the year to January 2020, which indicated pro forma full-year EBITDA of £5.4m, up £0.9m on Q120.
- A further update will be provided by the company as plans progress.

Investment trusts Special situations – private equity

25 May 2021

Price **550.5p**
Market cap **£210.6m**
NAV* **£196.9m**

NAV* per share 514.3p
 Premium to NAV 7.0%

*Including income. As at 31 March 2021.

Yield N/A
 Ordinary shares in issue 39.0m
 Code ELTA
 Primary exchange LSE
 AIC sector Private Equity
 52-week high/low* 550.0p 170.5p
 NAV** high/low 514.3p 353.4p

*A-shares. **Including income.

Gearing

Net cash (estimated) at 25 May 2021 (includes other liquid assets) £26.7m

Fund objective

Electra Private Equity's investment objective is to follow a realisation strategy, which aims to crystallise value for shareholders through balancing the timing of returning cash to shareholders with maximisation of value. Following the realisation of Sentinel, ELTA intends to retain the cash received pending further asset realisations and confirmation of future distributions to shareholders in due course.

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[Edison profile page](#)

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Investment strategy and management expectations

ELTA's investment objective remains to follow a realisation strategy, which aims to crystallise value for shareholders, through balancing the timing of returning cash to shareholders with maximisation of value. The reported net asset value (NAV) increased 46% from £135.1m on 30 September 2020 (see our [initiation note](#)) to £196.9m on 31 March 2021 (see Exhibit 1). In this report we reiterate (unchanged) management scenarios and the impact of applying sector multiples to these scenarios.

ELTA's board noted that the three operating businesses' valuations as at 31 March 2021 reflected a high degree of judgement. Amid the pandemic, the resulting lockdowns and restrictions on the businesses, Fridays and Hotter, in particular, had to operate at below their average capacity. Meanwhile, they continue to undergo restructuring and are following reorientation plans put in place by new managements from 2019. The disruption to the historical earnings of the comparator companies historically used in ELTA's internal valuation process have prompted the board to utilise published forward earnings multiples for sector peers within the consumer discretionary and industrial sectors.

Having received input from its auditors and other advisors, ELTA's board is comfortable that the published valuations are a reasonable reflection of Fridays, as it emerges from COVID-19 lockdown, and Hotter, as it demonstrates early delivery of its new business model.

Exhibit 1: NAV reconciliation with two key investments*: TGI Fridays and Hotter Shoes (post Sentinel's disposal)

| Investment | Sector | Projected % of UK revenue for 2021 | Year of investment | Purchase price (£m) | Unrealised value (£m) | Value (% of NAV) | Cum. value (% of NAV) |
|-------------------------------------|------------------------|------------------------------------|--------------------|---------------------|-----------------------|------------------|-----------------------|
| TGI Fridays | Consumer discretionary | 100 | 2015 | 99 | 146.2 | 74% | 74% |
| Hotter Shoes | Consumer discretionary | 90 | 2014 | 84 | 19.2 | 10% | 84% |
| Total | | | | | 165.4 | 84% | |
| Other portfolio core assets | | | | | 1.1 | 1% | 85% |
| Other portfolio non-core assets | | | | | 4.0 | 2% | 87% |
| Total portfolio | | | | 183 | 170.5 | 0.9 | |
| Liquid assets | | | | | 4.5 | 2% | |
| Cash | | | | | 22.2 | 11% | |
| Other non-core assets & liabilities | | | | | (0.4) | | |
| Net asset value (NAV) | | | | | 196.9 | 100% | |

Source: Electra Private Equity as at 31 March 2021, Edison Investment Research at 24 May 2021. Note: *Company projections.

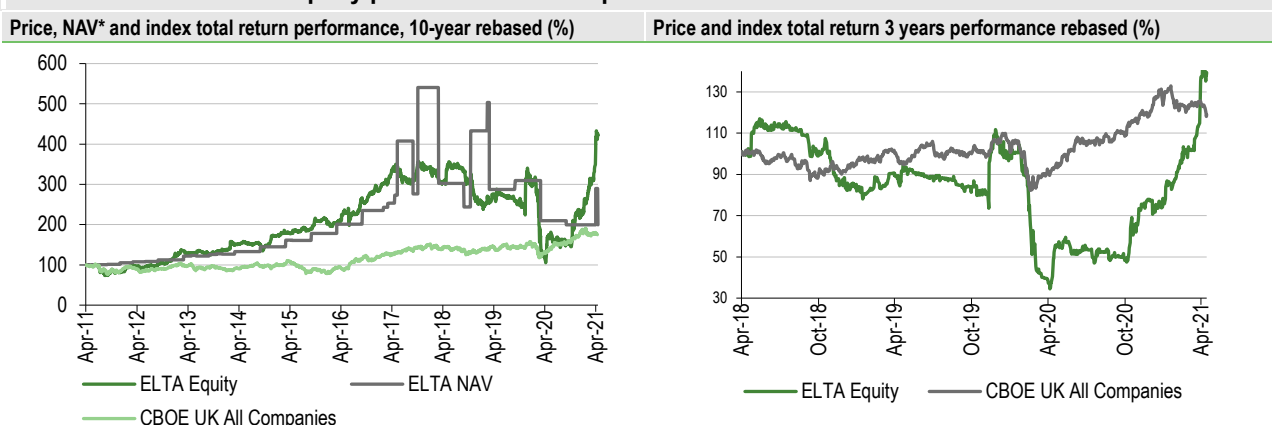
Both the Fridays and Hotter businesses have plans in place that aim to deliver long-term value creation. Fridays is a rejuvenated business with a sustainable growth strategy. It also has plans to win more market share in the casual dining market, as its recent performance indicates. Hotter has delivered on the early stages of its plan following the change in its operating model last year.

Performance and discount

Exhibit 2 illustrates the considerable improvement in ELTA's performance since November 2020 and its particular acceleration in 2021. In the last few months the company has been executing its realisation strategy and the increased NAV and narrowing discount reflect the value generated. Its performance during 2020 suffered materially, as the market discounted the hospitality industry and restaurants' shares in Q1, after the pandemic hit and lockdown was imposed in the UK.

Exhibit 2 shows that ELTA's price return was superior to UK equities over the past three and 10 years. Exhibit 3 demonstrates that ELTA's NAV outperformed the CBOE UK All Companies and MSCI Europe indices over one year and shorter periods.

Exhibit 2: Investment company performance to 30 April 2021



Source: Refinitiv, Edison Investment Research. Note: *NAV is backward looking.

Exhibit 3: Share price and NAV total return performance, relative to indices (%)

| | One month | Three months | Six months | One year | Three years | Five years | 10 years |
|---|-----------|--------------|------------|----------|-------------|------------|----------|
| Price relative to CBOE UK All Companies | 29.8 | 73.5 | 147.5 | 162.6 | 10.1 | 3.2 | 134.0 |
| NAV relative to CBOE UK All Companies | 42.4 | 44.1 | 26.7 | 1.7 | (23.1) | (25.3) | 62.3 |
| Price relative to MSCI Europe | 27.2 | 59.6 | 127.7 | 172.3 | 13.0 | 21.0 | 105.9 |
| NAV relative to MSCI Europe | 39.5 | 32.6 | 16.6 | 5.4 | (21.1) | (12.4) | 42.8 |

Source: Refinitiv, Edison Investment Research. Note: Data to end-November 2020. Geometric calculation.

We have also included peer comparison in Exhibit 4, including Dunedin Enterprise and JPEL Private Equity, which are also in a realisation mode, and the peer average of 11 (including ELTA) London-quoted private equity closed-end funds of funds. Over one year, ELTA's NAV returned 38.1%, outperforming peer group average of 26.0% and ranking third.

ELTA currently trades on a single-digit premium of 7.0%. This compares with the 15.4% discount of the peer group average and 18.4% and 26.9% discounts for Dunedin Enterprise and JPEL Private Equity, respectively.

Exhibit 4: Peer group comparison at 24 May 2021

| | Market cap £m | NAV TR 1 year (%) | NAV TR 3 year (%) | NAV TR 5 year (%) | NAV TR 10 year (%) | Discount/Premium (%) | Ongoing charge (%)* | Perf. fee | Net gearing (%) | Dividend yield (%) |
|----------------------------|---------------|-------------------|-------------------|-------------------|--------------------|----------------------|---------------------|-----------|-----------------|--------------------|
| Electra Private Equity | 193.5 | 38.1 | (4.2) | 44.4 | (5.1) | 7.0 | 1.8 | No | 98 | 0.0 |
| Dunedin Enterprise Ord | 71.8 | 14.2 | 16.6 | 57.1 | 69.8 | (18.4) | 1.3 | No | 95 | 0.5 |
| JPEL Private Equity | 79.3 | 1.4 | 2.7 | 53.5 | 58.6 | (26.9) | 1.3 | Yes | 90 | 0.0 |
| Average of 11 (incl. ELTA) | 734.4 | 26.0 | 45.6 | 99.2 | 179.3 | (15.4) | 1.3 | | 96 | 1.2 |
| ELTA's rank (of 11 peers) | 9 | 3 | 11 | 11 | 8 | 1 | 2 | | 4 | 7 |

Source: Morningstar, Edison Investment Research. Note: Performance to 24 May 2021. TR: total return. Net gearing is total assets less cash and equivalents as a percentage of net assets. The ongoing charge excludes carried interest. *Please note that in some of the peers, the ongoing charge may not fully capture the charges levied on the underlying funds.

ELTA's two remaining portfolio holdings

TGI Fridays (74% of ELTA's NAV): UK nationwide chain of American-styled casual dining restaurants

Exhibit 5: TGI Fridays investment summary

Total cost: £142m (including December 2014 £99m, July 2017 £2m and August 2017 £35m)

Source: ELTA at end March 2021

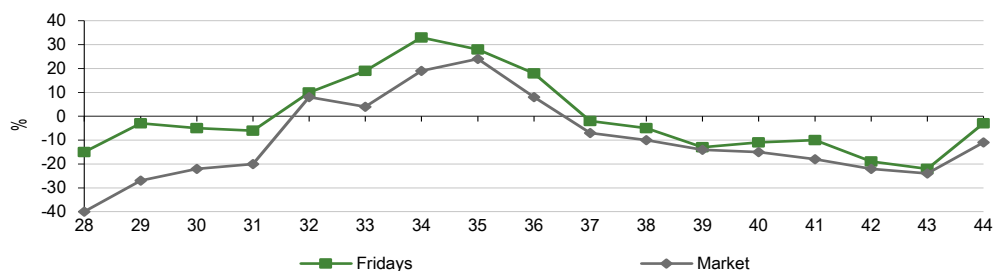
Born of the eponymous original casual dining bar and grill in 60s New York, TGI Fridays offers authentic American food, an innovative cocktail list and a high level of service at its 86 restaurants across the UK. Notwithstanding high brand awareness, the business has been newly renamed Fridays to reinforce the brand's promise of its well-known 'Friday Feeling' experience. Fridays holds exclusive UK rights to use the brand under its agreement with its American parent, from which it was acquired by ELTA in 2014.

Fridays continues to please with confirmation of robust demand on reopening (like-for-like sales at its eight Scottish sites up 14% on 2019 since 26 April despite COVID-19 restrictions) and an undimmed implementation of strategic initiatives arising from the 2019 business review. Assuming a return to trading normality, management's pro forma EBITDA projections based on demand at 2019 levels have been raised by 8% since December, thanks to the avoidance of previously anticipated 'no deal' Brexit costs. Indeed, the prospect of a favourable environment on pandemic fallout, notably pent-up demand and significantly less competition, supports confidence in management's 'best case' scenario of 10% top-line growth, translating into a step change in profit compared with 2019. While trading inactivity drove net bank debt up by over 50% to £62m in the half to March 2021, finances remain strong (liquidity headroom of c £20m and bank facilities, expiring in 2022, will be extended prior to the demerger) and should not inhibit expansion, that is self-funding of the two current dine-in openings and a further seven (Fridays and the new 63rd+1st brand) planned over coming months.

Good when allowed to open

The half to March 2021 saw the continuation of significant disruption as a result of COVID-19, with the loss of 75% of trading days (excluding the company's 'click & collect' and delivery services) and restrictions in place for the rest of the period. In October, results were 'encouraging' after two months of profitable trading post reopening after the spring lockdown. The strength of Fridays' underlying performance in 2020 is evident in its consistent outperformance of the UK restaurant market in terms of like-for-like sales (Exhibit 6). The renewed downturns in September and October highlight the boost from the government's campaign to eat out in August as well as the introduction of the 10pm curfew from 24 September and tougher regional (tier) restrictions from 15 October.

Exhibit 6: Fridays' weekly like-for-like % growth in sales from July 2020 dine-in reopening until lockdown in November 2020



Source: Fridays, Coffer Peach Business Tracker

On reopening after the recent lockdown, the trading indications for Fridays again appear positive, with like-for-like sales at its eight sites in Scotland up 14% on 2019 in the three weeks since 26 April, despite not being permitted to sell alcohol and an 8pm curfew. It was also without the benefit of outside trading as there was no available space. In England and Wales, which reopened on 17 May, the initial three days saw trading at 76% of 2019 levels, showing the strength of demand and scope to fill capacity midweek.

Strategic commitment unbowed

Management is at pains to point out that it has not been deflected by the pandemic in terms of implementing measures to enhance the core Fridays offering and develop additional revenue streams. Initial key measures already effected include a new brand identity, namely the renaming from TGI Fridays to Fridays, and, as a nod to the chain's heritage, the introduction of 'Famous At Fridays' (a focus on favourite dishes and classic cocktails) initially at 13 restaurants in larger cities and now being rolled out across the estate.

These have been complemented by further ambitious brand extensions via the company's delivery and digital channels. Click and collect takeaway is now available at about half the sites in addition to home delivery through partners (Deliveroo and Just Eat) from all outlets and by an in-house Fridays team from one site, plus a broadening of the Fridays at Home offer, for example 'Butcher's Boxes', DIY meal kits and 'Cocktails at Home.' 'Jailbreak Chicken' is a new delivery-only brand at almost a quarter of the sites, while an asset-light quick service restaurant proposition is under review. Digitalisation is being stepped up materially as a new gamification strategy, offering spontaneous rewards, is applied to the company's guest loyalty programme, Stripes (management expects to increase its database from the current 683,000 app users).

A new cocktail led bar and restaurant brand, 63rd + 1st, is being launched in Cobham, Surrey. Although visibly different from Fridays (typically c 40% smaller at 4,000 sq ft, and a focus on adults with the bar at its heart), the aim is still to cater for guest affection for the original brand. Importantly, it also meets changing market trends, notably the growing appeal of local/community all-day venues reflective of the popularity of boutique hotel and members' club environments. The Cobham site (previously Carluccio's) will have 96 covers with outdoor dining for a further 20. Deemed by management as 'a huge opportunity to drive further growth', 63rd + 1st is intended to be expanded across the UK with four further sites by early 2022.

Post-COVID-19 optimism

Despite the successful rollout of vaccines, it remains challenging to predict when trading normality will resume. Therefore, we support management's approach of using 2019 sales levels as a base for a pro forma assessment of potential annual profitability. On management's base assumption of zero like-for-like top-line growth, EBITDA (pre-IFRS 16 as in 2019) is expected to grow by 28% to £32.7m (see Exhibit 7), an increase of £2.3m on the December 2020 projection, which reflected potential costs, predominantly food, in the case of a 'no deal' Brexit. This absolute rise of £7.1m from £25.6m in 2019 derives in part from net openings in 2019, that is a full year contribution rather than part-year from five stores opened during 2019 less three removed (one closed in 2019 and two in 2020), which explains the stated £12m rise in pro forma sales despite assumed flat like-for-like assumptions. The bulk of the projected EBITDA gain is due to changes in the cost base, including labour efficiency cost savings (already implemented) and other fixed implemented cost savings (mainly rent reductions). Net bank debt of £62m at March 2021, up from September's balance of £39m (after adjusting for delayed creditor payments), reflects cash burn during protracted trading inactivity in the first half of the financial year. Management reiterates its commitment to expansion (it has medium-term development plans for about five net new sites per year). While these should still be funded from its operations, given their cash generative nature, it is also looking at capital-light quick-service (drive-in) restaurants.

Management's confidence in this zero like-for-like growth scenario appears well justified. First, market conditions were already difficult in 2019 owing to chronic overcapacity in the sector, significant cost pressures, particularly owing to labour costs, and consumer uncertainty on the eve of Brexit. The COVID-19 led reduction in supply and competition (widely estimated to be at least 20%) yields a more benign trading environment, complemented by the growing availability of properties at ever lower rents, as confirmed by restaurant operators. Secondly, there is the expected benefit of Fridays' own wide-ranging brand extension initiatives, already largely implemented and bearing early fruit in recent sustained market outperformance. These are supplemented by the addition of permanent outside trading space, the size of four restaurants, at sites in the south of England.

Consequently, on resumption of trading normality it is not unreasonable to foresee annual like-for-like sales growth rates of up to 10%, which with margin gain could drive a rise in EBITDA of over 60% on 2019 demand levels, according to management's EBITDA projections (see Exhibit 7).

Exhibit 7: Management's pro forma scenarios based on 2019 demand levels

| | 2019 actual | 0% revenue growth | 5% revenue growth | 10% revenue growth |
|-------------------------|-------------|-------------------|-------------------|--------------------|
| Revenue (£m) | 214.8 | 226.8 | 237.9 | 249.3 |
| Pre-IFRS 16 EBITDA (£m) | 25.6 | 32.7 | 36.5 | 41.3 |

Source: Company accounts

These growth scenarios take no account of Fridays' site expansion plans (typically five openings per year, which is 6% of the current estate). The noted availability of attractive sites at ever cheaper prices provides assurance that this may be achieved satisfactorily.

Valuation

Assuming 2020 to be a trading aberration and using pre IFRS 16 numbers for easier peer comparison, management's NAV of Fridays at £146.2m at March 2021 suggests an EV/EBITDA multiple of 6.4x on pro forma zero life-for-like growth on 2019 (see Exhibit 8). On a similar basis, that is pre-COVID-19 reported results, its closest listed competition, Loungers and Fulham Shore, trade on significantly higher multiples (17x and 13x, respectively). For Restaurant Group we have used the mid-point of its 'illustrative' and wide-ranging (£110m to £125m) EBITDA 'capability' on 2019 sales levels, hence some potential downside.

Exhibit 8: Peer comparison of EV/EBITDA rating, assuming return to 2019 sales levels

| Pre-IFRS16 | Share price | Management valuation £m | Historical net debt/(cash) £m | EV £m | Historical EBITDA £m | EV/EBITDA x |
|----------------------|-------------|-------------------------|----------------------------------|------------|-------------------------|----------------|
| Fridays* | | 146 | 62 (Mar 21) | 208 | Pro forma 32.7 | 6.4 |
| | | Market cap | | | 25.6 | 8.1 |
| Loungers** | 292p | 300 | 14 (Oct 20) | 314 | 18.8 | 16.7 |
| Fulham Shore*** | 17p | 105 | 6 (Feb 21) | 111 | 8.3 | 13.4 |
| Restaurant Group* | 127p | 970 | 225 (Feb 21) † | 1,195 | 118 § | 10.1 |
| Various Eateries**** | 104p | 93 | c (10) (Oct 20) ‡ | 83 | 5.3 | 15.7 |
| Average | | | | | | 14.0 |

Source: Company accounts. Note: Priced at 17 May 2021. *Year to December 2019. **Year to April 2020. ***Year to March 2020. ****Year to September 2020. † £400m less £175m gross proceeds from March 2021 capital raise. ‡ After £23m placing net proceeds. § Mid-point of management's 'illustrative' October 2020 indication of annualised EBITDA post restructuring on 2019 sales. || Adjusted run rate EBITDA.

Given its comprehensive restructuring ahead of its September 2020 IPO, we admit a caveat about our computed rating for Various Eateries. Even so, its very listing amid the pandemic endorses the opportunity for well-funded hospitality businesses. In summary, the blended average of 14x EV/EBITDA for four of its peers is more than twice that of Fridays on management's pro forma zero like-for-like growth trading assumptions (the multiple falls to 5x on management's 'best-case' 10% growth).

Hotter Shoes (10% of ELTA's NAV at 31 March 2021): A digitally led UK shoe manufacturer with a focus on customised comfort

Exhibit 9: Hotter investment summary

Total cost: £118m (including January 2014 £84m, 2017 £5m, 2018 £19m and 2019 £7.5m)

Source: ELTA at end March 2021

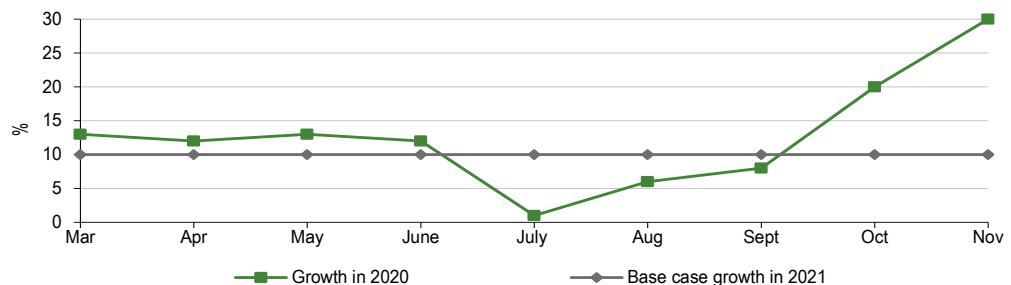
Hotter specialises in the design and manufacture of stylish comfort footwear (with 1.6m pairs manufactured in 2019, making it the UK's largest shoe manufacturer). It is renowned for its product quality and innovation as well as customer service, epitomised by its pioneering digital Footprint 3D fit technology, use of BASF's Infinergy foam inserts and over 40 width and size combinations via its Comfort Lab. The current target market is females over 55 with specific fit and comfort needs; while this is a favourable demographic, the company aims to broaden significantly its proposition. Sales are primarily through digital direct channels with a limited retail exposure (c 20 stores). Hotter's customer database exceeds four million, with one million active shoppers. 20% of sales are international, predominantly in the US, where it has a profitable and scalable operation.

Hotter's reshaping as a digital 'direct to consumer' business looks to be paying off, with 30% online sales growth in the seven months from October 2020, albeit boosted by restrictions on retail because of COVID-19. With its targeted operating model now in place (68% of revenue from direct channels in that period following 2020's retail de-risking with the closure of 70% of the UK estate), management is actively addressing opportunities in terms of both its core customers (product needs beyond comfort and fit) and a broader offering, for example menswear and safety shoes according to industry requirements. An improved digital marketing, personalisation and loyalty scheme, facilitated by a new app in Q121, is allowing enhanced management of a loyal customer base (four million, with 100,000 added annually) with long-term scope to market all manner of products and services related to footwear and customer profiles. The shops will be restyled as Technology Centres in Q221. International expansion is expected to capitalise on Hotter's successful US operation, possibly with a partner (or even a disposal), and address new markets in the Far East.

Promising financials

With Hotter's financial period under review marred by COVID-19 restrictions, it is more meaningful to look at the performance of direct channel sales, which are key to the new operating model. Exhibit 10 shows this to have been very encouraging, with double-digit percent year-on-year sales growth for the majority of the period since March 2020 lockdown and a marked acceleration in Q420.

Exhibit 10: Direct channel's year-on-year % sales growth in 2020 and management's base case of 10% growth in 2021



Source: ELTA

Taking management's reasonable approach of using FY20 sales levels as a base for a pro forma assessment of potential annual profitability, we look at its various revenue growth assumptions from

direct channels. The base case of 10% growth fits well with the performance in 2020 (see Exhibit 10). Indeed, with trading in the seven months from October up by 30% year-on-year (+44% from digital partnerships), 20% growth may be closer to the mark, even if flattered by COVID-19 retail constraints. The assumption of flat sales at the retained stores may be cautious, given their selection as optimum sites and planned conversion into Technology Centres in 2021. It is also encouraging, in terms of profit, that EBITDA for the seven months from October 2020 exceeded management's pro forma EBITDA of £5.4m for FY20 (the year to January 2020) by 8%.

Management has cut its estimate of EBITDA sensitivity to a 10% fall in retail revenue to just £0.2m (£0.5m indicated in December 2020) thanks to enhanced cost control.

Exhibit 11: Management's pro forma scenarios based on FY20 demand levels

| Year-end 31 January (£m) | 2020 actual | Direct channel revenue growth assumptions | | |
|------------------------------|-------------|---|------------|------------|
| | | 10% growth | 15% growth | 20% growth |
| Direct channels | 41.0 | 45.1 | 47.2 | 49.2 |
| % of revenue | 68% | 70% | 71% | 72% |
| Retail and wholesale Revenue | 19.5 | 19.5* | 19.5* | 19.5* |
| EBITDA | 60.5 | 64.6 | 66.7 | 68.8 |
| Margin | 5.4 | 7.3 | 8.3 | 9.2 |
| | 8.9% | 11.3% | 12.4% | 13.4% |

Source: Hotter accounts. Note: *10% reduction estimated by management to reduce EBITDA by £0.2m.

Valuation

Management's valuation of Hotter of £19.2m at March 2021 (more than trebling from £5.8m at September 2020) suggests an EV/EBITDA multiple of 4.3x pro forma 10% direct channel sales growth on FY20, assuming management forecasts. Notwithstanding residual retail exposure and the risk of executing planned business enhancements, such a rating appears unduly low. Favourable macro trends, for example a growing older population with increasing disposable incomes, a coherent strategy (largely in place) and proven management are grounds for optimism, while the joker in the pack may be Hotter's database, providing direct access to valuable customers and the opportunity to add related products and services.

Exhibit 12: Peer comparison of EV/EBITDA rating, assuming return to FY20 sales levels

| | Valuation* | Net debt* | EV | EBITDA | EV/EBITDA |
|---|------------|-----------|-------|-------------------|-----------|
| | £m | £m | £m | £m | x |
| Hotter | 19.2 | 12.0 | 31.22 | Pro forma 7.3** | 4.3 |
| | | | | Historical 5.4*** | 5.8 |
| PE (private equity) EMEA exits (consumer discretionary) in the 15 months to Sept 20 average**** | | | | | 11.1 |

Source: ELTA. Notes: *At March 2021. **Base case 10% sales growth scenario. ***Year to January 2020 adjusted for rationalisation of retail estate as a result of August 2020 CVA. ****S&P Global Market Intelligence as of Nov 2020.

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