

REDINGTON INDIA

Temporary slip; Outlook strong

India Equity Research | IT

Redington India (Redington) reported weaker-than-expected top line—up 4.8% YoY versus 10.5% Street’s estimate—on weakness in India business (down 3.9% YoY). Overseas business reported strong 10.0% YoY growth despite currency depreciation and challenging business environment in Turkey. EBITDA margin fell 12bps YoY as gross margin dipped 29bps due to change in business mix. Management expects performance to improve in FY19 riding increasing traction in India IT business and momentum in overseas business. We maintain positive outlook on the company as: 1) higher commodity prices driving strong demand in MEA region; 2) GST-led bounce back in India business; and 3) strong traction in ProConnect business (up 58% YoY in Q4FY18). Maintain ‘BUY’ with TP of INR166 (10x FY20E EPS).

Mobility weakness impacts India growth

Redington’s India business grew 2% YoY, adjusting for tax accounting, as while India IT business grew 11%, mobility business declined 34%. Management attributed weakness in mobility business to increase in customs duty leading to higher inventory in the channel. We believe, lower mobility growth could be due to significantly high price of iPhone X leading to lower demand. We expect the issue to be addressed post new iPhone launch, which is likely see refresh of older models at lower price points.

Overseas business strong despite Turkey dampener

The company’s overseas business reported 10.0% YoY growth; 13.6% adjusting for currency translation, despite challenges in Turkey business. Adjusting for Turkey business, revenue growth in overseas business was 11.0%. The company is participating in larger IT projects such as Smart Cities, which have longer credit cycles, leading to five days YoY increase in working capital cycle in India, while overall working capital days have increased by one day YoY to 40 days.

Outlook and valuations: Attractive; maintain ‘BUY’

We expect business tailwinds, operational excellence and GST benefits to lead to better margin, inturn spurring earnings growth. We believe, valuation at 7.4x FY20E EPS is attractive given improving returns profile. We expect valuation to expand over the medium to long term as high value-added businesses achieve scale. We maintain ‘BUY/SO’ with TP of INR166 (10x FY20E EPS).

Financials

(INR mn)

| Year to March | Q4FY18 | Q3FY18 | % Chg | Q4FY17 | % Chg | FY18 | FY19E | FY20E |
|-------------------|---------|---------|-------|---------|-------|---------|---------|---------|
| Net revenues | 113,140 | 117,284 | (3.5) | 107,950 | 4.8 | 434,594 | 484,447 | 543,092 |
| EBITDA | 2,321 | 2,099 | 10.5 | 2,340 | (0.8) | 8,163 | 9,475 | 10,827 |
| Adjusted Profit | 1,433 | 1,274 | 12.5 | 1,527 | (6.2) | 4,816 | 5,641 | 6,635 |
| Diluted EPS (INR) | 3.6 | 3.2 | 12.6 | 3.8 | (6.3) | 12.0 | 14.1 | 16.6 |
| Diluted P/E (x) | | | | | | 10.2 | 8.7 | 7.4 |
| EV/EBITDA (x) | | | | | | 7.6 | 6.5 | 5.7 |
| EV/Revenues (x) | | | | | | 0.1 | 0.1 | 0.1 |

EDELWEISS 4D RATINGS

| Absolute Rating | BUY |
|--------------------------------|-------------|
| Rating Relative to Sector | Outperform |
| Risk Rating Relative to Sector | Low |
| Sector Relative to Market | Equalweight |

MARKET DATA (R: REDI.BO, B: REDI IN)

| | |
|------------------------------|-------------|
| CMP | : INR 123 |
| Target Price | : INR 166 |
| 52-week range (INR) | : 210 / 121 |
| Share in issue (mn) | : 400.2 |
| M cap (INR bn/USD mn) | : 51 / 776 |
| Avg. Daily Vol.BSE/NSE('000) | : 638.8 |

SHARE HOLDING PATTERN (%)

| | Current | Q3FY18 | Q2FY18 |
|---|---------|--------|--------|
| Promoters * | 0.0 | 0.0 | 0.0 |
| MF's, FI's & BK's | 20.0 | 20.5 | 21.0 |
| FII's | 38.1 | 36.6 | 35.6 |
| Others | 41.9 | 42.8 | 43.4 |
| * Promoters pledged shares (% of share in issue) | : | NIL | |

RELATIVE PERFORMANCE (%)

| | Sensex | Stock | Stock over Sensex |
|-----------|--------|--------|----------------------|
| 1 month | 1.2 | (16.6) | (17.8) |
| 3 months | 3.2 | (17.3) | (20.5) |
| 12 months | 14.4 | (4.2) | (18.6) |

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Chart 1: Overseas revenue momentum strong

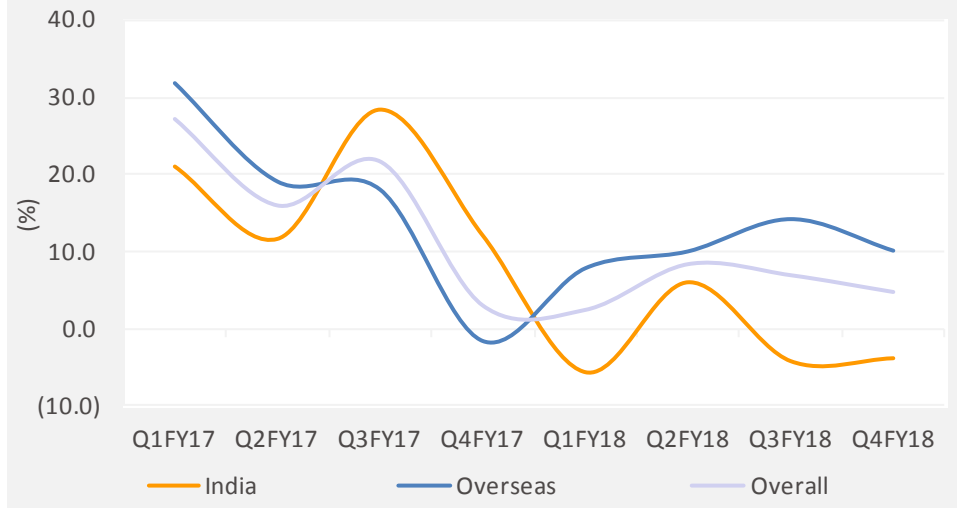


Chart 2: Working capital days increased by 1 day YoY to 40 days

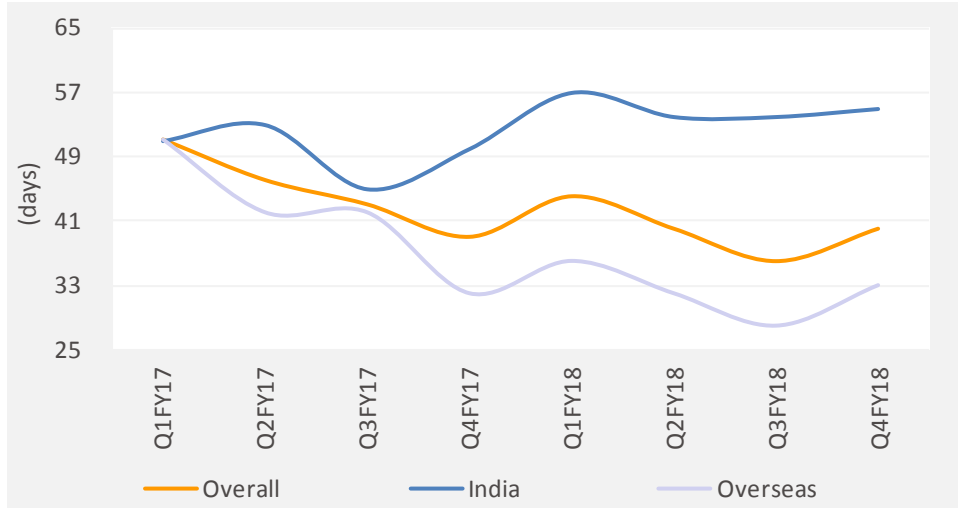


Chart 3: ProConnect continued robust growth momentum...

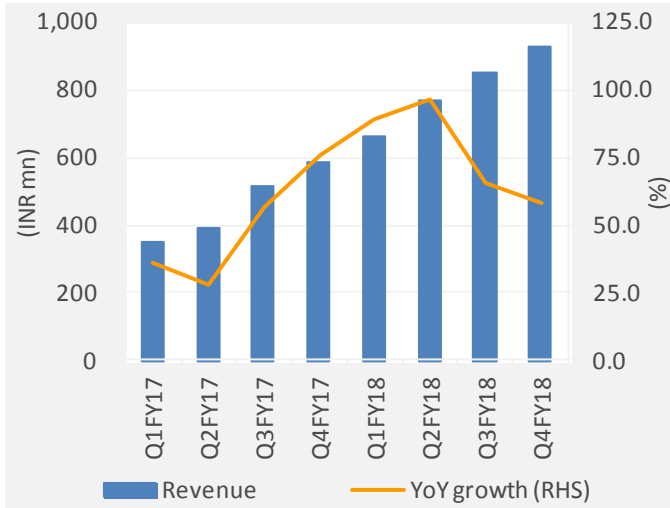
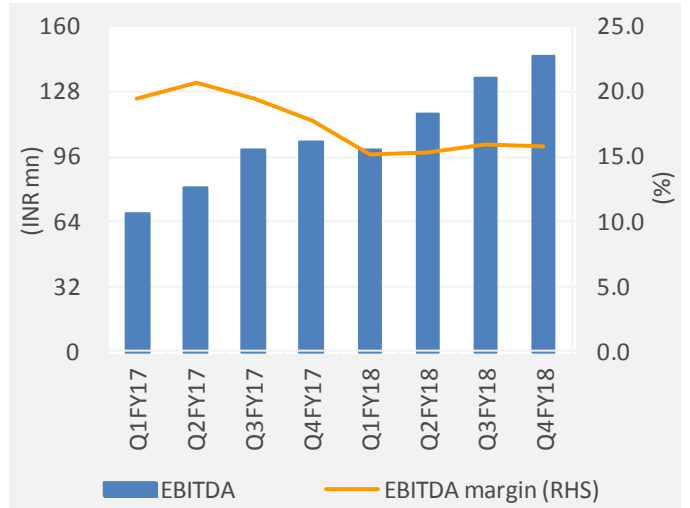


Chart 4: while maintaining EBITDA margins



Source: Company, Edelweiss research

Financial snapshot

(INR mn)

| Year to March | Q4FY18 | Q3FY18 | % Change | Q4FY17 | % Change | FY18 | FY19E | FY20E |
|------------------------|---------|---------|----------|---------|----------|---------|---------|---------|
| Net revenues | 113,140 | 117,284 | (3.5) | 107,950 | 4.8 | 434,594 | 484,447 | 543,092 |
| Direct costs | 106,649 | 111,324 | (4.2) | 101,444 | 5.1 | 410,566 | 457,855 | 513,446 |
| Gross profit | 6,492 | 5,960 | 8.9 | 6,506 | (0.2) | 24,028 | 26,592 | 29,646 |
| SG&A | 4,171 | 3,861 | 8.0 | 4,166 | 0.1 | 15,865 | 17,116 | 18,819 |
| EBITDA | 2,321 | 2,099 | 10.5 | 2,340 | (0.8) | 8,163 | 9,475 | 10,827 |
| Depreciation | 140 | 149 | (5.5) | 138 | 1.7 | 569 | 645 | 694 |
| EBIT | 2,180 | 1,951 | 11.8 | 2,202 | (1.0) | 7,594 | 8,830 | 10,133 |
| Interest | 485 | 388 | 24.9 | 378 | 28.3 | 1,680 | 1,617 | 1,564 |
| Other income | 137 | 98 | 39.7 | 181 | (24.4) | 392 | 353 | 276 |
| Profit before tax | 1,830 | 1,674 | 9.3 | 1,999 | (8.5) | 6,278 | 7,495 | 8,777 |
| Tax | 397 | 400 | (0.8) | 472 | (15.9) | 1,462 | 1,854 | 2,142 |
| Add: Exceptional items | | | | | | | | |
| Reported net profit | 1,433 | 1,274 | 12.5 | 1,527 | (6.2) | 4,816 | 5,641 | 6,635 |
| Exceptional items | | | | | | | | |
| Adjusted Profit | 1,433 | 1,274 | 12.5 | 1,527 | (6.2) | 4,816 | 5,641 | 6,635 |
| Diluted EPS (INR) | 3.6 | 3.2 | 12.6 | 3.8 | (6.3) | 12.0 | 14.1 | 16.6 |
| Diluted P/E (x) | - | - | - | - | - | 10.2 | 8.7 | 7.4 |
| EV/EBITDA (x) | - | - | - | - | - | 7.6 | 6.5 | 5.7 |
| EV/Revenues (x) | - | - | - | - | - | 0.1 | 0.1 | 0.1 |
| Direct costs | 94.3 | 94.9 | - | 94.0 | - | 94.5 | 94.5 | 94.5 |
| Gross profit | 5.7 | 5.1 | - | 6.0 | - | 5.5 | 5.5 | 5.5 |
| SG&A | 3.7 | 3.3 | - | 3.9 | - | 3.7 | 3.5 | 3.5 |
| EBITDA | 2.1 | 1.8 | - | 2.2 | - | 1.9 | 2.0 | 2.0 |
| EBIT | 1.9 | 1.7 | - | 2.0 | - | 1.7 | 1.8 | 1.9 |
| Reported net profit | 1.3 | 1.1 | - | 1.4 | - | 1.1 | 1.2 | 1.2 |
| Tax rate | 21.7 | 23.9 | - | 23.6 | - | 23.3 | 24.7 | 24.4 |

Company Description

Redington commenced its business operations in 1993 as distributor for HP Printers in India and slowly started foraying into distribution of other PC components. From being a single brand distributor in 1993, the company has now established partnerships with more than 200 leading global brands spread across 24 countries. Its business model has evolved from volume-driven products like printers and PCs along with components like hard disks, memory chips and processors to value-oriented technology distribution offering enterprise and infrastructure products. Redington has graduated to emerge an integrated services and solutions partner.

Investment Theme

Redington India (Redington), a leading technology distributor with a track record of tackling technology as well as economic cycles, is fundamentally well poised to ride business tailwinds and investments in sunrise segments. We expect the company to reap benefits of: 1) higher commodity prices driving strong demand in MEA region; 2) GST-led bounce back in India business; and 3) strong traction in third party logistics (3PL) business.

Key Risks

- Redington's revenue is majorly driven by success of its top-five brands, which contribute ~60% of revenues. As such, any loss of major vendor or significant reduction in business could materially impact revenues.
- The company's business operations also carry geo-political and currency risks given its diversified presence across India, South Asia, the Middle East, Turkey, Africa (META) and CIS region.
- Redington sells its products to small and large format retailers giving them credit period of 30-60 days. Though the company partly manages risks through credit insurance and factoring, inability or unwillingness to repay by some key channel partners/retailers, could adversely affect its profitability.

Financial Statements

Key Assumptions

| Year to March | FY17 | FY18 | FY19E | FY20E |
|-----------------------------|------|-------|-------|-------|
| Macro | | | | |
| GDP(Y-o-Y %) | 6.6 | 6.5 | 7.1 | 7.6 |
| Inflation (Avg) | 4.5 | 3.8 | 4.5 | 5.0 |
| Repo rate (exit rate) | 6.3 | 6.0 | 6.0 | 6.5 |
| USD/INR (Avg) | 67.1 | 64.5 | 66.0 | 66.0 |
| Company | | | | |
| India revenue growth (%) | 18.0 | (2.1) | 9.3 | 11.9 |
| Overseas revenue growth (%) | 14.9 | 10.6 | 12.6 | 12.2 |

Cost Assumptions

| | | | | |
|----------------------|------|------|------|------|
| Direct costs | 94.5 | 94.5 | 94.5 | 94.6 |
| Employee benefit exp | 1.5 | 1.5 | 1.5 | 1.4 |
| Other exp. | 2.0 | 2.1 | 2.1 | 2.0 |

Income statement

(INR mn)

| Year to March | FY17 | FY18 | FY19E | FY20E |
|--------------------------|---------|---------|---------|---------|
| Net revenue | 411,147 | 434,594 | 484,447 | 543,092 |
| Cost of revenues | 388,245 | 410,566 | 457,855 | 513,446 |
| Gross profit | 22,902 | 24,028 | 26,592 | 29,646 |
| Total SG&A expenses | 14,653 | 15,865 | 17,116 | 18,819 |
| EBITDA | 8,248 | 8,163 | 9,475 | 10,827 |
| Depreciation | 547 | 569 | 645 | 694 |
| EBIT | 7,702 | 7,594 | 8,830 | 10,133 |
| Add: Other income | 413.9 | 392.4 | 352.66 | 275.64 |
| Profit Before Tax | 6,545 | 6,306 | 7,567 | 8,844 |
| Less: Provision for Tax | 1,778 | 1,462 | 1,854 | 2,142 |
| Reported Profit | 4,642 | 4,816 | 5,641 | 6,635 |
| Adjusted Profit | 4,642 | 4,816 | 5,641 | 6,635 |
| Shares o /s (mn) | 400 | 400 | 400 | 400 |
| Adjusted Basic EPS | 11.6 | 12.0 | 14.1 | 16.6 |
| Diluted shares o/s (mn) | 400 | 400 | 400 | 400 |
| Adjusted Diluted EPS | 11.6 | 12.0 | 14.1 | 16.6 |
| Adjusted Cash EPS | 13.0 | 13.5 | 15.7 | 18.3 |
| Dividend per share (DPS) | 4.1 | 4.1 | 4.8 | 5.7 |
| Dividend Payout Ratio(%) | 41.6 | 40.0 | 40.0 | 40.0 |

Common size metrics

| Year to March | FY17 | FY18 | FY19E | FY20E |
|--------------------|------|------|-------|-------|
| Cost of revenues | 94.4 | 94.5 | 94.5 | 94.5 |
| Gross margin | 5.6 | 5.5 | 5.5 | 5.5 |
| SG&A expenses | 3.6 | 3.7 | 3.5 | 3.5 |
| EBITDA margins | 2.0 | 1.9 | 2.0 | 2.0 |
| EBIT margins | 1.9 | 1.7 | 1.8 | 1.9 |
| Net Profit margins | 1.2 | 1.1 | 1.2 | 1.2 |

Growth ratios (%)

| Year to March | FY17 | FY18 | FY19E | FY20E |
|-----------------|------|-------|-------|-------|
| Revenues | 16.0 | 5.7 | 11.5 | 12.1 |
| EBITDA | 7.1 | (1.0) | 16.1 | 14.3 |
| PBT | 10.9 | (3.7) | 20.0 | 16.9 |
| Adjusted Profit | 9.7 | 3.8 | 17.1 | 17.6 |
| EPS | 9.7 | 3.7 | 17.1 | 17.6 |

| Balance sheet | | (INR mn) | | | |
|--------------------------|---------------|---------------|---------------|---------------|--|
| As on 31st March | FY17 | FY18 | FY19E | FY20E | |
| Share capital | 800 | 800 | 800 | 800 | |
| Reserves & Surplus | 30,679 | 34,505 | 37,890 | 41,871 | |
| Shareholders' funds | 31,479 | 35,305 | 38,690 | 42,671 | |
| Minority Interest | 3,615 | 3,588 | 3,660 | 3,727 | |
| Def. Tax Liability (net) | (138) | (236) | (251) | (251) | |
| Sources of funds | 50,114 | 53,235 | 55,635 | 58,683 | |
| Net Block | 1,960 | 1,860 | 2,189 | 2,234 | |
| Capital work in progress | 5 | 28 | 28 | 28 | |
| Intangible Assets | 2,800 | 3,017 | 2,686 | 2,618 | |
| Total Fixed Assets | 4,765 | 4,905 | 4,903 | 4,880 | |
| Non current investments | 48 | 35 | 35 | 35 | |
| Cash and Equivalents | 7,212 | 5,413 | 4,593 | 3,212 | |
| Sundry Debtors | 50,873 | 60,726 | 63,817 | 73,714 | |
| Loans & Advances | 364 | 469 | 469 | 469 | |
| Other Current Assets | 3,516 | 5,783 | 5,783 | 5,783 | |
| Current Assets (ex cash) | 88,499 | 98,044 | 106,035 | 116,744 | |
| Trade payable | 44,618 | 46,840 | 52,426 | 58,684 | |
| Other Current Liab | 5,792 | 8,321 | 7,505 | 7,505 | |
| Total Current Liab | 50,410 | 55,161 | 59,931 | 66,189 | |
| Net Curr Assets-ex cash | 38,089 | 42,883 | 46,104 | 50,555 | |
| Uses of funds | 50,114 | 53,235 | 55,635 | 58,683 | |
| BVPS (INR) | 78.7 | 88.2 | 96.7 | 106.6 | |

| Free cash flow | | (INR mn) | | | |
|-----------------------|---------------|--------------|--------------|--------------|--|
| Year to March | FY17 | FY18 | FY19E | FY20E | |
| Reported Profit | 4,642 | 4,816 | 5,641 | 6,635 | |
| Add: Depreciation | 547 | 569 | 645 | 694 | |
| Interest (Net of Tax) | 1,144 | 1,291 | 1,220 | 1,185 | |
| Others | 477 | (133) | 932 | 170 | |
| Less: Changes in WC | (6,677) | 4,794 | 3,221 | 4,452 | |
| Operating cash flow | 13,486 | 1,750 | 5,217 | 4,233 | |
| Less: Capex | 640 | 648 | 693 | 670 | |
| Free Cash Flow | 12,846 | 1,102 | 4,523 | 3,562 | |

| Cash flow metrics | | | | | |
|---------------------|----------|---------|---------|---------|--|
| Year to March | FY17 | FY18 | FY19E | FY20E | |
| Operating cash flow | 13,486 | 1,750 | 5,217 | 4,233 | |
| Financing cash flow | (634) | (255) | (341) | (395) | |
| Investing cash flow | (11,197) | (4,230) | (4,873) | (5,218) | |
| Net cash Flow | 1,654 | (2,735) | 3 | (1,381) | |
| Capex | (640) | (648) | (693) | (670) | |
| Dividend paid | (1,931) | (1,927) | (2,256) | (2,654) | |

| Profitability and efficiency ratios | | | | | |
|-------------------------------------|------|------|-------|-------|--|
| Year to March | FY17 | FY18 | FY19E | FY20E | |
| ROACE (%) | 15.4 | 15.5 | 16.9 | 18.2 | |
| ROAE (%) | 14.0 | 13.1 | 14.1 | 15.1 | |
| Inventory Days | 34 | 29 | 27 | 26 | |
| Debtors Days | 46 | 47 | 47 | 46 | |
| Payable Days | 41 | 41 | 40 | 39 | |
| Cash Conversion Cycle | 39 | 35 | 34 | 33 | |
| Current Ratio | 1.9 | 1.9 | 1.8 | 1.8 | |

| Operating ratios | | | | | |
|----------------------|------|------|-------|-------|--|
| Year to March | FY17 | FY18 | FY19E | FY20E | |
| Total Asset Turnover | 7.8 | 8.4 | 8.9 | 9.5 | |
| Fixed Asset Turnover | 83.2 | 89.9 | 98.8 | 111.0 | |
| Equity Turnover | 13.5 | 13.0 | 13.1 | 13.4 | |

| Valuation parameters | | | | | |
|-------------------------|------|------|-------|-------|--|
| Year to March | FY17 | FY18 | FY19E | FY20E | |
| Adj. Diluted EPS (INR) | 11.6 | 12.0 | 14.1 | 16.6 | |
| Y-o-Y growth (%) | 9.7 | 3.7 | 17.1 | 17.6 | |
| Adjusted Cash EPS (INR) | 13.0 | 13.5 | 15.7 | 18.3 | |
| Diluted P/E (x) | 10.6 | 10.2 | 8.7 | 7.4 | |
| P/B (x) | 1.6 | 1.4 | 1.3 | 1.2 | |
| EV / Sales (x) | 0.1 | 0.1 | 0.1 | 0.1 | |
| EV / EBITDA (x) | 7.3 | 7.6 | 6.5 | 5.7 | |
| Dividend Yield (%) | 3.4 | 3.4 | 3.9 | 4.6 | |

Additional Data

Directors Data

| | | | |
|----------------------|----------------------|-----------------------|----------------------|
| Mr. Raj Shankar | MD & CEO | Mr. S. V. Krishnan | CFO |
| Prof. J Ramachandran | Independent director | Mr. Keith W F Bradley | Independent director |
| Mr. V. S. Hariharan | Independent director | Mr. EH Kasturi Ranjan | Independent director |
| Ms. Chen, Yi-Ju | Independent director | Mr. Tu, Shu-Chyuan | Independent director |
| Mr. Udai Dhawan | Independent director | Mr. B. Ramaratnam | Independent director |

Auditors - M/s Deloitte Haskins & Sells

**as per last annual report*

Holding – Top10

| | Perc. Holding | | Perc. Holding |
|----------------------|---------------|----------------------|---------------|
| Synnex mauritius ltd | 23.56 | Fmr llc | 9.95 |
| Marina iv sgp pteltd | 9.85 | Hdfc asset managemen | 8.91 |
| Standard chartered | 8.8 | Harrow investment ho | 8.19 |
| Icici prudential lif | 6.56 | Franklin resources | 6.01 |
| Sbi funds management | 3.77 | Fiam group trust | 3 |

**in last one year*

Bulk Deals

| Data | Acquired / Seller | B/S | Qty Traded | Price |
|-------------|--|------|------------|--------|
| 13 Jul 2017 | Morgan Stanley Investment Funds Indian Equity Fund | Buy | 7534460 | 141.40 |
| 13 Jul 2017 | Local Government Superannuation Scheme | Sell | 7534460 | 141.40 |
| 06 Jul 2017 | Harrow Investment Holding Ltd | Sell | 19950000 | 125.10 |
| 06 Jul 2017 | Norges Bank On Account Of The Government Pension Fund Global | Buy | 11950000 | 125.00 |
| 06 Jul 2017 | Reliance Mutual Fund | Buy | 7000000 | 125.00 |

**in last one year*

Insider Trades

| Reporting Data | Acquired / Seller | B/S | Qty Traded |
|----------------|-----------------------------------|------|-------------|
| 10 Jul 2017 | Harrow Investment Holding Limited | Sell | 32777599.00 |

**in last one year*

| Company | Absolute reco | Relative reco | Relative risk | Company | Absolute reco | Relative reco | Relative Risk |
|-----------------------------|---------------|---------------|---------------|---------------------------|---------------|---------------|---------------|
| Cyient | BUY | SP | H | ECLERX SERVICES | HOLD | SP | M |
| HCL Technologies | BUY | SP | H | Hexaware Technologies | HOLD | SP | M |
| Info Edge | BUY | SP | M | Infosys | BUY | SO | L |
| Just Dial | HOLD | SU | M | L&T Infotech Ltd | BUY | SO | M |
| L&T Technology Services Ltd | BUY | SO | M | Persistent Systems | BUY | SP | L |
| Redington India Ltd | BUY | SO | L | Tata Consultancy Services | HOLD | SP | L |
| Tech Mahindra | BUY | SP | M | Wipro | HOLD | SP | L |

ABSOLUTE RATING

| Ratings | Expected absolute returns over 12 months |
|---------|--|
| Buy | More than 15% |
| Hold | Between 15% and - 5% |
| Reduce | Less than -5% |

RELATIVE RETURNS RATING

| Ratings | Criteria |
|----------------------------|-------------------------------------|
| Sector Outperformer (SO) | Stock return > 1.25 x Sector return |
| Sector Performer (SP) | Stock return > 0.75 x Sector return |
| | Stock return < 1.25 x Sector return |
| Sector Underperformer (SU) | Stock return < 0.75 x Sector return |

Sector return is market cap weighted average return for the coverage universe within the sector

RELATIVE RISK RATING

| Ratings | Criteria |
|------------|---------------------------------------|
| Low (L) | Bottom 1/3rd percentile in the sector |
| Medium (M) | Middle 1/3rd percentile in the sector |
| High (H) | Top 1/3rd percentile in the sector |

Risk ratings are based on Edelweiss risk model

SECTOR RATING

| Ratings | Criteria |
|------------------|-------------------------------------|
| Overweight (OW) | Sector return > 1.25 x Nifty return |
| Equalweight (EW) | Sector return > 0.75 x Nifty return |
| | Sector return < 1.25 x Nifty return |
| Underweight (UW) | Sector return < 0.75 x Nifty return |

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Aditya Narain

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Coverage group(s) of stocks by primary analyst(s): IT

Cyient, ECLERX SERVICES, HCL Technologies, Hexaware Technologies, Infosys, Info Edge, Just Dial, L&T Infotech Ltd, L&T Technology Services Ltd, Persistent Systems, Redington India Ltd, Tata Consultancy Services, Tech Mahindra, Wipro

Recent Research

| Date | Company | Title | Price (INR) | Recos |
|-----------|--|---|-------------|-------|
| 10-May-18 | Redington | In step with the times; <i>Initiating Coverage</i> | 131 | Buy |
| 07-May-18 | Global Pulse: Cognizant | Digital shift potent booster; <i>Result Excerpts</i> | | |
| 04-May-18 | Cyient | Well entrenched on growth path; <i>Event Update</i> | 807 | Buy |

Distribution of Ratings / Market Cap

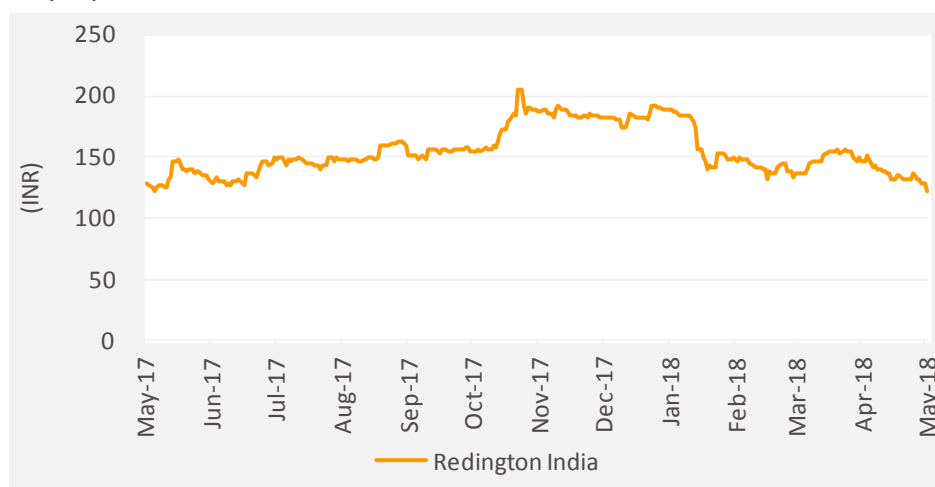
Edelweiss Research Coverage Universe

| | Buy | Hold | Reduce | Total |
|------------------------|--------|------------------------|--------|-------|
| Rating Distribution* | 161 | 67 | 11 | 240 |
| * 1stocks under review | | | | |
| | > 50bn | Between 10bn and 50 bn | < 10bn | |
| Market Cap (INR) | 156 | 62 | 11 | |

Rating Interpretation

| Rating | Expected to |
|---------------|---|
| Buy | appreciate more than 15% over a 12-month period |
| Hold | appreciate up to 15% over a 12-month period |
| Reduce | depreciate more than 5% over a 12-month period |

One year price chart



DISCLAIMER

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