

November 3, 2022

Q2FY23 Result Update

☑ Change in Estimates | ☑ Target | ■ Reco

Change in Estimates

| | Current | | Previous | |
|--------------|---------|--------|----------|--------|
| | FY24E | FY25E | FY24E | FY25E |
| Rating | HOLD | | HOLD | |
| Target Price | 230 | | 200 | |
| NII (Rs.) | 65,724 | 75,430 | 65,724 | 75,430 |
| % Chng. | - | - | - | - |
| PPoP (Rs.) | 38,148 | 42,005 | 38,148 | 42,005 |
| % Chng. | - | - | - | - |
| EPS (Rs.) | 13.7 | 15.4 | 13.1 | 14.8 |
| % Chng. | 4.2 | 4.0 | - | - |

Key Financials - Standalone

| Y/e Mar | FY22 | FY23E | FY24E | FY25E |
|---------------------|--------|--------|--------|--------|
| Net Int.Inc. (Rs m) | 57,378 | 58,781 | 65,724 | 75,430 |
| Growth (%) | 1.3 | 2.4 | 11.8 | 14.8 |
| Op. Profit (Rs m) | 37,252 | 35,995 | 38,148 | 42,005 |
| PAT (Rs m) | 9,888 | 15,598 | 16,869 | 18,938 |
| EPS (Rs.) | 8.0 | 12.7 | 13.7 | 15.4 |
| Gr. (%) | 121.1 | 57.7 | 8.1 | 12.3 |
| DPS (Rs.) | 0.3 | 0.8 | 1.2 | 1.3 |
| Yield (%) | 0.1 | 0.3 | 0.5 | 0.6 |
| Margin (%) | 8.5 | 7.7 | 7.8 | 7.9 |
| RoAE (%) | 6.5 | 9.7 | 9.8 | 10.2 |
| RoAA (%) | 1.3 | 1.9 | 1.9 | 2.0 |
| PE (x) | 27.4 | 17.4 | 16.1 | 14.3 |
| P/BV (x) | 1.7 | 1.6 | 1.5 | 1.4 |
| P/ABV (x) | 2.3 | 2.2 | 1.9 | 1.7 |

Key Data

MMFS.BO | MMFS IN

| | | |
|---------------------|---------------------|--|
| 52-W High / Low | Rs.235 / Rs.128 | |
| Sensex / Nifty | 60,836 / 18,053 | |
| Market Cap | Rs.272bn/ \$ 3,278m | |
| Shares Outstanding | 1,236m | |
| 3M Avg. Daily Value | Rs.1140.12m | |

Shareholding Pattern (%)

| | |
|-------------------------|-------|
| Promoter's | 52.36 |
| Foreign | 16.93 |
| Domestic Institution | 22.12 |
| Public & Others | 8.60 |
| Promoter Pledge (Rs bn) | - |

Stock Performance (%)

| | 1M | 6M | 12M |
|----------|------|------|------|
| Absolute | 22.3 | 20.8 | 12.4 |
| Relative | 14.2 | 13.2 | 10.5 |

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Mahindra & Mahindra Financial Services (MMFS IN)

Rating: HOLD | CMP: Rs220 | TP: Rs230

Decent Set, Strong Growth Seen

Quick Pointers:

- Asset Quality improved with GS3 at 6.7% v/s 8.0% in Q1'23.
- Provisions of Rs 1.9bn taken this quarter including write-offs of Rs5.3bn

MMFS reported a decent set of numbers with PAT coming in at Rs4.4 bn above our estimates of Rs 2.2bn due to sharp drop in provisions. Provisions at Rs1.9bn dropped sharply from Rs 6.4bn in Q1'23 as collection efficiencies showed improvement. Write-offs of Rs5.3bn was taken in this quarter compared to Rs5.7bn taken in Q1'23. SME and new businesses AUM recorded 60% QoQ growth could be a major growth driver. Tractors/Cars showed positive QoQ AUM growth of 2.9%/5% respectively after seeing a de-growth in the last quarter.

Our FY23 and FY24 EPS estimates are upgraded by 2.9%/4.2% respectively as we cut our provisions estimates of FY23/FY24 by .86%/2.1% as collection efficiency has improved and management does not foresee any impairment charge on account of IRAC migration in FY23 . One has to closely monitor the growth and credit costs in the upcoming quarters. We maintain our 'HOLD' rating on the stock and increase our price target to Rs 230 from Rs 200 as we value MMFS at 1.9x PABV Sep'24E.

- Loan growth sustainability is the key:** AUMs witnessed a growth of 21.6% YoY and 10.2% QoQ at Rs695bn [vs. PLe of Rs656bn]. Disbursements for the quarter clocked healthy 82.6%YoY/24.8% QoQ growth led by strong growth in SME & others (+81.0% QoQ) along with growth in auto/utility/pre-owned/cars. Disbursements in October 2022 was strong and came in at Rs 52.5bn. NIM contracted to 7.7% vs 8.37% in Q1'23 due to change in product mix to low yielding products, increased financing to affluent customers, higher liquidity buffer of 4 months and 26bps increase in cost of funds to 6.73% from 6.47% in Q1'23.
- Asset quality showed improvement, write-offs remain elevated:** GNPA at 6.7% stood lower than our estimates [vs. PLe of 7.8%] as against 8.0% in Q4'22 and 12.7% in Q2'22. Provisions at Rs 1.9bn dropped sharply on a QoQ basis vs Rs6.4bn recorded in Q1'23 [vs. PLe of Rs 6.5bn]. Credit charge includes Rs.6bn Stage 1 provisions, write back of Rs1.2bn stage 2 provisions, Rs2.8bn write back of stage3 provisions and write-off of Rs 5.4bn. Stage 3 provision cover remained stable at 58% QoQ. Company made a one time provision of Rs 550mn for joint venture in Sri Lanka. Business is profit making, but the company is looking to resize its business. On asset quality, company is comfortable with GNPA of 5-6% and NNPA of 2-2.5%.

PAT came in at Rs4.4bn above our estimates [vs. PLe of Rs2.3bn] mainly due to sharp fall in provisions.

NII came below our estimates and rose by 1.6% YoY but fell 2.4% QoQ to Rs15.1bn below our estimates [vs. PLe of Rs16.0bn] due to lower yields as yields fell to 15.59% vs 16.10% in Q1'23 due to change in product mix and cost of borrowing increased to 6.73% vs 6.47% in Q1'23. Hence NIM moderated to 7.7% vs 8.3% in Q1'23.

PPoP fell 15.0% YoY and 8.7%QoQ to Rs8.6bn below our estimates [vs. PLe of Rs9.7bn] due to elevated opex (up 37.8% YoY/ 9% QoQ) and lower NII growth.

Provisions at Rs 1.9bn dropped sharply on a QoQ basis vs Rs6.4bn recorded in Q1'23 [vs. PLe of Rs 6.5bn]. Credit charge includes Rs.6bn Stage 1 provisions, write back of Rs1.2bn stage 2 provisions, write back of Rs2.8bn stage3 provisions and write-off of 5.4bn . Write-offs continue to remain elevated, as of H1FY23 company has written off Rs11.14bn worth of loans vs Rs6.9bn in H1FY22

GNPA at 6.7% stood better than our estimates [vs. PLe of 7.8%] vs 8.0% in Q1FY23. NNPA also saw a decrease on a QoQ basis and came in at 2.9% vs 3.5% in Q1'23

AUM witnessed a good growth of 10.2% QoQ and 21.6% YoY at Rs695bn [vs. PLe of Rs656.0bn], Used Vehicles, CV/CE and auto/utility vehicles saw a strong QoQ growth of 10.2%,1.1% and 6.8% respectively. Tractors and cars segment also saw a positive 5% and 3% QoQ growth respectively.

Exhibit 1: Strong QoQ reduction in provisions lead to PAT beat

| (Rs m) | Q2FY23 | Q2FY22 | YoY gr. | Q1FY23 | QoQ gr. |
|--------------------------------|-----------------|-----------------|---------------|-----------------|---------------|
| Interest Income | 25,858 | 25,079 | 3.1% | 24,863 | 4.0% |
| Interest Expenses | 10,688 | 10,151 | 5.3% | 9,320 | 14.7% |
| Net Interest Income | 15,170 | 14,928 | 1.6% | 15,544 | -2.4% |
| Other Income | 235 | 145 | 62.0% | 122 | 91.8% |
| Total Income | 15,405 | 15,073 | 2.2% | 15,666 | -1.7% |
| Total Operating Expenses | 6,768 | 4,910 | 37.8% | 6,208 | 9.0% |
| Operating Profit (PPP) | 8,637 | 10,163 | -15.0% | 9,458 | -8.7% |
| Provisions & Write Offs | 1,985 | -3,668 | -154.1% | 6,453 | -69.2% |
| PBT | 6,652 | 13,831 | -51.9% | 3,005 | 121.4% |
| Exceptionals | 0 | 0 | | 0 | |
| Reported Profit | 4,483 | 10,229 | -56.2% | 2,229 | 101.1% |
| Assets Under Management | 6,95,640 | 5,71,960 | 21.6% | 6,30,990 | 10.2% |
| Off-Balance Sheet AUM | | | | | |
| NIM | 7.7% | 8.57% | -89 | 8.37% | -69 |
| AUM (Rs mn) | 6,95,640 | 5,71,960 | 21.6% | 6,30,990 | 10.2% |
| Auto/ Utility vehicles | 2,15,648 | 1,77,308 | 21.6% | 2,01,917 | 6.8% |
| Tractors | 97,390 | 97,233 | 0.2% | 94,649 | 2.9% |
| Cars | 1,39,128 | 1,25,831 | 10.6% | 1,32,508 | 5.0% |
| CV/CE | 76,520 | 80,074 | -4.4% | 75,719 | 1.1% |
| Used vehicles & Others | 1,66,954 | 91,514 | 82.4% | 1,26,198 | 32.3% |
| Asset Quality | | | | | |
| Gross NPAs | 46,608 | 72,525 | -35.7% | 50,668 | -8.0% |
| Net NPAs | 20,243 | 36,548 | -44.6% | 22,274 | -9.1% |
| Gross NPA (%) | 6.7% | 12.7% | -598 | 8.0% | -133 |
| Net NPA (%) | 2.9% | 6.4% | -3.5% | 3.5% | -0.6% |
| Coverage (%) | 58.2% | 53.0% | 5.2% | 58.1% | 0.1% |
| Credit costs - On Loans | 1.14% | -2.57% | 3.7% | 4.09% | -2.9% |
| Balance sheet Details | | | | | |
| Total Borrowed Funds | 6,76,530 | 5,60,160 | 20.8% | 5,93,090 | 14.1% |
| Loans & Advances & others | 6,95,640 | 5,71,960 | 21.6% | 6,30,990 | 10.2% |
| Insurance Brokers PAT | 60 | 100 | -40.0% | 20 | 200.0% |
| Rural Housing PAT | 310 | 470 | -34.0% | 20 | 1450.0% |

Source: Company, PL

Conference Call Highlights

- **Business Update:** Asset growth has come back and we are witnessing asset growth beginning to happen and it's not happening through just any single product or it's not happening through any single geography and therefore it's an outcome of the country across the product growth that we have seen. Barring taxi segment especially aggregators, company sees robust demand with increasing customer cashflows and positive macro indicators.

- **Pressure on margins:** Company has entered into financing certain affluent customers which are low-yield but bring stability into operation.

NIMs have fallen as growth is contributed by Car, Commercial Vehicles and SME segment as compared to tractor or pre-owned vehicle which are high yielding

Liquidity chest is maintained at 4 months which has resulted in drop in NIMs and is likely to continue till year end.

- **Subsidiaries:** Company has made one time provision of Rs. 55cr against its operations in Sri Lanka looking into the economic crisis and currency behaviour. However, the business is independently profitable and no further capital allocation is needed.

Also, company has bought out stake in MIBL from its partner AXA which will make MIBL 100% subsidiary of MMFS. Regulatory approval is pending.

- **Update on RBI Order:** Management has said that impact of RBI ban of repossession will be limited only to 2,000/3,000 vehicle per month. It has held healthy discussions with the regulator and is positive that the ban will lifted soon.

The company has launched a settlement scheme which whereby customers' whose vehicles were to repossessed will be allowed for a settlement of account. The company has also migrated about 6,000 employees on its roll under contract.

- **SME and Other Segment:** SME and other segment has grown mainly due to 3 products. 1) SME financing to auto engineering agri and suppliers of M&M. 2) Lending to smaller NBFCs in similar operations and 3) Trade advances to auto dealers for retail financing.

SME loans are all secured by either underlying capital of fixed assets

- **Asset Quality and Guidance:** Asset quality has improved due to robust collection of Stage 2 and Stage 3 assets.

GNPA gap between IRAC and Ind AS was about Rs. 9bn as on Oct end. However, there will be no impact in P&L as management has already booked enough provisions.

Company targets GNPA to in a range of around 5-6% and maintaining steady PCR of appx 58%.

- **Guidance:** Management sees that 2025 targets are achievable.



Exhibit 2: FY23/24 EPS estimates increased by 2.9%/4.2%, target price increased to Rs 230, maintain HOLD rating

| (Rs mn) | Old Estimates | | | Revised Estimates | | | % Change | | |
|---------------------|---------------|--------|--------|-------------------|--------|--------|----------|-------|-------|
| | FY22E | FY23E | FY24E | FY22E | FY23E | FY24E | FY22E | FY23E | FY24E |
| Net Interest Income | 58,781 | 65,724 | 75,430 | 58,781 | 65,724 | 75,430 | 0.0% | 0.0% | 0.0% |
| Operating Profit | 35,995 | 38,148 | 42,005 | 35,995 | 38,148 | 42,005 | 0.0% | 0.0% | 0.0% |
| Net Profit | 15,163 | 16,184 | 18,206 | 15,598 | 16,869 | 18,938 | 2.9% | 4.2% | 4.0% |
| EPS (Rs) | 12.3 | 13.1 | 14.8 | 12.7 | 13.7 | 15.4 | 2.9% | 4.2% | 4.0% |
| Price Target (Rs) | | 200 | | | 230 | | | 15.3% | |
| Reco | | HOLD | | | HOLD | | | | |

Source: PL



Income Statement (Rs. m)

| Y/e Mar | FY22 | FY23E | FY24E | FY25E |
|----------------------------|---------------|---------------|---------------|---------------|
| Int. Inc. / Opt. Inc. | 96,580 | 1,06,833 | 1,17,818 | 1,29,868 |
| Interest Expenses | 39,202 | 47,451 | 51,465 | 53,851 |
| Net interest income | 57,378 | 58,781 | 65,724 | 75,430 |
| Growth(%) | 1.3 | 2.4 | 11.8 | 14.8 |
| Non-interest income | 608 | 700 | 839 | 1,007 |
| Growth(%) | (50.0) | 15.0 | 20.0 | 20.0 |
| Net operating income | 57,986 | 59,480 | 66,564 | 76,437 |
| Expenditures | | | | |
| Employees | 11,714 | 13,471 | 16,165 | 19,398 |
| Other Expenses | 7,752 | 8,682 | 10,853 | 13,566 |
| Depreciation | 1,268 | 1,332 | 1,398 | 1,468 |
| Operating Expenses | 19,466 | 22,153 | 27,018 | 32,964 |
| PPP | 37,252 | 35,995 | 38,148 | 42,005 |
| Growth(%) | (10.3) | (3.4) | 6.0 | 10.1 |
| Provisions | 23,683 | 15,150 | 15,605 | 16,697 |
| Profit Before Tax | 13,569 | 20,845 | 22,543 | 25,308 |
| Tax | 3,682 | 5,247 | 5,674 | 6,370 |
| Effective Tax rate(%) | 27.1 | 25.2 | 25.2 | 25.2 |
| PAT | 9,888 | 15,598 | 16,869 | 18,938 |
| Growth(%) | 200.5 | 57.8 | 8.1 | 12.3 |

Balance Sheet (Rs. m)

| Y/e Mar | FY22 | FY23E | FY24E | FY25E |
|-----------------------------|-----------------|-----------------|------------------|------------------|
| Source of funds | | | | |
| Equity | 2,466 | 2,466 | 2,466 | 2,466 |
| Reserves and Surplus | 1,53,815 | 1,62,937 | 1,76,279 | 1,89,587 |
| Networth | 1,56,281 | 1,65,403 | 1,78,745 | 1,92,053 |
| Growth (%) | 6.2 | 5.8 | 8.1 | 7.4 |
| Loan funds | 5,58,139 | 6,13,486 | 6,73,140 | 8,69,387 |
| Growth (%) | (4.7) | 9.9 | 9.7 | 29.2 |
| Deferred Tax Liability | - | - | - | - |
| Other Current Liabilities | - | - | - | - |
| Other Liabilities | 38,467 | 89,435 | 1,49,876 | 1,54,868 |
| Total Liabilities | 7,52,887 | 8,68,324 | 10,01,761 | 12,16,308 |
| Application of funds | | | | |
| Net fixed assets | 3,929 | 3,780 | 4,044 | 4,044 |
| Advances | 6,04,537 | 6,52,802 | 7,18,082 | 7,89,891 |
| Growth (%) | 0.8 | 8.0 | 10.0 | 10.0 |
| Investments | 84,403 | 76,052 | 64,393 | 64,393 |
| Current Assets | 44,004 | 1,29,345 | 2,06,926 | 3,47,656 |
| Net current assets | 44,004 | 1,29,345 | 2,06,926 | 3,47,656 |
| Other Assets | 16,014 | 6,346 | 8,316 | 10,325 |
| Total Assets | 7,52,887 | 8,68,324 | 10,01,760 | 12,16,309 |
| Growth (%) | (2.3) | 15.3 | 15.4 | 21.4 |
| Business Mix | | | | |
| AUM | 6,04,446 | 6,52,802 | 7,18,082 | 7,89,891 |
| Growth (%) | 0.8 | 8.0 | 10.0 | 10.0 |
| On Balance Sheet | 6,00,648 | 6,48,013 | 7,13,888 | 7,89,891 |
| % of AUM | 99.37 | 99.27 | 99.42 | 100.00 |
| Off Balance Sheet | 3,798 | 4,789 | 4,195 | - |
| % of AUM | 0.63 | 0.73 | 0.58 | - |

Profitability & Capital (%)

| Y/e Mar | FY22 | FY23E | FY24E | FY25E |
|---------|------|-------|-------|-------|
| NIM | 8.5 | 7.7 | 7.8 | 7.9 |
| ROAA | 1.3 | 1.9 | 1.9 | 2.0 |
| ROAE | 6.5 | 9.7 | 9.8 | 10.2 |

Source: Company Data, PL Research

Quarterly Financials (Rs. m)

| Y/e Mar | Q3FY22 | Q4FY22 | Q1FY23 | Q2FY23 |
|----------------------------------|---------------|---------------|---------------|---------------|
| Int. Inc. / Operating Inc. | 25,317 | 24,424 | 24,863 | 25,858 |
| Income from securitization | - | - | - | - |
| Interest Expenses | 9,514 | 9,357 | 9,320 | 10,688 |
| Net Interest Income | 15,802 | 15,067 | 15,544 | 15,170 |
| Growth (%) | 14.2 | (0.3) | 34.2 | 1.6 |
| Non-Interest Income | 113 | 239 | 122 | 235 |
| Net Operating Income | 15,916 | 15,306 | 15,666 | 15,405 |
| Growth (%) | 12.4 | (1.2) | 34.0 | 2.2 |
| Operating expenditure | 5,294 | 6,327 | 6,208 | 6,768 |
| PPP | 10,622 | 8,979 | 9,458 | 8,637 |
| Growth (%) | - | - | - | - |
| Provision | (1,474) | 639 | 6,453 | 1,985 |
| Exchange Gain / (Loss) | - | - | - | - |
| Profit before tax | 12,096 | 8,341 | 3,005 | 6,652 |
| Tax | 3,158 | 2,333 | 776 | 1,624 |
| Prov. for deferred tax liability | - | - | - | - |
| Effective Tax Rate | 26.1 | 28.0 | 25.8 | 24.4 |
| PAT | 8,938 | 6,008 | 2,229 | 5,028 |
| Growth | (426) | 301 | (115) | (51) |
| AUM | 5,82,780 | 6,04,450 | 6,30,990 | 6,95,640 |
| YoY growth (%) | (6.2) | 0.8 | 11.9 | 21.6 |
| Borrowing | 5,70,630 | 5,58,139 | - | - |
| YoY growth (%) | (3.6) | (4.7) | - | - |

Key Ratios

| Y/e Mar | FY22 | FY23E | FY24E | FY25E |
|--------------------------|-------|-------|-------|-------|
| CMP (Rs) | 220 | 220 | 220 | 220 |
| EPS (Rs) | 8.0 | 12.7 | 13.7 | 15.4 |
| Book value (Rs) | 126.7 | 134.1 | 145.0 | 154.9 |
| Adj. BV(Rs) | 96.9 | 101.9 | 117.0 | 131.6 |
| P/E(x) | 27.4 | 17.4 | 16.1 | 14.3 |
| P/BV(x) | 1.7 | 1.6 | 1.5 | 1.4 |
| P/ABV(x) | 2.3 | 2.2 | 1.9 | 1.7 |
| DPS (Rs) | 0.3 | 0.8 | 1.2 | 1.3 |
| Dividend Payout Ratio(%) | 7.7 | 14.5 | 21.1 | 16.9 |
| Dividend Yield(%) | 0.1 | 0.3 | 0.5 | 0.6 |

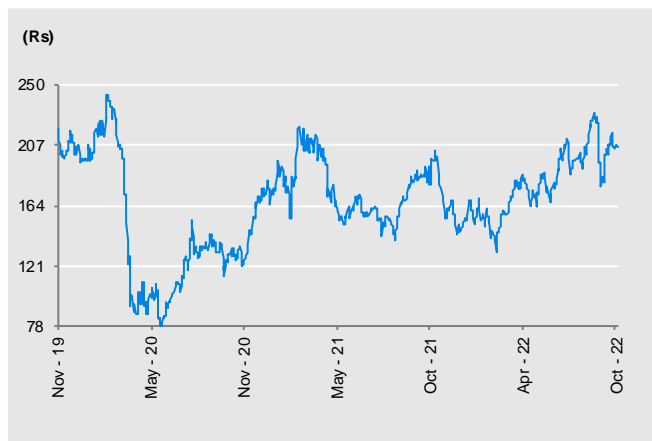
Asset Quality

| Y/e Mar | FY22 | FY23E | FY24E | FY25E |
|-----------------------------|--------|--------|--------|--------|
| Gross NPAs(Rs m) | 96,831 | 86,484 | 75,095 | 64,866 |
| Net NPA(Rs m) | 36,796 | 39,783 | 34,544 | 29,838 |
| Gross NPAs to Gross Adv.(%) | 7.7 | 6.7 | 6.2 | - |
| Net NPAs to net Adv.(%) | 3.5 | 3.4 | 3.1 | 3.1 |
| NPA coverage(%) | 62.0 | 54.0 | 54.0 | 54.0 |

Du-Pont as a % of AUM

| Y/e Mar | FY22 | FY23E | FY24E | FY25E |
|----------------------------|------|-------|-------|-------|
| NII | 9.5 | 9.4 | 9.6 | 10.0 |
| NII INCL. Securitization | 9.5 | 9.4 | 9.7 | 10.0 |
| Total income | 9.6 | 9.6 | 9.8 | 10.1 |
| Operating Expenses | 3.4 | 3.7 | 4.1 | 4.6 |
| PPOP | 6.2 | 5.8 | 5.7 | 5.6 |
| Total Provisions | 3.9 | 2.4 | 2.3 | 2.2 |
| RoAA | 1.3 | 1.9 | 1.9 | 2.0 |
| Avg. Assets/Avg. net worth | 5.0 | 5.0 | 5.3 | 5.2 |
| RoAE | 6.5 | 9.7 | 9.8 | 10.2 |

Source: Company Data, PL Research

Price Chart
Recommendation History


| No. | Date | Rating | TP (Rs.) | Share Price (Rs.) |
|-----|-----------|--------|----------|-------------------|
| 1 | 06-Oct-22 | Hold | 200 | 201 |
| 2 | 29-Jul-22 | Hold | 200 | 187 |
| 3 | 07-Jul-22 | Hold | 200 | 189 |
| 4 | 04-May-22 | Hold | 200 | 182 |
| 5 | 12-Apr-22 | UR | - | 176 |
| 6 | 11-Jan-22 | Reduce | 146 | 155 |

Analyst Coverage Universe

| Sr. No. | Company Name | Rating | TP (Rs) | Share Price (Rs) |
|---------|----------------------------------------------|------------|---------|------------------|
| 1 | Bajaj Finance | BUY | 8,953 | 7,432 |
| 2 | Cholamandalam Investment and Finance Company | BUY | 792 | 736 |
| 3 | L&T Finance Holdings | BUY | 88 | 80 |
| 4 | Mahindra & Mahindra Financial Services | Hold | 200 | 201 |
| 5 | Manappuram Finance | BUY | 126 | 99 |
| 6 | Muthoot Finance | BUY | 1,431 | 1,042 |
| 7 | SBI Cards and Payment Services | Accumulate | 1,013 | 858 |
| 8 | Shriram Transport Finance | BUY | 1,521 | 1,198 |

PL's Recommendation Nomenclature (Absolute Performance)

| | |
|--------------------------|-----------------------------------|
| Buy | : > 15% |
| Accumulate | : 5% to 15% |
| Hold | : +5% to -5% |
| Reduce | : -5% to -15% |
| Sell | : < -15% |
| Not Rated (NR) | : No specific call on the stock |
| Under Review (UR) | : Rating likely to change shortly |



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