Penguin International Ltd

This Penguin can flex and fly

SINGAPORE | OIL & GAS | INITIATION

- Expanded shipbuilding capabilities beyond crew and security boats into passenger ferries, fire and rescue vessels, patrol boats and windfarm support vessels
- Rising recurrent charter income from crewboats amidst rising utilisation and charter rates. Offshore oil and gas activity is recovering and more customers opt for more cost-effective and safer crewboats.
- Valuations attractive at 3x PE (ex-cash). Initiate coverage with a BUY and TP of S$0.61.

Company Background

In 1995, Penguin International Ltd (Penguin) built its first aluminium boat. Listed on the SGX in 1997, it has since built more than 200 high-speed aluminium vessels, including 120 of its trademark Flex crewboats/security boats. The boats are sold under the Flex brand. Penguin has two shipyards, Tuas (Singapore) and Batam (Indonesia). A major milestone was reached when it sold its regional passenger ferrying ticketing business in 2011 to Sindo Ferry. This was a loss-making business which was highly exposed to fuel price volatility and intense competition.

Almost 80% of Penguin's revenue now comes from shipbuilding and ship repair. The remaining 20% of revenue is from charter income. Penguin owns 15 crewboats for charter income and several passenger ferries, harbour launches and a landing craft for special projects in Singapore. The common feature of all Penguin boats is the aluminium material and the speed. Such boats can travel as fast as 30 knots as compared to 10-12 knots by a steel vessel of similar specifications. Penguin's business model revolves around constructing vessels for their stock programme (i.e. built without an order). In addition, Penguin will opportunistically dispose crewboats on charter after converting them into security vessels when the prices are attractive.

Investment Merits

1. **Expanded capabilities and opportunities.** Penguin has honed expertise in crewboat and security vessels. In December 2016, it was awarded a contract by the Singapore Ministry of Home Affairs to build and maintain Marine Fire and Rescue Vessels. It also secured new orders for patrol boats and windfarm support vessels in 2018.
2. **Rising charter income.** Following the deep lull in 2016, demand for crewboats is on track for a recovery. Firstly, oil and gas companies are switching from costly helicopter transportation to more economical and safer crewboats. Secondly, a rebound in oil prices has resurrected global offshore rig activity, including in Malaysia – Penguin's key market.
3. **Healthy balance sheet and attractive valuations** Penguin has maintained a conservative net-cash balance sheet for the past 12 years and management has been prudent in cash deployment. We find the current valuations attractive at 3x PE FY19e (excluding cash).

Outlook

We are positive on its outlook. The strong balance sheet has helped Penguin weather the offshore and marine downcycle of 2015-17. Several competitors have either exited the business or fallen under debt restructuring. The current upturn in oil prices and offshore rig activity is another positive for the company. We also see Penguin diversifying outside its primary oil and gas vessels into other categories, including government and offshore windfarm vessels.

Initiating coverage with BUY rating and target price of S$0.61

We initiate Penguin with a BUY and a target price of S$0.61. We value Penguin at 5x PE, excluding its S$41mn net cash. Shipyards of similar size traded at 5x PE on average back when the industry was in at steady state.

25 April 2019

BUY (Initiation)

LAST CLOSE PRICE	SGD 0.435
FORECAST DIV	SGD 0.0125
TARGET PRICE	SGD 0.610
TOTAL RETURN	**43.1%**

COMPANY DATA

BLOOMBERG CODE	PBS SP
O/S SHARES (MN) :	220.2
MARKET CAP (USD mn / SGD mn) :	74 / 101
52 - WK HI/LO (SGD) :	0.46 / 0.26
3M Average Daily T/O (mn) :	0.38

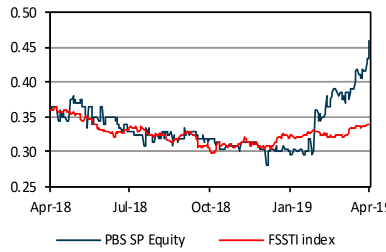
MAJOR SHAREHOLDERS (%)

Hing Yih Pier	19.7%
Keppel Corp Ltd	6.2%

PRICE PERFORMANCE (%)

	1MTH	3MTH	1YR
COMPANY	13.0	45.0	20.7
STI RETURN	4.8	6.0	(2.6)

PRICE VS. STI



Source: Bloomberg, PSR

KEY FINANCIALS

Y/E Dec	FY17	FY18	FY19e	FY20e
Revenue (SGD mn)	79.8	107.3	122.4	134.4
EBITDA (SGD mn)	(2.8)	7.8	18.3	31.8
NPAT (SGD mn)	2.3	13.6	17.2	28.6
EPS (Cents)	1.0	6.2	7.8	13.0
PER (x)	42.1	7.1	5.6	3.3
P/BV (x)	0.7	0.6	0.6	0.5
Div Yield (%)	1.0%	2.9%	2.9%	2.9%
ROE (%)	10.8%	15.9%	1.7%	5.3%

Source: Company, PSR

VALUATION METHOD

5x PE FY19x (excluding net cash)

Paul Chew (+65 6212 1851)
paulchewkl@phillip.com.sg

MCI (P) 062/10/2018
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Revenue

Shipbuilding (77% of FY18 revenue): Penguin builds crewboats, security vessels, ferries and patrol boats. In recent years, it has ventured into constructing patrol boats and fire and rescue vessels. Vessels can either be built-to-order or built-to-stock. For the former, revenue is recognised on a percentage of completion method. Penguin does not disclose its order books. Built-to-stock ships are parked as inventory before disposal. The average selling price of a security boat is around US$5mn. In 2018, 59% or S$48mn of revenue was from the sale of stocked Flex crewboats/security boats. The balance S$33mn were newbuild orders.

Ferry and charter income (23% of FY18 revenue): Charter income from 30 vessels: 15 are crewboats and the rest specialised vessels utilised in Singapore for ferry support, landing craft and harbour motor launch. Its crew boats are deployed in Malaysia, mainly by the oil and gas industry to transport crews from shore to rigs or between rigs. Spot rental is US$4,000-5,000 per day. Most are rented for 180 days with a few under-3-year charters that come with lower rates. We expect the company to expand their fleet as demand is improving. Penguin also sells its crewboats as security vessels when prices are attractive. Gains are recognised as other income. In 2018, Penguin sold 3 Flex crewboats, which were converted into security vessels.

Types of boats built by Penguin:

1. Offshore Crewboat (Flex brand): *Used in offshore oil and gas activities to ferry crew from onshore to offshore rigs or platforms. Alternatively, it is used to transports crew between rigs. Crewboats are branded under the Flex series (e.g. Flex-36, Flex-40 series), with the latest vessel being a Flex-42X (Figure 1). This vessel is installed with CCTVs and electronic fuel management. Crewboats require 6 to 7 months to build.*

2. Armoured Security boats (Flex Fighter, Figure 2): *These are aluminium armoured vessels sold to oil companies for patrolling their offshore oil facilities in Nigeria. Its boats escort tankers and patrol offshore platforms. Demand for Flex Fighter boats is around a dozen a year.*

3. Passenger Ferries (Figure 3): *These are aluminium boats to ferry passengers in the leisure industry, which take 8 to 9 months to build. Customers typically want these ferries to be fast-speed and fuel-efficient, as well as to be able to accommodate as many passengers as possible. Penguin has sold one unit of Flex Ferry to an African customer. This ferry is a large monohull passenger ferry with high-speed craft safety code. The older ferry model called Queen Star had been sold to customers such as Sindo Ferry, Shipping Corporation of India and Horizon Fast Ferry.*

4. Patrol boats: *Penguin has sold seven patrol boats to an Australian customer. These are for law enforcement and search and rescue purposes. Speed and crew comfort are two major criteria for patrol boats.*

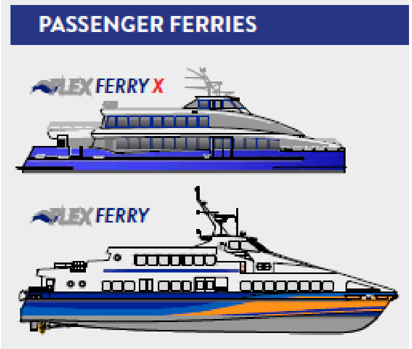
5. Wind farm support vessel: *Secured a contract in 2018 for two vessels used for transferring crew from shore to offshore windfarm sites in Taiwan.*

6. Fire and rescue vessel (Figure 4): *In December 2016, the Singapore Ministry of Home Affairs awarded a US$23mn contract to a consortium comprising Penguin and ST Marine for a design, construction and system maintenance programme involving a heavy marine fire vessel, a heavy marine rescue vessel and a marine rescue vessel.*

Figure 1: Latest crewboat Flex-42X

Figure 2: Flex Fighter security boat

Figure 3: Passenger Ferries



Source: Company, PSR

Figure 4: Fire fighting and rescue vessel

Source: Company, PSR

The common feature of all these boats is the aluminium design and speed. We believe the capacity of the yard is 30 to 40 vessels per year. It requires 7 to 8 months to build a crewboat. Challenges in building aluminium vessels are the hull form design, weight management, space planning and selection of equipment, machinery and material.

Cost

Charter costs include the costs of crew on board (around eight per vessel) and vessel maintenance. Fuel costs are borne by customers. The largest cost component of crewboats is the engine. For instance, three Caterpillar C32 ACERT engines are required in one crew boat.

Figure 5: Tuas yard

Source: Company, PSR

Cash-flow

Recurrent cash flow is derived from its chartering business. In shipbuilding, customers place 10-30% deposits upfront when they place orders. Built-to-stock vessels, once completed, are recognised as inventory. They are recognised as sales upon delivery and full payment. Penguin will build vessels for stock only with cash in hand and when they are not geared up.

Figure 6: Yard in Batam, Indonesia

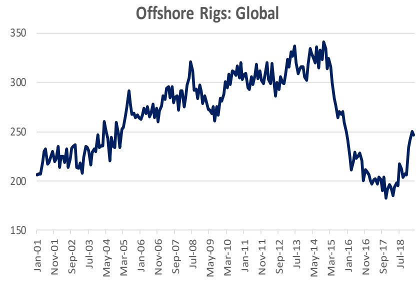
Source: Company, PSR

Balance Sheet

Asset composition: plant and equipment 40% (buildings, motor launches, machinery), cash 20%, inventory 10%, trade receivables 10% and contract assets 7%. Contract assets are vessel-building costs yet to be recognised as revenue. There is also an original S$8mn invested in SGX-listed Marco Polo Marine. Its value had been written down to S$5.1mn as at end-December 2018.

Liabilities composition: 44% are other payables and accruals (bulk are accrued operating expenses and deposits received) and 33% is trade payables.

Figure 7: Sharp rebound in global offshore rigs



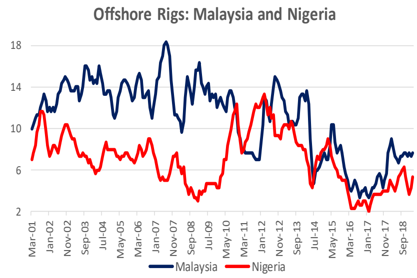
Source: CEIC, Baker Hughes, PSR

Industry

Since 2008, the top five largest aluminium crew boat manufacturers in the world are Penguin, Grandweld (Dubai), Strategic Marine, Marsun and NGV Tech. Of the top 10, around one-third are being liquidated or under some form of restructuring. These include Strategic Marine (owned by Triyards), NGV Tech and Nautic Africa. Meanwhile, competitors in ferry construction are Cochin Shipyard, Damen Shipyards (Netherlands), Grandweld and L&T.

In 2014-18, around 192 aluminium (30m to 50m-length) crewboats and crew/supply vessels were built globally. Around 68 were from Penguin's yards. In 2014, there were 78 of such boats built. This dwindled to only 9 and 16 units in 2017 and 2018, respectively. Penguin's share of all such vessels built in 2017/18 was 60%, the single largest market share.

Figure 8: Penguin's key markets seeing improvements in offshore rigs



Source: CEIC, Baker Hughes, PSR

Outlook

We are positive on Penguin's outlook.

Firstly, improving oil prices have fuelled a revival in offshore activity. The number of offshore rigs globally has recovered from their low at end-2017 (Figure 7). The recovery is visible in countries where Penguin has a large presence, namely, Nigeria and Malaysia (Figure 8).

Secondly, the net cash balance sheet has allowed Penguin to weather the 2015-17 vicious oil and gas downturn. Several major competitors have left or downsized their activities. Over the past two years, Penguin has captured a large share of the crewboat and security boat market.

Thirdly, Penguin is securing more orders outside its crewboat and security boat business. It has successfully diversified outside this core business to secure new orders from patrol boats, offshore vessels and rescue and fire safety vessels.

Build-for-stock is not applicable for every type of vessel. It carries the risk of inventory overhang. For this model to work, the vessel must have a robust and ongoing demand. The advantage for such models are the higher margins and ability for customers to secure their vessels faster and in turn, expedite their own charter income.

Investment Merits

1. **Expanded capabilities and opportunities.** Penguin has honed its expertise in crewboat and security vessels. In December 2016, it was awarded a contract by the Singapore Ministry of Home Affair to build and maintain Marine Fire and Rescue Vessel. It also also secured new orders for patrol boats and windfarm support vessels in 2018.

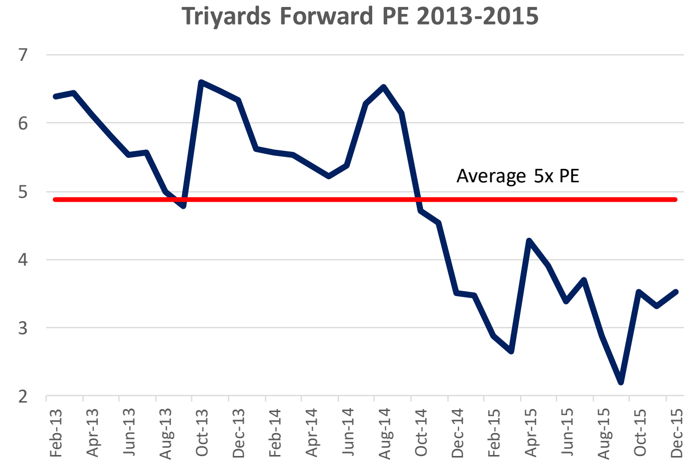
2. **Rising charter income.** Following the deep lull in 2016, demand for crewboats is on track for a recovery. Firstly, oil and gas companies are switching from costly helicopter transportation to more economical and safer crewboats. Secondly, a rebound in oil prices has resurrected global offshore rig activity, including in Malaysia – Penguin's key market. In June 2017, Petronas Carigali terminated their charter contract for five Eurocopter EC225 Super Puma helicopters with MHS Aviation.

3. **Healthy balance sheet and attractive valuations** Penguin has maintained a conservative net-cash balance sheet for the past 12 years. We find the current valuations attractive at 3x PE FY19e (excluding cash).

Valuation

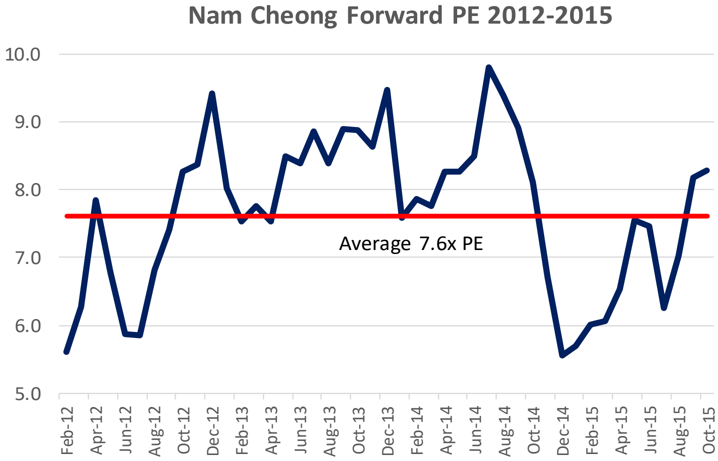
We initiate coverage on Penguin with a BUY rating. As there are very few direct comparables, we use the PE ratios of two Singapore yards when the shipbuilding cycle was in a steady state cycle. During the normalised shipbuilding cycle of 2012-15, both Triyards (Figure 9) and Nam Cheong (Figure 10) traded at an average 5-8x PE. Although, they build different vessels and have more geared balance sheet profiles, both can be considered proxies for Penguin as their yard sizes are similar. We used the lower PE average of 5x to value the business and added back the net cash from FY19e.

Figure 9: Triyards average valuation was 5x PE



Source: Bloomberg, PSR

Figure 10: Nam Cheong valuations averaged 7.6x PE



Source: Bloomberg, PSR

Financials

Income Statement

Y/E Dec, SGD '000	FY16	FY17	FY18	FY19e	FY20e
Revenue	33,405	79,761	107,268	122,449	134,425
Gross profits	**14,727**	**19,457**	**33,707**	**43,482**	**56,961**
Operating expenses	-25,203	-22,226	-25,871	-25,200	-25,200
EBITDA	**-10,476**	**-2,769**	**7,836**	**18,282**	**31,761**
Depreciation & Amortisation	-8,682	-8,933	-8,888	-9,406	-9,965
EBIT	**-1,794**	**6,164**	**16,724**	**27,688**	**41,727**
Other income/(loss)	3,248	4,304	6,711	1,000	1,000
Net finance income/(expense)	-249	563	950	900	900
Profit/(loss) before tax	**-7,477**	**2,098**	**15,497**	**20,182**	**33,661**
Income tax credit/(expense)	1,046	180	-1,915	-3,027	-5,049
Profit/(loss) after tax	**-6,431**	**2,278**	**13,582**	**17,155**	**28,612**
Minority interest	0	-1	-1	0	0
Net Income, reported	**-6,431**	**2,277**	**13,581**	**17,155**	**28,612**

Per share data

Y/E Dec, SG cents	FY16	FY17	FY18	FY19e	FY20e
EPS, reported	(2.9)	1.0	6.2	7.8	13.0
EPS, adj.	(2.9)	1.0	6.2	7.8	13.0
DPS	0.0	0.45	1.25	1.25	1.25
BVPS	68.2	64.0	69.1	75.7	87.4

Cash Flows

Y/E Dec, SGD '000	FY16	FY17	FY18	FY19e	FY20e
CFO					
PBT	**-7,477**	**2,098**	**15,497**	**20,182**	**33,661**
Adjustments	14,293	4,891	2,532	8,506	9,065
WC changes	(14,266)	10,567	(5,657)	221	(4,068)
Taxes paid, others	(5,883)	576	1,052	(2,127)	(4,149)
Net cash flows used in ops	**(13,333)**	**18,132**	**13,424**	**26,781**	**34,510**
CFI					
CAPEX, net	(5,738)	(2,988)	(19,222)	(15,000)	(15,000)
Proceeds from disposal	5,312	12,778	20,052	-	-
Others	-	-	(8,000)	-	-
Net cash flows from/(used in) investing	**(426)**	**9,790**	**(7,170)**	**(15,000)**	**(15,000)**
CFF					
Proceeds from issuance of shares	-	-	-	-	-
Loans, net of repayments	(3,360)	(6,647)	(2,250)	-	-
Dividends	(1,651)	-	(991)	(2,752)	(2,752)
Others	-	(836)	(472)	-	-
Net cash flow generated from financing	**(5,011)**	**(7,483)**	**(3,713)**	**(2,752)**	**(2,752)**
Net change in cash and cash equivalents	**(18,770)**	**20,439**	**2,541**	**9,029**	**16,758**
Foreign exchange	148	(873)	512	-	-
CCE, end	**18,675**	**38,241**	**41,294**	**50,323**	**67,081**

Source: Company, Phillip Securities Research (Singapore) Estimates

Balance Sheet

Y/E Dec, SGD '000	FY16	FY17	FY18	FY19e	FY20e
ASSETS					
Intangible asset	78	78	78	78	78
PPE	104,405	74,100	86,559	92,153	97,188
Other investments	-	-	5,157	5,157	5,157
Trade receivables	1,876	1,542	-	-	-
Other receivables	2,708	9,348	8,471	8,471	8,471
Non-current assets	**109,067**	**85,068**	**100,265**	**105,859**	**110,894**
Cash and bank balances	18,675	39,077	42,619	51,648	68,406
Trade receivables	8,058	10,352	20,200	11,179	22,188
Inventory	40,187	18,906	20,608	22,662	19,784
Others	10,819	23,723	8,078	8,078	8,078
Current assets	**77,739**	**93,070**	**106,480**	**108,542**	**133,431**
Total assets	**186,806**	**178,138**	**206,745**	**214,401**	**244,325**
LIABILITIES					
Borrowings	3,360	2,250	1,000	1,000	1,000
Trade payables	8,523	8,422	18,085	11,338	15,402
Other payables	17,147	11,630	23,790	23,790	23,790
Others	1,246	9,698	7,695	7,695	7,695
Current liabilities	**30,276**	**32,026**	**50,570**	**43,823**	**47,887**
Borrowings	6,620	1,083	83	83	83
Others	3,871	4,164	3,877	3,877	3,877
Non-current liabilities	**10,491**	**5,247**	**3,960**	**3,960**	**3,960**
EQUITY					
Share capital	94,943	94,943	94,943	94,943	94,943
Reserves	55,174	45,923	57,274	71,677	97,537
Minority interest	(4,078)	(1)	(2)	(2)	(2)
Total equity	**146,039**	**140,865**	**152,215**	**166,618**	**192,478**

Valuation Ratios

Y/E Dec	FY16	FY17	FY18	FY19e	FY20e
P/E (X)	n.m.	42.1	7.1	5.6	3.3
P/B (X)	0.6	0.7	0.6	0.6	0.5
EV/EBITDA (X)	0.8	12.8	-5.3	-2.8	0.0
Dividend Yield (%)	0.0%	1.0%	2.9%	2.9%	2.9%

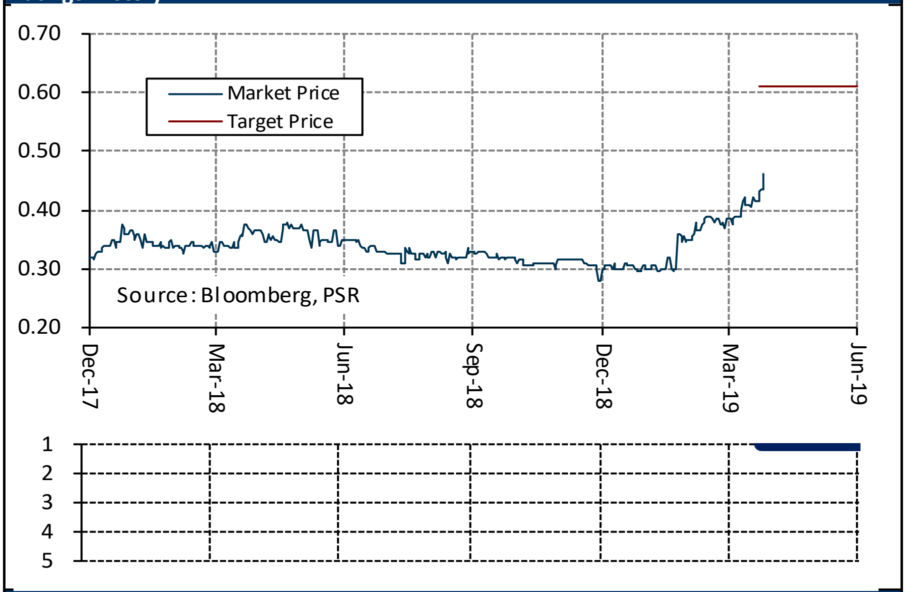
Growth & Margins

Growth					
Revenue	-72.1%	138.8%	34.5%	14.2%	9.8%
EBITDA	-201.5%	-73.6%	-383.0%	133.3%	73.7%
EBIT	-108.5%	-443.6%	171.3%	65.6%	50.7%
Net Income	-130.3%	-135.4%	496.4%	26.3%	66.8%
Margins					
EBITDA margin	-31.4%	-3.5%	7.3%	14.9%	23.6%
EBIT margin	-5.4%	7.7%	15.6%	22.6%	31.0%
Net Profit Margin	-19.3%	2.9%	12.7%	14.0%	21.3%

Key Ratios

ROE	-4.3%	1.6%	9.3%	10.8%	15.9%
ROA	-3.3%	1.2%	7.1%	8.1%	12.5%
Interest coverage (X)	(0.2)	0.7	1.9	2.9	4.2
Net gearing (X)	Net cash	Net cash	Net cash	Net cash	Net cash

Ratings History



PSR Rating System

Total Returns	Recommendation	Rating
> +20%	Buy	1
+5% to +20%	Accumulate	2
-5% to +5%	Neutral	3
-5% to -20%	Reduce	4
<-20%	Sell	5

Remarks

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

Contact Information (Singapore Research Team)

Head of Research
Paul Chew – paulchewkl@phillip.com.sg

Siti Syazwina
syazwina@phillip.com.sg

Banking & Finance | Healthcare
Tin Min Ying – tinmy@phillip.com.sg

Oil & Gas | Energy
Chen Guangzhi - chengz@phillip.com.sg

Telco | Technology
Alvin Chia - alvinchiawy@phillip.com.sg

Property | REITs
Tara Wong - tarawongsj@phillip.com.sg

REITs
Natalie Ong - natalieongpf@phillip.com.sg

China/HK Equity
Zheng Jieyuan – zhengjy@phillip.com.sg

US Equity
Edmund Xue – edmundxuejj@phillip.com.sg

Contact Information (Regional Member Companies)

SINGAPORE
Phillip Securities Pte Ltd
Raffles City Tower
250, North Bridge Road #06-00
Singapore 179101
Tel +65 6533 6001
Fax +65 6535 6631
Website: www.poems.com.sg

MALAYSIA
Phillip Capital Management Sdn Bhd
B-3-6 Block B Level 3 Megan Avenue II,
No. 12, Jalan Yap Kwan Seng, 50450
Kuala Lumpur
Tel +603 2162 8841
Fax +603 2166 5099
Website: www.poems.com.my

HONG KONG
Phillip Securities (HK) Ltd
11/F United Centre 95 Queensway
Hong Kong
Tel +852 2277 6600
Fax +852 2868 5307
Websites: www.phillip.com.hk

JAPAN
Phillip Securities Japan, Ltd.
4-2 Nihonbashi Kabuto-cho Chuo-ku,
Tokyo 103-0026
Tel +81-3 3666 2101
Fax +81-3 3666 6090
Website: www.phillip.co.jp

INDONESIA
PT Phillip Securities Indonesia
ANZ Tower Level 23B,
Jl Jend Sudirman Kav 33A
Jakarta 10220 – Indonesia
Tel +62-21 5790 0800
Fax +62-21 5790 0809
Website: www.phillip.co.id

CHINA
Phillip Financial Advisory (Shanghai) Co Ltd
No 550 Yan An East Road,
Ocean Tower Unit 2318,
Postal code 200001
Tel +86-21 5169 9200
Fax +86-21 6351 2940
Website: www.phillip.com.cn

THAILAND
Phillip Securities (Thailand) Public Co. Ltd
15th Floor, Vorawat Building,
849 Silom Road, Silom, Bangrak,
Bangkok 10500 Thailand
Tel +66-2 6351700 / 22680999
Fax +66-2 22680921
Website www.phillip.co.th

FRANCE
King & Shaxson Capital Limited
3rd Floor, 35 Rue de la Bienfaisance 75008
Paris France
Tel +33-1 45633100
Fax +33-1 45636017
Website: www.kingandshaxson.com

UNITED KINGDOM
King & Shaxson Capital Limited
6th Floor, Candlewick House,
120 Cannon Street,
London, EC4N 6AS
Tel +44-20 7426 5950
Fax +44-20 7626 1757
Website: www.kingandshaxson.com

UNITED STATES
Phillip Capital Inc
141 W Jackson Blvd Ste 3050
The Chicago Board of Trade Building
Chicago, IL 60604 USA
Tel +1-312 356 9000
Fax +1-312 356 9005
Website: www.phillipusa.com

AUSTRALIA
Phillip Capital Limited
Level 10, 330 Collins Street
Melbourne, Victoria 3000, Australia
Tel +61-03 8633 9803
Fax +61-03 8633 9899
Website: www.phillipcapital.com.au

SRI LANKA
Asha Phillip Securities Limited
No. 60, 5th Lane,
Colombo 3, Sri Lanka
Tel: (94) 11 2429 100
Fax: (94) 11 2429 199
Website: www.ashaphillip.net

INDIA
PhillipCapital (India) Private Limited
No.1, 18th Floor, Urmi Estate
95, Ganpatrao Kadam Marg
Lower Parel West, Mumbai 400-013
Maharashtra, India
Tel: +91-22-2300 2999 / Fax: +91-22-2300 2969
Website: www.phillipcapital.in

TURKEY
PhillipCapital Menkul Degerler
Dr. Cemil Bengü Cad. Hak Is Merkezi
No. 2 Kat. 6A Caglayan
34403 Istanbul, Turkey
Tel: 0212 296 84 84
Fax: 0212 233 69 29
Website: www.phillipcapital.com.tr

DUBAI
Phillip Futures DMCC
Member of the Dubai Gold and
Commodities Exchange (DGCX)
Unit No 601, Plot No 58, White Crown Bldg,
Sheikh Zayed Road, P.O.Box 212291
Dubai-UAE
Tel: +971-4-3325052 / Fax: + 971-4-3328895

CAMBODIA
Phillip Bank Plc
Ground Floor of B-Office Centre,#61-64,
Norodom Blvd Corner Street 306,Sangkat
Boeung Keng Kang 1, Khan Chamkamorn,
Phnom Penh, Cambodia
Tel: 855 (0) 7796 6151/855 (0) 1620 0769
Website: www.phillipbank.com.kh

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