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September 2002

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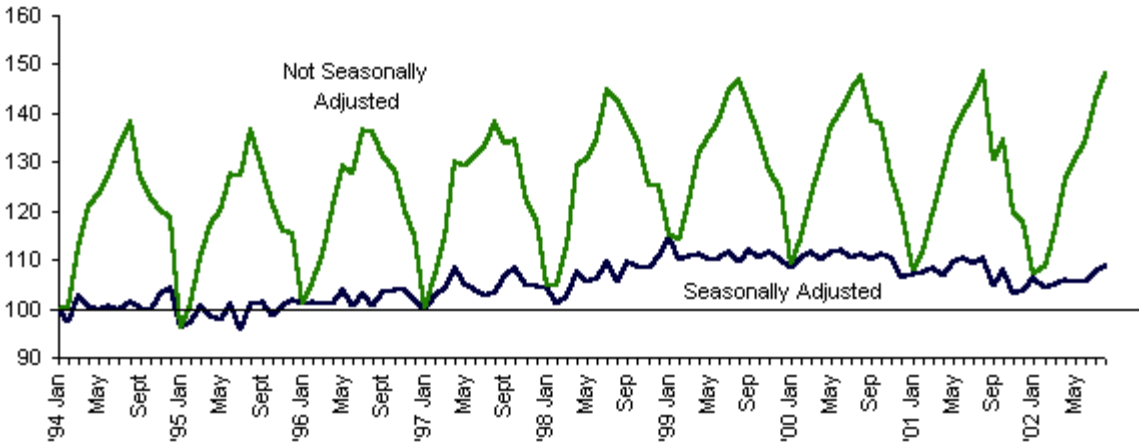
Composite Index



Key Statistics		Leading Indicators	
Humboldt County		***Seasonally Adjusted***	**% Change From Previous Month**
Median Home Price*	$169,900	Help Wanted Advertising	-7.4
30 Yr. Mortgage Rate (9/27)	6.375%	Building Permits	-32.6

Average Hotel Occupancy Rate	82.6%	Unemployment Claims	-6.0
Unemployment Rate**	5.3%	Manufacturing Orders	+5.9

* Home price data are provided by the Humboldt Association of Realtors. MLS is not responsible for accuracy of information. The information published and disseminated by the Service is communicated verbatim, without change by the Service, as filed with the Service by the Participant. The Service does not verify such information provided and disclaims any responsibility for its accuracy. Each Participant agrees to hold the Service harmless against any liability arising from any inaccuracy or inadequacy of the information.

** Preliminary EDD data. See the EDD Website for updates.

Sectoral Performance, *Index of Economic Activity for Humboldt County*							
* * *		**Percent Change From:**					
Sector	**Seasonally Adjusted Sectoral Index Value (1994=100)**	**Previous Month**	**Same Month 2001**	**Same Month 2000**	**Same Month 1999**	**Same Month 1998**	**Same Month 1997**
Home Sales	159.5	+20.8	+16.3	+14.0	+46.2	+78.1	+101.2
Retail Sales	136.6	+1.7	+1.8	+12.7	+9.7	+14.5	+17.5
Hospitality	96.4	-1.3	-0.3	+6.5	-1.5	-3.4	+2.9
Electricity Consumption	108.7	+4.6	-14.3	-14.8	-13.0	--	--
Total County Employment	102.9	-0.7	+0.2	-2.7	-1.9	-1.0	+0.5
Lumber Manufacturing	80.5	-9.4	-10.0	-25.4	-24.0	-30.8	-33.3

Discussion

Composite Index and Overall Performance

The *Index of Economic Activity*'s seasonally adjusted composite value, which now stands at 109.0, rose by a respectable 1.3 percent from last month's downwardly revised figure.

A look at the graph above shows that the Humboldt County economy continued to exhibit signs of increased activity in August for a second consecutive month. The gain was led by a spectacular increase in the home sales sector and the ongoing strength of the retail sales sector. One can also see that virtually all of the ground lost over the past year has been regained. The question remains, however, whether this level of performance can be sustained given the lingering weakness of the national economy. Other factors adding to the uncertainty include war with Iraq and an ongoing contract dispute between West Coast shippers and dockworkers that has begun to heat up.

Apart from home sales and retail sales, electricity consumption was the only other sector to show positive growth in August. The latter's *Index* value is based on estimates though, so actually performance won't be known until next month's report. The hospitality sector declined a bit from the previous month's level, but business has been brisk at most of the participating establishments, as one would expect for this time of year. The preliminary report from the Employment Development Department shows that Humboldt County gained around 300 jobs during August, but seasonal adjustment resulted in a decrease in the employment sector's *Index* level. Finally, the lumber manufacturing sector fell to its second lowest level ever. About the only thing positive to report here is that the depth of the current level is due to a technical adjustment in how this series is derived. As a result of the revision, the entire history of the sector's performance dropped slightly. So, if the

current number is compared with those appearing in past reports, the decline is marginally less bleak than would otherwise be the case.

The Leading Indicators are mixed once again. August building permits saw most of the huge gain in July evaporate. The most recent performance doesn't cause too alarm because permit activity lately has been on what appears to be a two-month cycle, with one month being very busy and the next not nearly so. Also, the seasonally adjusted four-month moving average of this indicator is trending in a positive direction. A fairly large drop in help-wanted advertising for the second straight month is more worrisome since the trend here is negative. The August number is also down by double-digit percentages when compared with same month performance in each of the last three years. On the positive side, manufacturing orders are up by a healthy amount with a trend suggesting very modest growth. And unemployment claims were down in August. This is the most volatile of our four leading indicators and the four-month moving average does not suggest any trend.

Home Sales

The *Index* value of this sector is based on the number of homes sold in Humboldt County each month as recorded by the Humboldt Association of Realtors.

The local real estate market sizzled in August as buyers scrambled to take advantage of interest rates that are near historic lows. The seasonally adjusted *Index* value for this sector jumped by over 20 percent in August from the previous month, reaching an all-time high. The average number of days a home for sale remained on the market dropped dramatically from 68 in July to 47 in August.

August's median home price fell 2.9 percent from July's $175,000. This sometimes volatile measure is over 18 percent higher than it was in August 2001. The current statewide median sale price of $334,100 for existing homes rose 3.2 percent from July's upwardly revised number. This figure is up 16.3 percent from August 2001, when it was $282,420 (www.car.org). August's national median price for existing homes rose 0.5 percent from July's level to $163,600, while the similar figure for new homes increased 2.8 percent to $175,300. These two measures are up by 6.4 percent and down by 0.9 percent, respectively over August 2001(www.realtor.org and www.census.gov).

The nationwide average for a 30-year fixed rate mortgage dropped to 5.99 percent in late September according to the country's largest mortgage company, Freddie Mac. This is the lowest level since the firm began tracking rates in 1971 (www.nytimes.com).

Retail Sales

The local retail sector experience registered a second consecutive month of improvement in August. The current level of the *Index* value is also up in all of the year-over-year comparisons.

National retail sales rose 0.8 percent in August from the previous month's downwardly revised level. Automobile sales alone accounted for half of the increase. Sales at health and personal care stores were also up substantially once again. Overall retail sales were 5.2 percent higher that in August 2001 (www.census.gov).

The September release of the Conference Board's Consumer Confidence Index fell another 1.3 percent to 93.3 from August's revised 94.5. This is the fourth straight monthly decline and the Index's lowest level since last November. Given that spending on big-ticket items has been largely responsible for buoying the economy over the last year and that interest rates remain low, this month's findings are troublesome to say the least. The proportion of consumers planning to purchase a home fell to 3.3 percent, a ten-month low. The similar measure of those planning to buy a car dropped by an even steeper amount to 2.7 percent. This is a six-month low (www.nytimes.com).

Hospitality

We use average occupancy at a cross section of local hotels, motels and inns as our indicator of economic activity in the hospitality sector. While the performance of this sector is, in turn, a good indicator of performance in the local tourism industry, it's important to note that not all visitors to Humboldt County are tourists, nor do all tourists stay in lodging establishments.

Average occupancy at the participating hotels, motels and inns increased from the previous month's level once again in August, but when the effect of seasonality is accounted for, month-to month performance in this sector actually declined slightly.

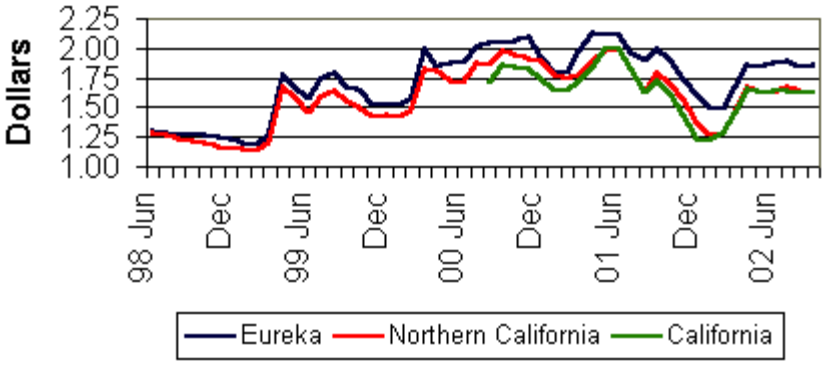
Humboldt County Transient Occupancy Tax data for the fiscal year ending June 2002 indicate that the hospitality industry grew at an annual, inflation adjusted rate of 1.6 percent. The strongest growth occurred in the county's unincorporated areas and in Fortuna where TOT collections rose 3.4 percent and 3.2 percent, respectively, in real terms. TOT collections in Ferndale, on the other hand, fell by 10.6 percent in real terms. This latter figure is suggestive of the large economic potential of movie production in Humboldt County locales. Filming of *The Majestic* took place in Ferndale during FYE 2001. Anecdotal accounts from industry sources hint that this summer's activity, as measured by the TOT, is strong. Thanks once again to Don Leonard and the Humboldt County Convention and Visitor Bureau for compiling this information.

Industry analysts claim that some combination September 11 and weak business conditions that were evident even before then are responsible for a nearly 11 percent drop in Northern California hotel and motel occupancy rates during the first seven months of 2002. According to PKF Consulting, average occupancy for the region was 62.8 percent for the period. The figure for the corresponding period in 2001 was 70.3 percent (www.sfgate.com).

Gasoline Prices:

Average Price* (as of 9/17)		Change From Previous Month (cents/gal.)
Eureka	$1.86	+1
Northern California	$1.62	-3
California	$1.62	-1

* Current average price per gallon of self-serve regular unleaded gasoline as reported by The American Automobile Association's monthly gas survey (www.csaa.com).



Click here for a brief description of the local gasoline market's structure.

California's supply of gasoline will not keep pace with demand over the next twenty years according to a recently released report from the Natural Resources Defense Council, a New York based environmental organization. Based on current rates of consumption and production, expected population growth alone will

lead to a supply shortfall of 280,000 barrels per day by 2020. Further restrictions on gasoline supply will occur with the mandated phase out of fuel additive MTBE scheduled for the end of 2003. (Click here and here for a brief description of the MTBE issue.) As a result, the statewide average price for a gallon of gasoline will likely rise to well over $2.00, costing California drivers an extra $5 billion annually the report claims. If current price differences hold, this means Humboldt County consumers could pay as much as $2.50-$3.00 per gallon. Rather than building additional refining capacity, which would further contribute to declining air quality, the NRDC suggested a four point conservation plan that it maintains would save consumers $28 billion by 2020:

- **Increase automobile fuel economy to 42 miles per gallon by 2015, up from 24 miles per gallon toady.**
- **Provide more hydrogen fueling stations to support emerging technological advances.**
- **Provide education to help drivers understand the fuel saving benefits of following speed limits.**
- **Encourage civic planning that limits sprawl and expands public transportation.**

Some critics of the report agree with its premise, but argue that focusing solely on the demand side of the issue is unrealistic. They claim a combination of conservation and increased production will be required for a viable solution (www.sfgate.com).

Electricity Consumption

We use kilowatts-hours of electricity consumed as our indicator of the energy sector of the Humboldt county economy. Electricity consumption is a somewhat mixed or ambiguous indicator that usually correlates with economic activity. However, beneficial increases in energy efficiency and conservation reduce the sector's *Index* value. Because we collect our data for this sector quarterly, the *Index* values are estimated, and are revised when the quarterly data are received.

Estimated August consumption of electricity rose a seasonally adjusted 4.6 percent from the previous month. We will have a more comprehensive report of this summer's electricity consumption next month when actual third quarter data become available.

The chief administrative law judge of the Federal Energy Regulatory Commission recently concluded that El Paso Corporation illegally manipulated the California energy market during the winter of 2000-2001. By withholding at least 10 percent of the natural gas supply it was required to ship to the state, a crisis was precipitated and gas prices soared. As a direct result, Californians paid an estimated $4 billion in inflated energy costs and El Paso reportedly increased their profits by more than $200 million. If the five FERC commissioners approve the finding, state officials will be in a much stronger position as they seek to have as much as $9 billion refunded from a number of energy firms. William Wise, chairman and CEO of El Paso claimed his company has always operated its pipeline properly and is confident that the full commission will reject the judge's finding (www.sfgate.com and www.nytimes.com). Not to be cynical or anything, but Mr. Wise may have an additional reason to feel confident. According to Federal Election Commission records, he personally made nearly $40,000 in political donations during the 1998, 2000 and 2002 election cycles (www.opensecrets.org).

Meanwhile California Public Utilities Commission investigators continue to build their case against electricity producers who allegedly withheld generating capacity during the energy crisis in order to increase their profits. According to a recently released report, the PUC claims it now has proof that there was sufficient capacity to meet demand during several of the blackouts California experienced in early 2001. The energy firms involved disputed the claim. The report does not prove that suppliers illegally manipulated the market (www.sfgate.com).

The United States Justice Department recently convened a grand jury in San Francisco to investigate the role Enron played in the California energy crisis. A separate federal grand jury in Houston is looking into allegations of securities fraud on the part of the failed energy giant. Justice Department officials refused to comment, but it is suspected that this latest in a long string of federal investigations of Enron will attempt to determine whether the company illegally gamed the state's deregulated electricity market (www.sfgate.com).

Governor Gray Davis signed legislation requiring the state's utilities to buy 20 percent of the power they provide to consumers from renewable energy sources like wind farms and solar generators. Proponents of the measure hope to decrease California's dependence on out-of-state supplies of natural gas for electricity generation. The law should greatly aid renewable energy companies in arranging financing for their projects. According to the law's author, rates will not increase because the higher-priced renewable power will be subsidized by a fee consumers are already paying as part of their monthly bills (www.sfgate.com).

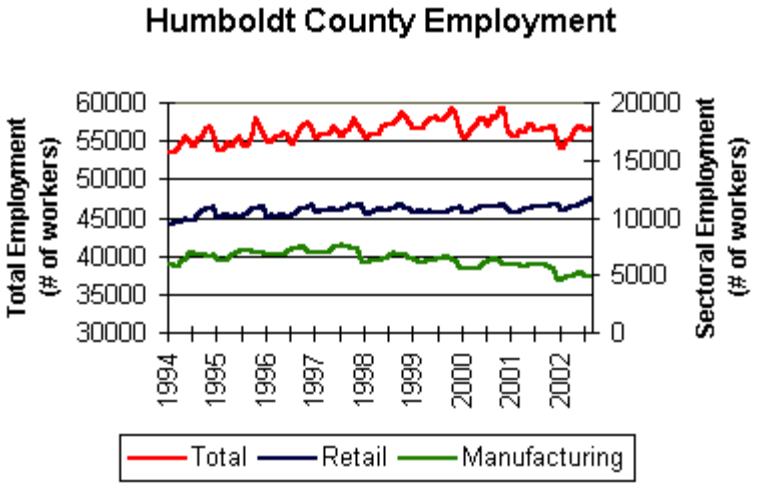
Total County Employment

In their preliminary report for August, the Employment Development Department (EDD) reported that 56,700 people were employed in Humboldt County. This is up 0.5 percent, or 300 workers, from July's figure. The small increase Preliminary EDD data indicate the following changes in Humboldt county employment:

- **Total county employment in the various service industries increased 1.2 percent from a revised 42,300 in the month of July to a preliminary 42,800 for the month of August. This sector is up 3.1 percent over last year's figure. The preliminary figure for the retail subsector shows 11,600 jobs, an increase of 0.9 percent from July's revised figure. This number is 7.4 percent higher than it was in August 2001.**

- **Total county manufacturing employment came in at 4,800. This is 2.0 percent lower than July's downwardly revised 4,900. Total manufacturing employment is down 12.7 percent from August 2001.**

The graph below shows employment trends over the past several years for the retail and manufacturing sectors (this includes all manufacturing jobs, not just those in the lumber industry), and for the overall economy. The line representing total employment illustrates that job growth over the last 8 years has been painfully slow. This is true even in retail, which has been the county's most consistently strong economic sector over this period. Manufacturing, on the other hand, has had a net loss of jobs since 1998. When one looks the graph for lumber manufacturing activity below, it becomes obvious that despite their declining performance in recent years, sawmills still provide the majority of the manufacturing jobs in Humboldt County.



The unemployment rate for Humboldt County fell from July's revised 5.9 percent to the current 5.3 percent according to the preliminary EDD report. Meanwhile, the national rate fell two-tenths of a percentage point to 5.7 percent and the state rate fell five-tenths of a percentage point from July's upwardly revised 6.7 percent to a preliminary 6.2 percent.

One of the more disturbing trends emerging in the national employment picture is the increasing number of workers who are dropping out of the labor force because they are not finding jobs to their liking. For example, an unemployed factory worker is less likely to be satisfied with a service sector job paying at or near the minimum wage when a better option might be to work for "under the table" wages. Also, more workers who

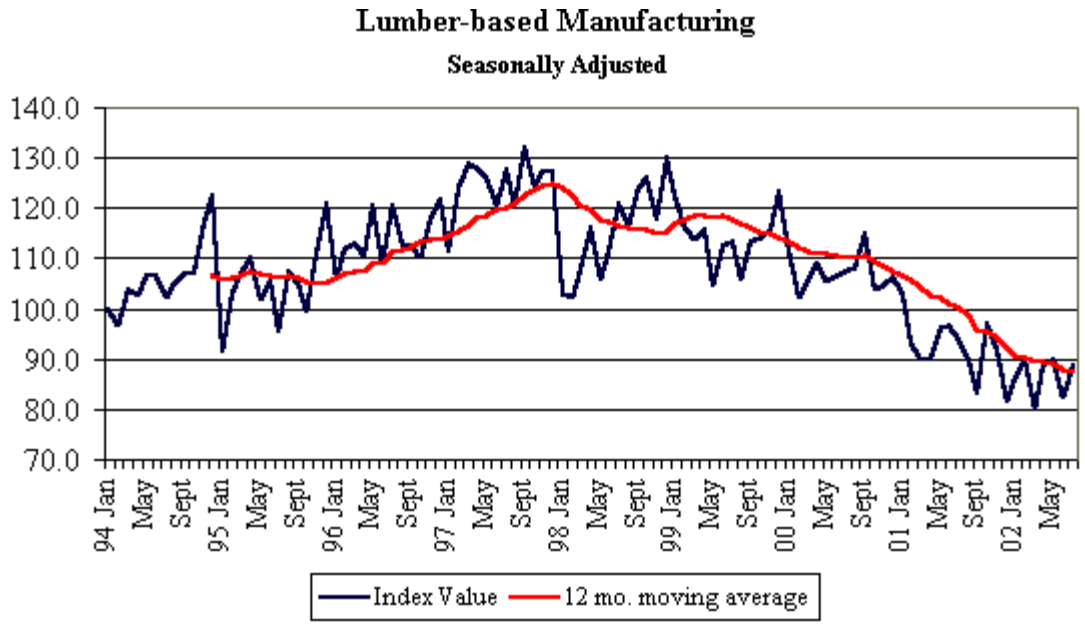
once might of worked in spite of injuries like chronic back pain and repetitive stress syndrome are now choosing to collect disability benefits. The number of people on the disability rolls has nearly doubled since 1990. In any event, these workers are no longer counted as being unemployed. Some economists claim that if all the workers who have left the workforce for reasons other than retirement or serious disability (this includes the 2 million, presumably able bodied, individuals currently incarcerated in this country) were official considered unemployed, the current unemployment rate would be much closer to the peak of 10.8 percent reached during the early 1980s (www.nytimes.com).

Lumber Manufacturing

We use a combination of payroll employment and board feet of lumber production at major county lumber companies as our indicator of the manufacturing sector for the Humboldt county economy. Lumber-based manufacturing generates about two-thirds of total county manufacturing employment.

The preliminary August *Index* value for this sector plunged once again from July's downwardly revised figure. It now stands at its second lowest level ever. The record low occurred last March when the *Index* value hit 79.8.

This data series underwent a technical revision and now more accurately portrays activity in the sector. As a result, performance levels shifted downwards slightly. This is reflected in the graph below. Unfortunately, the overall trend in the local lumber manufacturing industry remains bleak.



A Humboldt County Superior Court judge recently ruled that a previously issued stay prohibits Pacific Lumber Company from logging any timber harvest plans that rely on the approval of the firm's Sustained Yield Plan, which guides PL's harvesting practices for 100 years. Several environmental groups have challenged the legality of this document. A trial has been scheduled for next January. Most of the parties involved in the dispute characterized the initial stay as being unclear. PL claims its interpretation allowed for continued logging. The judge also ruled that six other harvest plans are exempt from the stay. A company representative said that the amount of timber available under these plans will not be sufficient to maintain current production levels through the end of the year (www.times-standard.com).

The sale of Eel River Sawmills remains on hold pending the approval of the company's shareholders. Should the deal go through, local trucking magnate Donald E. Nolan, Sr. will buy the firm's four mills, rolling stock and Fairhaven power plant to for an undisclosed cash amount. The proposed sale includes an option to purchase some 7,000 acres of timberland (www.times-standard.com).

National manufacturing output, as measured by the Institute of Supply Management, grew for a seventh

consecutive month in August. The current ISM Index level of 50.5 is unchanged from July, indicating a flat growth rate (www.ism.ws).

August saw the largest one-month loss in manufacturing jobs since January, when some 68,000 people were put out of work. Job losses in this sector had been slowing substantially for several months prior to August.

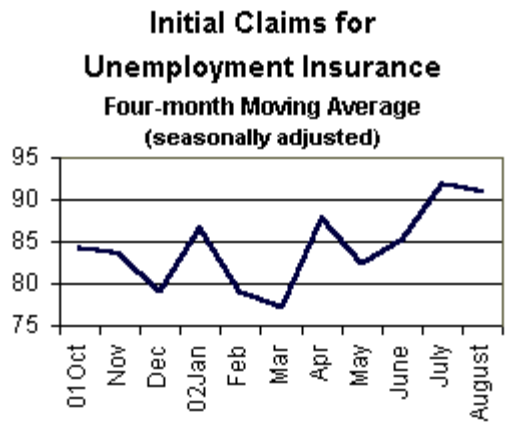
Leading Indicators

We track four leading indicators to get a sense of the direction of change in the county economy in the near future. The four leading indicators are (i) number of help-wanted advertisements in the *Times Standard*, (ii) number of claims for unemployment insurance, (iii) volume of manufacturing orders, and (iv) number of building permits issued. Our graphs in this section use a four-month moving average in order to "smooth" ordinary month-to-month volatility. In this way, any underlying trends present in the series become more apparent.

Employment-Based Economic Indicators:

A count of help-wanted ads indicates the number of new job openings.

Claims for unemployment insurance indicate the number of newly unemployed people in Humboldt County. Thus the number of new unemployment claims is a negative indicator of economic activity.

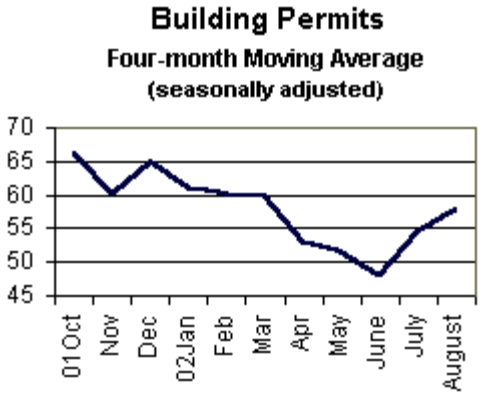


Manufacturing Economic Indicator:

Manufacturing orders, are a leading indicator of activity and employment in the County.

Home Sales Economic Indicator:

Building permits are an indicator of both construction activity and the availability of new housing stock.



The Bigger Picture

The past year has been a rough one on the national economy. About 520,000 lost jobs and $63 billion in reduced output resulted from the tragic attacks of last September according to analysts at Economy.com, a West Chester, PA economic consulting firm. Since September 11, total annual spending on defense and homeland security has grown to $657.5 billion, an increase of nearly 10 percent over the 2000 level. This rate of annual growth is expected to continue into the foreseeable future. According to Sung Won Sohn, the chief economist at Wells Fargo Bank, the additional spending represents a permanent shifting of resources from the private sector to the government sector that in the long-term will reduce productivity and economic activity. "If we are producing computers, they can be used to produce other goods. But if we are producing weapons, that is the final use of those products," Sohn said (Contra Costa Times, 9-9-02). Some might argue that weapons have the potential for far more devastation, economic and otherwise, than just the diversion of resources from more productive endeavors.

The several recent cases of corporate malfeasance have also taken a sizable chunk out of the national economy. According to the transcript of a panel discussion at the Brookings Institute, a non-partisan public policy think tank in Washington DC, the recent business scandals have cost the U.S. economy approximately $35 billion this year in lost GDP. This estimate is based on the realistic assumption that 17 percent of the loss of stock market wealth is directly attributable to the scandals and that each dollar of stock market wealth lost results in a $0.035 reduction in additional spending (the latter figure is based on a Federal Reserve Bank model) (www.citizenworks.org).

Bastions of Socialism

One of the more surprising turn of events resulting from the stock market meltdown occurred when the Conference Board, a leading not-for-profit business research firm, and the Federal Reserve Bank of New York, separately issued public statements in recent weeks calling for an end to the excessive compensation of executives at publicly traded companies. In the first of three reports to be issued by its Blue-Ribbon Commission on Public Trust and Private Enterprise, the Conference Board sharply criticized the stratospheric levels of compensation at many of the country's largest firms that have little bearing on the actual performance of those businesses. "Executive compensation has become too 'delinked' from long-term performance goals in many corporations," the report reads. "There is an imbalance between unprecedented levels of executive compensation, with little apparent financial downside risk or relationship of this compensation to long-term company performance." Among the remedies proposed by the commission are "tighter linkage between executive operating performance and executive compensation," "a fully independent, accountable, and vigorous compensation committee, "accounting neutrality," and "full disclosure of all material information on an understandable and timely basis" (www. conference-board.org).

Characterizing excessive compensation as "terribly bad social policy and perhaps even bad morals," William McDonough, the president of the New York Fed, went on to state in a commemoration speech given in Lower Manhattan on September 11 that "CEOs and their boards should simply reach the conclusion that executive pay is excessive and adjust it to more reasonable and justifiable levels." McDonough suggested these levels should be "truly related to the benefit of shareholders and other stakeholders, such as workers and the community" (www.nytimes.com).

In 1980, the average CEO earned 42 times the average worker at his or her company. By 2001, this multiple had risen to more than 400. Legislation recently introduced in the House of Representatives (HR 2691) would prevent executive pay greater than 25 times that of the average worker at a firm from being tax deductible (www.citizenworks.org).

GDP Growth Improves, But...
So far, the economy has weathered the effects of terrorism and levels of corporate greed not seen since the Gilded Age. The latest revision of second quarter GDP from the Commerce Department shows that the economy grew at an annual rate of 1.3 percent. While this number is far from robust, it is a slight improvement over the previous estimate of 1.1 percent growth. Many analysts believe third quarter GDP growth will be between 3 percent and 4 percent. The strength of current economic performance is based almost entirely on the sale of interest rate sensitive items like homes and automobiles. There is a vigorous debate among economists whether recent levels of spending on big-ticket items are sustainable. Most agree, though, that an ongoing expansion is unlikely until businesses resume capital spending. Business investment plummeted 17.6 percent in the second quarter, following a 14.2 percent drop in the first quarter (www.nytimes.com).

The Federal Reserve's Open Market Committee voted once again to leave interest rates unchanged at its September 24 meeting. Fears of further economic weakness led to the first split decision since 1998, however. Two of the committee's 12 members voted to lower rates. This result led to immediate speculation that the Fed would lower rates at its next meeting on November 6, the day after the midterm election. The federal funds target rate remains at a 40 year low of 1.75 percent (www.nytimes.com).

To Attack Or Not To Attack
An impending war with Iraq remains as the biggest cloud of uncertainty looming on the economic horizon. While the benefits of "regime change," as proposed by the Bush administration, are still being debated, the expected costs of a war are solidifying. The president's chief economic advisor estimates that the conflict would cost American taxpayers between $100 billion and $200 billion. Should the war go as planned, a huge infusion of capital will then be needed to reconstruct Iraq's devastated infrastructure and to keep the peace. Most experts estimate initial costs at an additional $50 billion. Iraq's oil reserves will undoubtedly pay for a portion of this, but it is likely that the U.S. will have annual costs of up to $20 billion in Iraq for the foreseeable future. Meanwhile, as much as $2 billion a month continues to be spent in Afghanistan. One of the issues not being debated very vigorously is where this money will come from. The federal government is expected to run a deficit of $157 billion to $165 billion this year and the Congressional Budget Office projects yearly deficits through

2010 when last year's $1.3 trillion tax cut expires (www.sfgate.com).

There is further potential for economic havoc in the volatile market for crude oil. An attack on Iraq, especially a unilateral preemptive strike, could very well lead to a significant spike in oil prices. History teaches that an OPEC embargo following the 1973 Arab-Israeli war, the 1979 Iranian revolution and the 1991 Gulf conflict all led to skyrocketing oil prices, which, in turn, contributed to subsequent recessions.

On The Waterfront
The Pacific Maritime Association, which represents U.S. and foreign shippers, instituted an indefinite lockout of dockworkers along the entire West Coast September 29 in response to what it claims was a union organized work slowdown earlier in the week. The International Longshore and Warehouse Union claims that cargo volume has been increasing steadily at ports as merchants begin to stock up from the holiday retail season and that its members are merely following safety procedures more closely. The often acrimonious contract negotiations broke down on the evening of September 27. The primary point of contention between the two groups is whether or not new job classifications created by new technologies will be union positions. $300 billion in trade moves through West Coast ports each year. Experts place the economic cost of the closure at an estimated $1 billion per day (www.sfgate.com).

Explanatory Note: For those of you who are new or less familiar with the *Index*, we have been tracking economic activity since January 1994. The composite indices plotted as blue and green lines in the diagram at the top of this page are weighted averages of each of the six sectors described in the table above. Each sectoral index, and the composite index, started at a value of 100 in 1994. Thus if the retail sectoral index value is currently 150, that means that (inflation-adjusted) retail sales among the firms that report data to us are 50 percent higher than in January 1994. We also *seasonally adjust* each sector, and the composite index, to correct for "normal" seasonal variation in the data, such as wet season vs. dry season, and so trends in the seasonally-adjusted composite index (the blue line in the diagram above) provide a better indication of underlying growth and fundamental change in the economy. This month's report reflects data gathered from the previous month, and so the "September 2002" report reflects data from August 2002. As is common, our initial report is preliminary, and as we receive final data we revise our reports accordingly.

The Eureka Times-Standard website

The San Francisco Chronicle website

The Contra Costa Times website

The New York Times website

Humboldt County Convention and Visitor Bureau website

California Association of Realtors website

National Association of Realtors website

American Automobile Association website

The Conference Board website

Institute of Supply Management webpage

U.S. Bureau of the Census's homepage

U.S. Bureau of the Census's Economic Briefing Room webpage

The Federal Reserve Bank's Beige Book webpage

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