



## Journal of Economics and Financial Analysis

Type: Double Blind Peer Reviewed Scientific Journal

Printed ISSN: 2521-6627 | Online ISSN: 2521-6619

Publisher: Tripal Publishing House | DOI:10.1991/jefa.v6i2.a56

Received: 10.09.2021 | Accepted: 30.12.2022 | Published: 30.12.2022

Journal homepage: [ojs.tripaledu.com/jefa](https://ojs.tripaledu.com/jefa)



# Oil Sector Revenues and the Marginal Propensity to Import: A Focus on Oil-Exporting African Countries

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## Abstract

Countries that possess abundant natural resources are often criticized for spending a larger portion of their revenue from selling those resources on imports, as their economies tend to lack diversification. This study aims to examine whether this claim is valid for oil-rich African countries. The paper uses the panel ARDL method to investigate the effect of oil sector revenues on the marginal propensity to import in oil-exporting African countries from 2000-2020. The findings show that in the short run, oil sector revenues do not have a significant impact on the marginal propensity to import. However, in the long run, oil sector revenues have a positive and significant effect on the marginal propensity to import. Additionally, the study reveals that exchange rates have a positive and significant impact on the marginal propensity to import, while the impact of trade openness is negative and significant. Furthermore, gross domestic savings have a negative and significant effect on the marginal propensity to import during the same period. Therefore, the study concludes that increasing oil revenues in the selected countries only resulted in a rise in imports in the long run. It suggests that oil-exporting African countries should save more during periods of rising oil prices as a buffer, and channel these savings towards building facilities that encourage economic growth. It also recommends that exchange rate policies should be used to discourage excessive importation during periods of rising oil prices.

**Keywords:** Panel ARDL; Marginal propensity to import; Oil rents; Trade openness; Foreign exchange; gross domestic savings.

**JEL Classification:** C33, F31, O24.

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## 1. Introduction

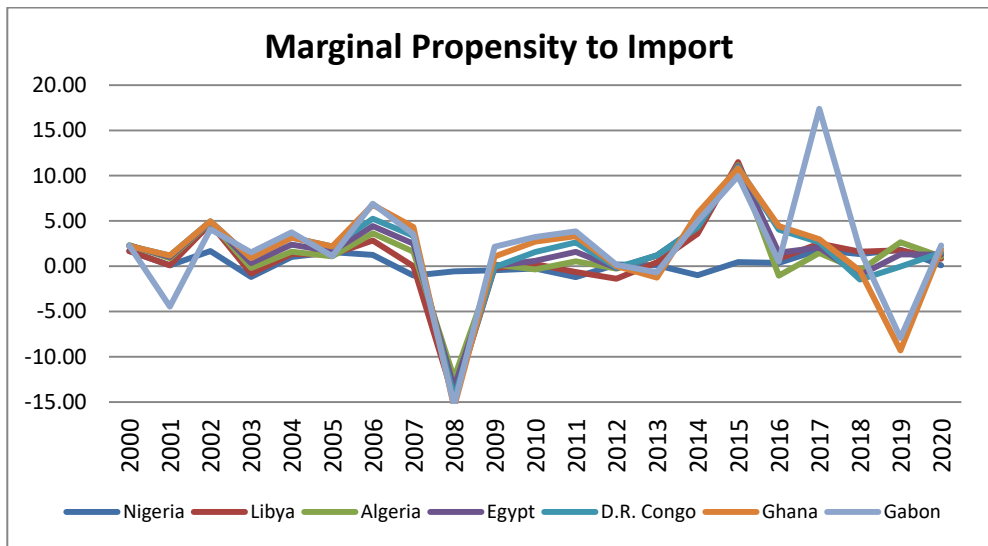
Revenues from the sale of crude oil have become a major factor that sustains many oil-exporting countries, especially developing countries that have limited sources of income. The importance of oil revenue to these countries manifests in the way provisions in their budgets is distorted each time there is a shock in the international oil price. Thus, falling oil price in any fiscal year often leads to deficit budgeting as provisions in the budget are tied to receipts from the sale of oil. As noted by Alekhina and Yoshino (2018), fluctuations in oil price have significant impact on the export revenues and government budget of energy-exporting countries. Fluctuations in oil price equally influence import propensity in oil-exporting countries. Hamdi and Sbia (2013) observed that revenues from the sale of oil are sources of financing government expenditures and the imports of goods and services. Marginal propensity to import means an increase in imports as a result of an increase in income. As income rises or falls, economic agents raise or lower their demand for imported items.

In this study the focus is on some oil-rich African countries, namely: Nigeria, Libya, Algeria, Egypt, Democratic Republic of the Congo (DRC), Ghana and Gabon. The economy of these countries is not much diversified and as such dependence on the revenues from the oil sector is a common feature. Also, the fact that their economy is less diversified means that the capacity of the manufacturing sector is low, so much so that the supply of domestically produced products is low. With this phenomenon, these countries are import-dependent and servicing the imports is mainly dependent on revenues from the sale of oil. By implication, rising oil price is expected to increase the propensity to import in these countries.

Previous empirical works focused on the contribution of oil revenue to the economic performance of oil-exporting countries. Our paper departs from previous studies by investigating if rising oil revenues led to rising marginal propensity to import in oil-exporting African countries. This study is necessary because, much as increased oil revenue improves the terms of trade of oil-exporting countries and hence, their reserve position; if such rise in oil revenue leads to rise in importation, the terms of trade gain may be eroded. Rising import bills that do not correspond to increased export could lead to balance of payments crisis, mainly if the imports are on consumer goods. The outcome of the study should therefore provide directions to policy makers in the oil-exporting African countries and indeed other oil-exporting developing countries.

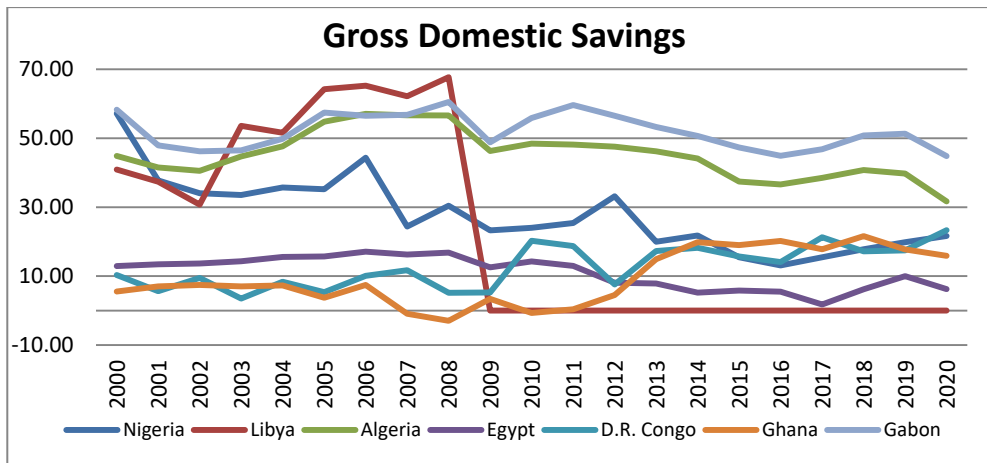
### Some Stylized Facts

The trend of marginal propensity to import shown in figure 1 indicates that major fluctuations occurred for three countries, namely: Gabon, Libya and Ghana. For instance, in 2001 the marginal propensity to import was low for Gabon, but in 2017 the country had high marginal propensity to import. Libya had low marginal propensity to import in 2008, but in 2015, the trend was high. Ghana's trend of marginal propensity to import was low in 2019. Evidence shows that apart from these years, the trend for other years for the three countries and the rest of the countries was almost flat within the study period.



**Figure 1.** Trend of Marginal Propensity to Import for each of the Countries

The trend of gross domestic savings in figure 2 showed that from 2003, Libya's trend was highest within the period when data was available and this was followed by Gabon and Algeria, respectively. The two countries that had the lowest trend were Ghana and Egypt, except before 2010 when the trend for DRC was higher than that of Egypt. When Libya had low marginal propensity to import, the trend of her gross domestic savings was high and such scenario played out in the trend for Ghana whose marginal propensity to import was low in 2019 but her gross domestic savings was high in the same period. For Gabon, evidence shows that while the trend of marginal propensity to import was high in 2017, the trend of gross domestic savings was low within the same period. All these show the dampening effect of high domestic savings on the marginal propensity to import.



**Figure 1.** Trend in Gross Domestic Savings for the Selected Countries

## 2. Literature Review

The literature has been replete with empirical studies that have investigated the impact of oil revenue on the economy of oil-exporting countries. For Nigeria, Aregbeyen and Kolawole (2015) investigated the link among oil revenue, economic growth and government spending. The study used the Granger causality test to show that oil revenue Granger caused both total government spending and growth. In a study involving 52 developing countries, AL-Risheq (2016) used the fixed effects model to reveal that an increase in oil prices has a negative and significant impact on industrial production. In Malaysia, Zakaria and Shamsuddin (2017) used Granger causality to reveal that crude oil variables did not Granger cause government expenditure in the long run. Rotimi and Ngalawa (2017) used the panel structural vector autoregressive (P-SVAR) to show that economic performance of the sampled countries was significantly influenced by oil price shock. In Russia, Alekhina and Yoshino (2018) used the vector autoregressive (VAR) approach to reveal that volatility in oil price had significant impact on the macroeconomic variables considered in the study such as consumer price index, interest rate, real GDP, among others. In another study for Nigeria, Imandojemu and Toyosi (2018) used the ARDL to show that a direct and significant relationship existed between revenue from oil and economic growth.

Farhad, Yoshino, Rasoulinezha and Chang (2019) applied a simultaneous equation model (SEM) through a weighted two stage least squares (W2SLS) to show that oil-producing countries gained from oil price increases, while for oil-

importing countries, the effect differed across the countries. In Saudi Arabia, Haque and Imran (2020) used the ARDL to show that a positive link existed between oil prices and terms of trade both in the short run and in the long run. Ologunde, Kapingura and Sibanda (2020) used the pooled mean group (PMG) and the panel ARDL to reveal that changes in crude oil price had a negative impact on sustainable development in some selected oil-producing African countries. In a cross-country study involving nine Arab oil-exporting countries, Bentour (2021) used a Bayesian vector autoregressive (BVAR) method to reveal that volatility in oil price had much impact on the real sector. In another cross-country study involving African OPEC countries, Bala and Chin (2022) used a fully modified OLS and a dynamic OLS to show that both an increase in oil prices and in oil exports improved the trade balance of the sampled countries. For selected African oil-producing countries, Olayungbo and Umechukwu (2022) used the panel VAR to reveal that oil price shocks were persistent and higher in Algeria and Egypt, but for Gabon and Nigeria, the impact was lower. In another study for Nigeria, Ebimobowei (2022) used the OLS to reveal that, while crude oil sales and crude oil/gas export had negative link with real gross domestic product, petroleum profit tax/royalty had positive relationship with real gross domestic. In Malaysia, Kriskkumar, Naseem and Azman-Saini (2022) used the ARDL and the nonlinear ARDL models to show that oil price changes impacted the economic growth asymmetrically.

### **3. Methodology**

The panel autoregressive distributed lag (ARDL) model was used in this study to examine the impact of oil sector revenues on the marginal propensity to import in the selected oil-exporting African countries. The ARDL can be used in the investigation of the stationarity of the series, notwithstanding that the series are integrated of order zero  $I(0)$  or order one  $I(1)$  or even when they have mixed order of integration. In this study, the panel unit root tests such as the Levin, Lin and Chu (LLC), Im, Pesaran and Shin (IPS), augment Dickey Fuller-Fisher (ADF-Fisher) and the Phillip-Perron-Fisher (PP-Fisher) were employed to identify the stationarity (unit root) in the variables. The cointegrating relationship among the variables was conducted using both the Pedroni residual panel cointegration and the Johansen Fisher panel cointegration tests. The existence of a long run relationship among the series led to the examination of both the short run and long run impact of the independent variables on the marginal propensity to import.

## Data

This study uses annual series that covered the period from 2000-2020 and the data for all the series are obtained from the data bank of the World Development Indicators. Inflation Rate is measured by the consumer prices in annual percentage, Oil Rent is measured as a percentage of GDP, while Exchange Rate is measured by the official exchange rate in local currency unit per USD period average. Gross Domestic Savings is measured as a percentage of GDP, while the GDP used in the calculation of the marginal propensity to import as well as trade openness is measured in constant 2010 US Dollars for all the countries, except Nigeria and Ghana whose GDP is measured in 2015 US Dollars. Also, both the export and import used in the calculation of trade openness are measured in constant 2010 US Dollars for all the countries, except Nigeria and Ghana whose export and import are measured in 2015 US Dollars. Trade openness is calculated as the ratio of the sum of export and import to the GDP which can be expressed as follows:

$$TO = \frac{X + M}{GDP}$$

Where TO is Trade Openness, X is Exports, and M is Imports.

The marginal propensity to import was calculated as the ratio of the increase in total imports to increase in GDP. Mathematically, this can be expressed as:

$$MPIM = \frac{\Delta M}{\Delta GDP}$$

Where MPIM is Marginal Propensity to Import, M is Imports, GDP is Gross Domestic Product. The  $\Delta$  indicates change from previous period.

## Model Specification

The relationship between the marginal propensity to import, the oil sector revenue and other explanatory variables can be expressed in the following functional form:

$$MPIM_t = f(OIL_t, TO_t, EX_t, INF_t, GDS_t) \quad (1)$$

The above equation is expressed in a panel ARDL form as follows:

$$\begin{aligned}
 \Delta MPIM_{i,t} = & \delta_0 + \sum_{j=1}^p \delta_{1j} \Delta MPIM_{i,t-j} + \sum_{j=1}^p \delta_{2j} \Delta OIL_{i,t-j} + \sum_{j=1}^p \delta_{3j} \Delta TO_{i,t-j} \\
 & + \sum_{j=1}^p \delta_{4j} \Delta EX_{i,t-j} + \sum_{j=1}^p \delta_{5j} \Delta INF_{i,t-j} + \sum_{j=1}^p \delta_{6j} \Delta GDS_{i,t-j} \\
 & + \varphi_1 \Delta MPIM_{i,t-1} + \varphi_2 \Delta OIL_{i,t-1} + \varphi_3 \Delta TO_{i,t-1} + \varphi_4 \Delta EX_{i,t-1} \\
 & + \varphi_5 \Delta INF_{i,t-1} + \varphi_6 \Delta GDS_{i,t-1} \\
 & + \varepsilon_{i,t}
 \end{aligned} \tag{2}$$

Where  $MPIM_{i,t}$  is marginal propensity to import of country  $i$  at time  $t$ ;  $OIL$  is oil rent (a proxy for oil revenue);  $TO$  is trade openness index of the country;  $EX$  is exchange rate of the country;  $INF$  is inflation rate of the country;  $GDS$  is gross domestic savings of the country; and  $\varepsilon$  is an error term.

The model comprises both short-term coefficients ( $\delta_1, \delta_2, \delta_3, \delta_4, \delta_5$ , and  $\delta_6$ ) and long-term coefficients ( $\varphi_1, \varphi_2, \varphi_3, \varphi_4, \varphi_5$ , and  $\varphi_6$ ). To test whether there is a long-term relationship between the series, the null hypothesis is formulated as  $\varphi_1 = \varphi_2 = \varphi_3 = \varphi_4 = \varphi_5 = \varphi_6 = 0$ . This hypothesis is test with Wald analysis where its rejection based on the critical values from Pesaran et al (2001) indicates the presence of long-term cointegration between the series, but only if the residual of equation 1 is stationary. If these requirements are met, a Panel Error Correction Model (PECM) can be created, as shown below.

$$\begin{aligned}
 \Delta MPIM_{i,t} = & \gamma_0 + \sum_{j=1}^n \gamma_{1j} \Delta MPIM_{i,t-j} + \sum_{j=1}^n \gamma_{2j} \Delta OIL_{i,t-j} + \sum_{j=1}^n \gamma_{3j} \Delta TO_{i,t-j} \\
 & + \sum_{j=1}^n \gamma_{4j} \Delta EX_{i,t-j} + \sum_{j=1}^n \gamma_{5j} \Delta INF_{i,t-j} + \sum_{j=1}^n \gamma_{6j} \Delta GDS_{i,t-j} + \lambda_c ECT_{i,t-1} \\
 & + \omega_t
 \end{aligned} \tag{3}$$

where  $\lambda$  is error-correction coefficient of the PECM.

#### 4. Results and Discussion

The descriptive statistics results shown in table 1 reveal that the variable with the highest mean is exchange rate with the mean value of 241.2761 and a corresponding standard deviation of 357.9374. On the other hand, marginal propensity to import has the least mean value of 0.3250 and a standard deviation

of 2.3597. The mean value of gross domestic savings is higher than the mean value of oil rent, implying that savings from the oil rent is just but a fraction of total savings in the economy of the sampled countries. In another respect, exchange rate has the highest range among the variables sampled which indicates that it exhibited the highest volatility within the sample period. However, marginal propensity to import, with the least range, has the lowest volatility. Findings equally show that the mean and the median of marginal propensity to import and trade openness are very close, indicating that these variables experienced low volatility within the study period. For the rest of the other variables, their mean and median are not close, indicating that they are volatile.

**Table 1.** Descriptive Statistics

	MPIM	OIL	EX	GDS	INF	TO
<i>Mean</i>	0.3250	15.5555	241.2761	25.5770	13.8240	0.6523
<i>Median</i>	0.3698	9.9865	77.4655	18.8516	5.8984	0.6304
<i>Maximum</i>	14.4206	66.7128	1851.1220	67.7111	513.9068	4.4914
<i>Minimum</i>	-14.0774	0.0000	0.0000	-2.9634	-2.1976	-0.3485
<i>Std. Dev.</i>	2.3597	16.5431	357.9374	20.1472	51.7722	0.4895
<i>Skewness</i>	-0.0316	1.2836	2.1231	0.3948	8.4173	3.6673
<i>Kurtosis</i>	24.1641	3.9280	8.0446	1.7729	75.3708	28.8057
<i>Jarque-Bera</i>	2687.5350	44.7111	260.8637	12.7754	33125.6300	4318.3820
<i>Probability</i>	0.0000	0.0000	0.0000	0.0017	0.0000	0.0000
<i>Sum</i>	46.8030	2239.9980	34743.7600	3683.0870	1990.6600	93.9283
<i>Sum Sq. Dev.</i>	796.26	39135.45	18321039.00	58044.81	383290.80	34.26
<i>Obs.</i>	144	144	144	144	144	144

At above part of the table 2, the panel unit root (stationarity) results evaluated at level revealed that, at the 5% level of significance, both the marginal propensity to import and inflation rate achieved stationarity (had no unit root) at level in all the tests. In other words, both variables are  $I(0)$ . However, other variables did not achieve stationarity at level, indicating that they need to be differenced in order to achieve stationarity.

At below part of table 2, results of the panel unit root at first difference is presented. The results show that they series now achieve stationarity. In other words, after first differencing of the series, they all became  $I(1)$ .

**Table 2.** Panel Unit Root Tests

Variable	Common		Individual	
	LLC	IPS	ADF-Fisher	PP-Fisher
<b>Test at Level</b>				
<i>MPIM</i>	-3.44*** (0.00)	-3.27*** (0.00)	35.06*** (0.00)	67.12*** (0.00)
<i>OIL</i>	2.07 (0.98)	0.991 (0.83)	7.92 (0.89)	8.52 (0.86)
<i>EX</i>	3.07 (0.99)	2.96 (0.99)	12.03 (0.60)	5.61 (0.97)
<i>GDS</i>	0.44 (0.67)	0.53 (0.70)	8.47 (0.86)	17.26 (0.24)
<i>INF</i>	-42.69*** (0.00)	-18.78*** (0.00)	301.3*** (0.00)	314.47*** (0.00)
<i>TO</i>	-0.40 (0.34)	-0.51 (0.30)	20.61 (0.11)	12.85 (0.53)
<b>Test at First Difference</b>				
<i>MPIM</i>	-2.28*** (0.01)	-6.75*** (0.00)	68.68*** (0.00)	636.49*** (0.00)
<i>OIL</i>	-1.42* (0.08)	-3.97*** (0.00)	40.981*** (0.00)	50.62*** (0.00)
<i>EX</i>	-3.37*** (0.00)	-2.41*** (0.00)	28.39*** (0.01)	36.03*** (0.00)
<i>GDS</i>	-4.74*** (0.00)	-5.90*** (0.00)	60.64*** (0.00)	129.49*** (0.00)
<i>INF</i>	-35.92*** (0.00)	-19.58*** (0.00)	333.08*** (0.00)	393.66*** (0.00)
<i>TO</i>	-4.52*** (0.00)	-3.95*** (0.00)	41.10*** (0.00)	61.73*** (0.00)

**Note:** The \*\*\*, \*\*, \* signify significance at 1%, 5%, 10% level of significance.

Having investigated the order of integration of the series with the results showing a mixture of I(0) and I(1), the study went further to ascertain the cointegrating relationship (long run relationship) among the variables. The results of Pedroni panel cointegration in table 3 reveals that in the within group, the PP and the ADF tests are significant since their p-values are less than 5%. Also, the between group results show that the p-values for both the PP and the ADF tests are less than 5%. With these results, the conclusion is that the series are cointegrated. To further confirm the result of the Pedroni panel cointegration

test, the results of the Johansen-Fisher panel cointegration test in table 4 reveals that in all the levels, the p-values of both the Trace and the Maximum Eigenvalues are less than 5%. Again, this indicates that the series are cointegrated.

**Table 3.** Pedroni Residual Cointegration Test

	t-statistics	Prob.
<b>Within Group</b>		
panel v-statistics	-1.3361	0.9095
panel rho-statistics	0.3942	0.6533
panel pp-statistics	-6.5997***	0.0000
panel ADF- statistics	-2.0555***	0.0199
<b>Between Group</b>		
panel rho-statistics	1.0023	0.8419
panel pp-statistics	-12.1159***	0.0000
panel ADF- statistics	-2.1774***	0.0147

**Note:** The \*\*\*, \*\*, and \* indicate rejection of the null hypothesis at 1%, 5%, and 10% significance levels respectively.

**Table 4.** Johansen Fisher Panel Cointegration Test results

Unrestricted Cointegration Rank Test (Trace and Maximum Eigenvalue)				
Hypothesized No. of CE(s)	Fisher Stat.*		Fisher Stat.*	
	Trace Stat.	Prob.	Max-Eigen Stat.	Prob.
None	319.6***	0.0000	178.5***	0.0000
At most 1	170.6***	0.0000	118.6***	0.0000
At most 2	93.98***	0.0000	67.74***	0.0000
At most 3	67.48***	0.0000	50.04***	0.0000
At most 4	33.32***	0.0026	28.25**	0.0132
At most 5	23.67**	0.0501	23.67**	0.0501

**Note:** The \*\*\*, \*\*, and \* indicate rejection of the null hypothesis at 1%, 5%, and 10% significance levels respectively.

With the cointegration results showing that the series are cointegrated, the study investigates both the short-run and the long-run impact of oil revenue and other explanatory variables on the marginal propensity to import. The results of the short run ARDL in table 5 reveals that none of the independent variables have significant impacts on the marginal propensity to import within the study period. It implies that in short-run these variables fail to influence the marginal propensity

to import. Thus, it takes time before the effect of these variables to manifest on the marginal propensity to import. In terms of the impact of the individual independent variables on the marginal propensity to import, findings show that oil rent has a negative impact on the marginal propensity to import in the short run; however, the impact of exchange rate is positive within the period. The reason for the negative impact of oil revenue on the marginal propensity to import could be that the increase in oil rent does not transmit to additional import in the short run. Evidence also shows that both inflation rate and gross domestic savings have inverse relationships with the marginal propensity to import, while the link between trade openness and marginal propensity to import is positive. As expected, the coefficient of the error correction model (ECM) is negative and statistically significant, which supports the long run relationship among the variables. It indicates that the system adjusts to its long-run equilibrium at a speed of 87 percent per period.

**Table 5.** Short-run PECM ARDL Results

<b>Variable</b>	<b>Coefficient</b>	<b>Std. Error</b>	<b>t-Statistic</b>	<b>Prob.*</b>
<b><math>\Delta OIL</math></b>	-0.0355	0.0533	-0.6657	0.5073
<b><math>\Delta EX</math></b>	1.2858	1.0963	1.1729	0.2439
<b><math>\Delta INF</math></b>	-0.0457	0.0472	-0.9684	0.3354
<b><math>\Delta TO</math></b>	6.6122	4.0278	1.6416	0.1042
<b><math>\Delta GDS</math></b>	-0.0015	0.0354	-0.0421	0.9665
<b><i>intercept</i></b>	1.1934	0.4324	2.7598	0.0070
<b><math>ECM_{t-1}</math></b>	-0.8732	0.1984	-4.4014	0.0000

The long run ARDL results in table 6 reveals that all the series have significant impact on the marginal propensity to import with the exception of inflation rate. To begin with, oil rent has a positive and significant impact on the marginal propensity to import. One unit rise in oil rent leads to an increase in the marginal propensity to import by 0.13 units. By implication, as revenues from oil rose in the oil-exporting African countries, their propensity to import foreign goods rose. Exchange rate also has positive and significant impact on the marginal propensity to import in the long run. It indicates that a unit increase in exchange leads to 0.003 unit increase in the marginal propensity to import. This result is in line with economic expectation as rise in oil rent leads to currency appreciation which encourages more imports since it makes the value of domestic currency in relation to the value of foreign currency to be strong.

The results show that inflation rate has positive but insignificant impact on the marginal propensity to import. In addition, our findings indicate that trade openness has a significant and negative effect on the marginal propensity to import. Specifically, an increase of one unit in trade openness results in a reduction of 4.38 units in the marginal propensity to import. This finding is surprising because it is commonly believed that opening up the economy would encourage more imports. On the other hand, we also observe that gross domestic savings has a significant and negative impact on the marginal propensity to import during the period analysis. When domestic savings increases by one unit, the marginal propensity to import decreases by 0.05 units. This result is in line with the expected outcome, as domestic savings should reduce the amount of money allocated towards importing goods.

**Table 6.** Long-run ARDL Results

<b>Variable</b>	<b>Coefficient</b>	<b>Std. Error</b>	<b>t-Statistic</b>	<b>Prob.*</b>
<i>OIL</i>	0.1339	0.0259	5.1632	0.0000
<i>EX</i>	0.0028	0.0004	7.3764	0.0000
<i>INF</i>	0.0022	0.0014	1.6443	0.1036
<i>TO</i>	-4.3800	1.1427	-3.8330	0.0002
<i>GDS</i>	-0.0473	0.0210	-2.2465	0.0271

## 5. Conclusion

This study is conducted in response to the observation that many African countries that export oil tend to waste revenue from oil on unnecessary imports instead of investing in productive ventures. The aim of the study is to determine whether an increase in oil revenues leads to an increase in the marginal propensity to import in these countries. The results of this study reveal no significant impacts of oil revenues on the marginal propensity to import in the short-run. However, in the long run, oil revenues have positive and significant impact on the marginal propensity to import. On the other hand, the study finds that gross domestic savings and trade openness reduces the marginal propensity to import, while the exchange rate has a positive and significant impact on it. The study concludes that the rise in oil rents in these countries has a positive impact on their marginal propensity to import in the long run.

Furthermore, the study also finds that an increase in the exchange rate, which often occurs when oil prices rise, is a major factor in the increase of imports. While improved domestic savings tends to decrease importation. These results have important policy implications for African countries that export oil. One such implication is that exchange rate policies should be adjusted during periods of rising oil prices, and complemented with other measures to control inflation. Additionally, these countries should encourage savings by implementing an excess crude account in countries that do not have one, and strengthening existing savings measures in countries that do. The savings should then be directed towards developing infrastructure to support economic growth.

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