INSTITUTIONS AND ECONOMIC PERFORMANCE

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ABSTRACT

The article aims to examine important research on the impact of institutions on economic performance, specifically how they influence investment in physical and human capital. The goal is to create a clear and inclusive definition and classification of institutions, and also to build a conceptual model that explains how institutions and socioeconomic development interact with each other. Research has shown that organizations and systems played a key role in making technological advancements possible and bringing the world into the current economic system. Furthermore, scientific studies show that institutions have a strong influence on how well a country or region performs economically and socially in different parts of the world.

Keyword: Institutions, Institutions and Economic Growth, Development Economy, Industrial Change

INTRODUCTION

There is a lot of talk about why some countries have better economies than others. Rodrik and his colleagues in 2004, someone said that there is no question in economics that is more important or relevant to most people in the world.

Many books and articles have talked about how institutions (like laws and organizations) play a big role in why some countries are richer than others. Institutions are rules and customs that impact how much money is spent on building things and on people's education and skills. They include both official rules set by the government and unwritten beliefs, norms, and customs. Institutional economics is different from traditional micro and macro analysis.

The purpose of this study is to examine information about the importance of institutions in economic performance. This will involve looking at economic history and data. The study also intends to create a clear definition and grouping of institutions. Additionally, it aims to develop a model that shows how institutions and socio-economic development interact with each other. This study focuses on economic, political, and value institutions. The study used logical thinking and comparing different sources of information to analyze the information. It also brought all the findings together and made conclusions based on the information that was gathered.

1. Organizations and economic growth

Institutional economics emphasizes the important role of organizations in how well the economy performs. Some people believe that things like new ideas, making things on a larger scale, education, or saving money are not what make economies grow, but are actually the growth itself. They think that the real reason for differences in how economies develop is because of the way a country is run and its economic rules.

In the late 1900s, economists started studying the rules and systems that affect the economy. This change has been affected by the end of communism, the shift from socialism to capitalism in countries that used to be part of the Soviet Union and China, and the continued lack of development in poorer countries.

We have understood that the market won't work well unless the public and private institutions create an atmosphere that encourages productive behavior. Horwitz and Boettcher (2005) describe it as a shift from the government directly controlling economic activity to creating favorable conditions for growth, where the role of economic policymakers' changes from trying to plan economic development to nurturing economic development.

Institutions are things that people create to help them interact with each other. They are like the rules we follow in society. These are the social rules and norms that affect how people interact with each other. They encourage people to behave in a certain way and are reinforced through people's interactions with each other. North (1993) says that institutions are made up of rules, norms, and ways they are enforced. Hall and Jones (1999) describe social infrastructure as "the systems and rules created by the government that affect how people gain skills, businesses make money, and goods are produced."

The way institutions work can have an impact on how much money is invested in things like buildings and equipment, as well as people's skills and knowledge. It can also affect how businesses are run and how things are made or provided. To have more output from each worker, the social structure should create an environment that helps people work efficiently and saves money, learn new skills, come up with new ideas, and share new technologies. Figure 1 shows how institutions contribute to economic development.

The reason why institution are important is because transaction can be expensive. Transaction costs are the expenses the expenses related to determine measurements, ensuring and protecting rights. And making sure agreements are followed. Efficient economic institutions help save money by reducing the costs of gathering information and taking risks.

By making sure products are good, reducing the chance of having things taken away, and making sure agreement are followed.(North 1990)

As we face uncertain economic and political situation, we cannot completely rely on the assumption that people always make rational decisions based on their own interest. North (1993) says that institutions change and develop because people learn from their experiences. This include both individuals and whole societies. Institutions are created by people and depend on the decisions made by society. They are shaped by what we learn over time and are passed down through our culture. Institutional economic focus on how things like history, culture, and social and political factors affect institutions. Rodrik and his team in simple terms, the authors suggests that institutions are the result of past policy decisions. The first equation represents policy as something that change over time, and institutional quality as something that remains constant. I use the letter I to represent the size or importance of the policy. This text is talking about three different types of policies (fiscal, monetary, trade) and their impact in institutional quality. It also mentions a rate at which institutional quality decrease if no action is taken to prevent it.

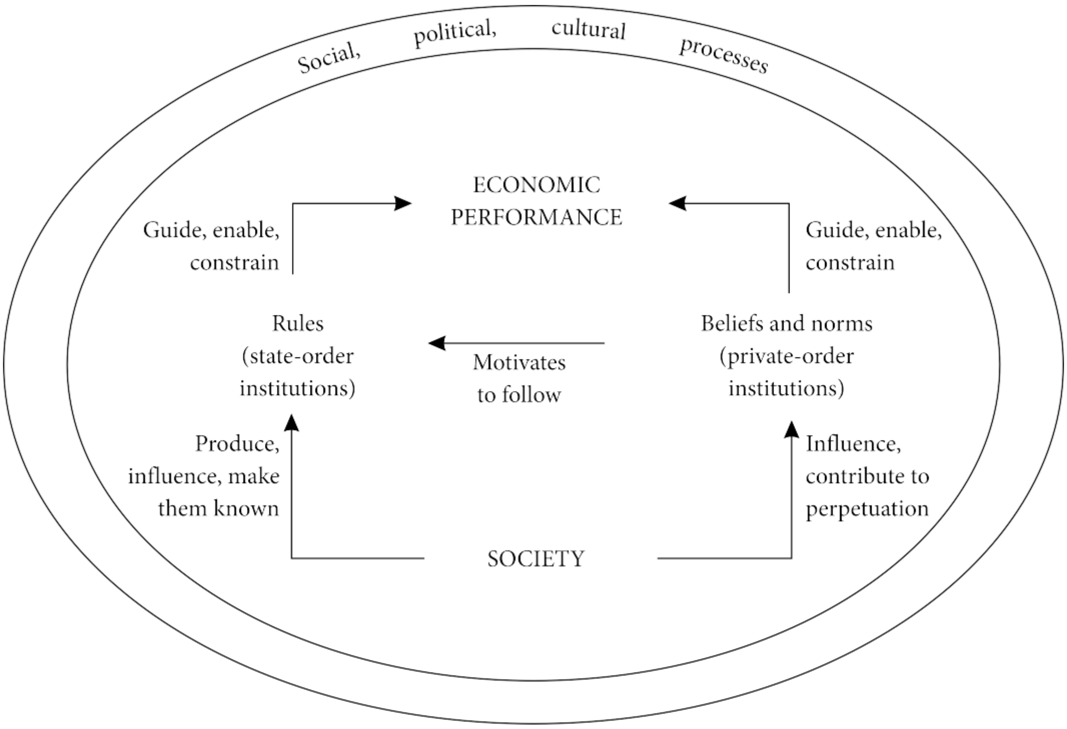

Fig. 1. Conceptual framework for the relationship between institutions and socioeconomic success (created by the authors)

$$I = \sum \alpha_i \mathrm{p}_i - \delta I \qquad (1)$$

Also, because knowledge is passed down from one generation to another shared culture, institutions are greatly impacted by past decisions and experience. Sometimes, what we have learned from the past might not be enough to solve new problems. As a result, societies could end up being unable to make progress. North (1994) says that many societies in the past stayed in a system of rules and structures that didn't change into a fair way of trading that is necessary for gaining the benefits of productivity and specialization that have created wealth in nations. History shows that ideas, beliefs, stories, rigid belief, and biases are important. To make progress in understanding how societies change, it is important to understand how these things develop over time.

1. Institutions of economics, politics and morality

According to our study, institutions are accepted ways of behaving that limit a person's choices and guide their actions. These institutions can either restrict or encourage how people behave in their communities. We believe that good institutions help society use limited resources effectively to meet everyone's needs. In addition, we divide institutions into three different groups - economic institutions, political institutions, and value institutions. 2) Rewrite this text usingsimpler words:

Economic organizations should give rewards or motivations for investing in both people and physical assets. Economic institutions are judged based on how much the rule of law is followed and how good the rules and regulations are. Corruption also plays a role as it can unfairly affect how markets work by limiting fair competition.

The most important parts of the economy are the rules about owning things and being able to buy and sell things. The market is a type of organization that is spread out in many different places. It helps to divide resources effectively, motivates people to work hard, and can adjust well to changes. (Williamson 1995) Property rights encourage people to invest in things like land, buildings, and money. Protection against expropriation helps motivate people to invest their time and money, particularly in things that will last a long time, like buildings and equipment. Control and stability often come at the expense of individual freedoms and human rights.

Protection for physical and intellectual property rights is attractive to high-tech industries and industries that rely on specialized, long-lasting assets.

This study shows that institutions have a stronger effect on the accumulation of physical capital (such as buildings and machinery) than on the accumulation of human capital (such as education and skills). In fact, the impact of institutions on physical capital accumulation is about six times higher than on human capital accumulation, and it also has a similar effect on productivity.

The literature also suggests that people trusting and believing in property rights is more crucial than the specific way they are written or defined. This is referring to the situation in China and Russia, the quality of institutions are not as good because they don't protect private property rights very well. In China, they don't have a strong legal system to protect property rights. This example emphasizes that actual institutions are more important than officially established institutions, simple term political organizations should guarantee that the government remains stable.

To promote investment and ensure fair competition, it is important to have a level playing field in politics. This will help ensure that decisions and actions benefit the whole society rather than just a select few in power. Furthermore, a skilled and politically unbiased group of government officials plays a significant role. These officials prioritize long-term productivity over short-term political gains because they have job security and a desire to maintain a good reputation.

The key things in politics are how the government is organized and the limits on what politicians can do. They work closely with organizations that deal with money and the economy. Political institution and the distribution of resources are two main things that stay the same in a cause-and- effect relationship. (Fig Number three.)

Political institutions are the official structures or organizations that have power in a society. These can include things like governments, laws, and rules. The distribution of resources in a society refers to how things like money, jobs, and Goods are divided among the people. It represents the actual power that exists in a society, even if it is not officially recognized. Political power, both formal and actual, shapes the way a country is governed, while economic institutions decide how the economy functions and how resources are divided. So, people pick economic organizations based on how they impact distribution.

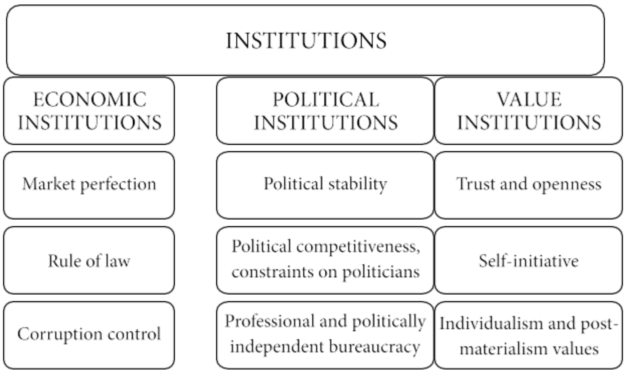

Fig. 2 shows the institutions of economics, politics, and values as developed by the authors.

The economic institutions that come into existence depend on who has control over political power. Political institutions and how power is distributed determine the differences in economic institutions. In 2005 According to North (1994), institutions are usually made to benefit powerful individuals, rather than to be socially efficient. The formal rules are created to serve the interests of those who have the power to make new rules.

A fair sharing of resources and being able to move up in society make things more equal, and the government becomes the most powerful. But, since political institutions last longer than actual political power, significant changes in political power are usually necessary to change them. In simpler terms, an institutional change that doesn't upset the current political situation is more likely to happen, even if it's not the most effective for the economy.

Achieving long-term efficiency and credibility is not an easy task.

This text is saying that politicians want to keep their jobs for the short and medium-term. According to Williamson (1995), if politicians who think short-term take control of resources or give benefits to their preferred groups immediately, and if people believe that having a large and guaranteed share of a small amount is better than having a smaller and uncertain share of a bigger amount in the future, then trustworthiness may be compromised. He believes that having a professional organization with job security and a good reputation helps improve productivity in the long term. In simple terms, when the economy gets better and grows, it is beneficial for everyone involved.

Governments want to be in charge because it will allow them to make more money through taxes and taking people's property, which will also grow their own wealth. However, advancements in technology and improvements in organizations could also be advantageous for other groups in society who may challenge political authority in the future. There is no one else who can make sure an agreement between the people in charge and their supporters is followed; if the people in charge lose power, there's no way for them to make up for it, at least not in a believable way. The issue of how to distribute political power creates a problem where we have to choose between economic productivity and fairness. 2005 is a year that happened in the past.

Acemoglu and Robinson (2006) refer to this as a "political replacement effect". As a result, if there is a lot of competition in political power and they have a strong commitment to solving problems, it will likely lead to better economic performance. To make it simpler: - By changing political systems to keep some power in check. - The country has a highly educated population, so the benefits of modernization in the future are greater.

In simpler terms, economic change is more likely to occur when: 1) a wide range of people in society have the power to make decisions and also have the opportunity to invest money, 2) the people in power are not able to take advantage of the rest of society for their own benefit, and 3) there are enough rules and regulations in place to control and monitor those in power. In 2005 Acemoglu and Robinson (2006) say that sometimes new technologies and better institutions are not allowed because people are afraid of losing power, not because of the money they could make.

Furthermore, the beliefs and principles of society affect how we utilize our resources for production. When people trust each other more, they are more likely to share information and resources. This helps to lower the costs of making things and encourages new ideas. Research has shown that businesses that share information and work together are more likely to be innovative. When people take more initiative, it helps boost the economy and society. This results in more jobs, new businesses, and activities that are not controlled by the government. Individualism reduces the importance of following normal rules and expectations. This helps with creating new ideas and thinking logically. (Greif 2000) Finally, post-materialism supports being active in the community and getting involved in politics, which helps democracy and puts more limits on those in power (Inglehart, Wenzel 2005).

2. Historical institutions in the economy

People have talked a lot about the importance of institutions in how economies grow and succeed throughout history. The research on how the economy has changed over time talks about three different stages of economic development: the old way, the improved old way, and the current way. The Malthus phase in economic development means that real wages (the amount of money people earn adjusted for inflation) do not tend to increase in the long term because any increase in wages is balanced out by a growth in population. In a Malthus economy, the number of people is controlled by two things: having fewer babies (preventive check) and more people dying (positive check), all to keep a balance. Therefore, places that are more developed will have more people living close together, but the quality of life will be the same for everyone. The main reason for having a low income per person is because there is a limited amount of an important resource called land. This resource doesn't produce as much as it used to when technology doesn't get better.

The Malthusian regime was when there was not enough food for everyone because the population was growing too fast. Then, the Post-Malthusian regime came and the population grew even faster because people got more money. The amount of money people made increased because technology improved over time (people disagree on whether this improvement was caused by factors outside or inside the system). At the same time, the use of land for production slowly decreased as other resources were used instead. The movement of people to colonies and the resources they produced helped create more land and resources for everyone.

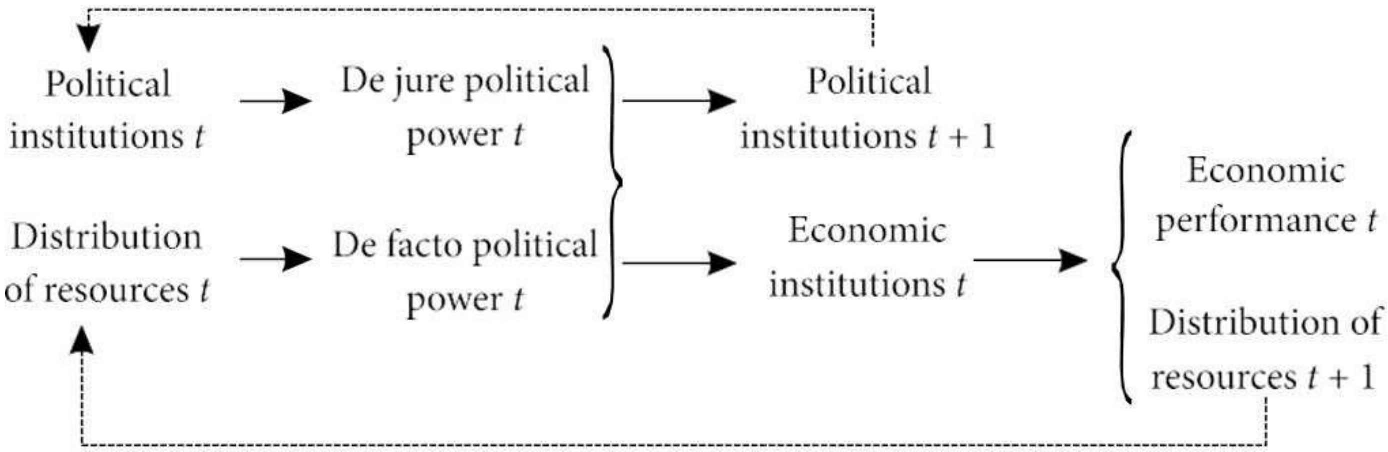

Fig. 3 shows how political and economic institutions interact (Acemoglu et al., 2005).

The increase in the number of people, advancements in technology, and the development of people's skills eventually brought about the modern era. In this era, there is a consistent growth in the level of technology and the amount of money earned per person. The connection between average income and population growth is not good because people started valuing the quality of life more than having a lot of children. This made them decide to have fewer children, as they realized that it requires a lot of resources and time to raise them. Research has shown that the English economy before the industrial era stopped following Malthusian theories around the 17th century. The factors that were preventingoverpopulation and encouraging population growth were no longer visible. The system slowly returned to a state of equilibrium according to Malthusian principles. In England, people did not have a positive check-in even in the middle of the 16th century. The demographic transition happened after the industrial revolution and started the modern growthin the early 20th century.

What role did institutions play in helping technology and progress, and therefore making progress even when there were limits? Acemoglu et al. It is believed that as early as the 14th century, the Black Death caused an increase in the income and therefore the actual political influence of peasant communities. The people gained more political power, which caused the end of feudal rules. This led to more changes in how resources were divided in society.

The literature explains that the Dutch economy in the 16th-17th century is considered the first modern economy. This time period had access to markets that worked well, people had specific jobs, the government protected people's property rights, and were accepting of skilled immigrants. Adam Smith thought that the Dutch economy was the best example for others to follow. Britain became the most powerful economy in place of the Netherlands after the Glorious Revolution in 1689. It created a group of people to make decisions, a group of employees who are experts in their field, and systems to manage money. Actually, some of these inventions were brought over from the Dutch. In 2010, Perssonpublished a study.

The Napoleonic wars happened from 1803 to 1815 and Napoleon spread his laws throughout Europe during this time. Napoleon's civil law helped those who owed money and took a long time to settle legal matters, while his commercial code favored creditors and had a faster process. At the same time, there was a helpful change in the law for creating businesses called corporations. They made it easier to form corporations that offer limited liability. Policy and institutions in England were important for the industrial revolution, while China had a higher level of knowledge but lacked those policies and institutions. Max Weber compared the legal systems of the Western world with that of China. He found that Western law was based on rational principles, while Chinese law was influenced by spiritual and magical beliefs. As a result, Weber concluded that the Western legal tradition played a key role in the development of capitalismin Western Europe.

Let's make the meaning of this text easier to understand. (Horwitz, Boettcher 2005).

The Napoleonic wars led to a greater say in politics in return for fighting in the wars, as well as the making of Europe more like a constitutional government. During the wars, the governments wanted to collect more money and pay off their debts, so they started centralizing their fiscal systems. Before, taxes were collected by using tax farming, but getting someone else to do it was expensive. In the year 2010. The growth of markets had a big impact on how the economy grew. The increase in cities and global trade led to more people taking part. After a while, the telegraph and the commercial press were introduced, giving people inexpensive, quick, and trustworthy information. The drop in information costs and the rise in law enforcement played a critical role in reducing transaction expenses. Trade and institutions influenced each other. For example, Crafts and Mills say that the Atlantic trade might have helped create capitalist institutions.

Moreover, the growth of cities and global trade altered how money and resources were spread throughout society. In the 17th century, merchants and wealthy landowners became richer because of their trade within the country and with other countries. This wealth allowed them to create armies strong enough to defeat a king. As a result, there were changes in who held political power. Changes in governmental systems caused significant changes in business systems, making the rights of land and capital owners stronger and also promoting growth in financial and commercial activities. Therefore, when economic institutions changed, it resulted in fast economic growth, the Industrial Revolution, and additional changes in how resources were shared in society. In 2005

Furthermore, the "knowledge revolution" in the educational field is taking place differently for each individual.

The enlightenment period and urbanization led to the exchange of ideas and new inventions. They are often seen as the main reasons for changes in economic systems. (Crafts, Mills 2009). Simplified: The enlightenment period and urbanization allowed people to share ideas and create new things. This is often believed to be why economic systems changed. (Crafts, Mills 2009). Rewrite this text in simple words: Glaser et al. Glaser and his team. The text from 2004 emphasizes the importance of human capital for both economic growth and democratization. It states that every community has certain opportunities and these opportunities mainly depend on the knowledge and skills of its people. The more skills and resources people have in a community, the better the chances of finding good opportunities in the community. Lastly, Acemoglu and Robinson (2006) emphasize the significance of the "commitment problem" and "political replacement effect". Industrialization was more likely to happen in states where traditional rulers and land owners were not as afraid of losing their political power and the money they made from their land. Because society became more focused on making money and the parliament gained more power over the king, Britain was better equipped for economic growth compared to countries like Russia and Austro-Hungary, where the rulers had complete control. The rich landowners in Britain started to do farming for profit. Unlike the powerful government officials in other European countries, they did not resist the growth of industries. On the other hand, the leaders of Russia and Austro-Hungary were concerned that if the country became industrialized, it may result in a revolution. In simpler terms, their income from the economy was quite high because they still had old-fashioned feudal systems in place that hadn't changed. Russia began to modernize because they were scared of other countries attacking them after they lost in the Crimean War. Austria-Hungary also started to modernize after a revolution happened in 1848.

2. Quantitative evidence

Many researchers have studied and measured how institutions impact economic growth. Hall and Jones (1999) studied information about 127 countries. They looked at things like the number of physical resources a country has, the main language spoken, how far the country is from the equator, how much it trades with other countries, how open it is to trade, the level of education of its people, the contribution of mining to its economy, and how strict its government is about preventing illegal activities. Researchers discovered that disparities in social infrastructure, which refers to the institutions and government policies that shape the economic environment in which individuals acquire skills and companies build capital and generate output, are the main reason behind variations in productivity per worker. This is because countries with strong social infrastructure possess a significant amount of physical and human capital, along with enhanced productivity levels. In addition, Hall and Jones found that countries influenced by Western Europe tend to have better social systems and produce more. This is because these countries have a larger percentage of European languages as their main language.

Also, Rodrik and the rest of the authors. In 2004, it was proven that the quality of institutions is more important than geography and trade. By looking at many different factors like geography, integration, and institutions in a group of 80 and 140 countries, researchers tried to see how these things affected income. They discovered that the quality of institutions had the biggest impact on income differences. Rodrik et al. is a scholarly article written by a group of researchers named Rodrik and others. The conclusion is that when we consider the influence of institutions, integration does not impact incomes. On the other hand, geography has only a small direct effect, if any at all.

The text is already written in simple words and does not need to be rewritten. Countries that sell oil usually have more money, while countries with a lot of malaria usually have less money.

When it comes to natural resources, we need to consider the different experiences of countries that have a lot of them. Frequently, when a large portion of a country's economy relies on selling raw materials, it results in a lower overall economic growth, higher levels of unequal distribution of resources, more corrupt practices, and an increase in conflicts within society. This trend is more common with resources that require substantial investment, like oil, rather than resources that rely more on labor, such as coffee, rice, or bananas. Countries with poor governing systems have sufferedfrom the negative effects of having valuable natural resources.

Rodkin and his team found some interesting findings. In 2004, a study revealed that certain parts of the

Trade and geography indicators, as well as property rights and the rule of law, are factors that affect income levels. Trade and geography indicators have a negative impact on income, while property rights and the rule of law have a positive impact on income. These relationships are statistically significant. Also, when studying the connections between factors, they discovered that the quality of institutions and integration both have a strong and positive influence on each other. Furthermore, the location or physical characteristics of an area greatly impact how well its institution’s function. It is interesting that having a legal system based on French laws helps increase income. On the other hand, being colonized by the United Kingdom has a negative effect on income.

Acemoglu and his colleagues wrote this text. Zoography, determine economic development. They contend that even though some countries may have favorable geographic conditions, such as fertile land or natural resources, if their institutions are weak or corrupt, they will still struggle to achieve economic growth.

In simpler words, a biography would discuss why certain areas that were once wealthy in terms of having a lot of people are now very poor after being colonized. They disagree with the idea that geography directly impacts how well the economy does, and instead believe that the reason for the change in fortune is because of changes in institutions. The research looked at data on urbanization and population density, as well as factors like institutional quality, economic performance, and geography. The findings confirmed their idea. However, they don't dismiss the importance of geography, but suggest that it was the institutions that were influential. Europeans tended to establish institutions that took resources away from people in regions that had a lot of people living there. There, they were able to use cheap workers to directly get natural resources or create large farms and mines. However, they could also gain power over institutions that were already involved in taking resources away, for example,

Tax systems are the rules and regulations put in place by a government to collect money from individuals and businessesto fund public services and programs.

Institutions that last for a long time have greatly changed societies in areas that were previously prosperous. For instance, the slave trade drastically changed how African society was structured. It caused African governments to become more powerful and engage in conflicts with each other in order to control the supply of slaves for Europeans. As a result, areas that have extractive institutions are less likely to adopt new technologies. Because of this, these areas have not become industrialized and are still not developed.

In places with very few people and not many diseases, the people created rules to protect ownership of land and belongings. This made it easier for them to trade and do business. Also, in places where many Europeans moved to, theywanted the same or even better rights than what they had in their own country.

In 2009, Reputing studied how institutions affect income levels in 128 countries. They looked at indicators like freedom, laws, corruption, and property rights. The study used GDP per capita as a measure of income level. In simpler terms, her study found that institutions (like laws and rules) are more important than trade and where a country is located. However, this is only true for 41 countries that have good-quality institutions. She believes that when institutions are of good quality, it has a positive effect on investment and the development of new technology, which in turn increases theGDP per person.

The authors of this article have also studied how institutions affect economic and social development in their earlier research. They measured the effects of institutions on development using numbers and data. We did a study that looked at many countries around the world using a type of math analysis called multiple linear regression. Lastly, we used information from the World Value Survey to measure certain values. This includes indicators like trust, self-initiative, post-materialism, and individualism. The study showed that institutions are important for how well a country is doing in terms of its economy and overall well-being.

The quality of institutions has a big impact on things like how much money people have on average and how satisfied they are with their lives.

At the same time, how much specific institutions matter depends on how developed the economy is. These findings provide evidence that when property rights are clear and market transactions work well, it helps to strengthen the argument or main point being made.

Being able to invest in things like money and people is really important for making a country develop and grow.

Corruption control, voice, and accountability are all very important in economies that focus on efficiency. Controlling corruption helps markets work better and reduces expenses for businesses. On the other hand, having a say and being able to hold leaders accountable allows people to be more involved in decision-making, which helps create laws supporting and promoting social and economic growth. In simpler words: Additionally, how well the government functions, the values of society, working together, and taking action all have a big effect on how well the economy and society do at this point in time.

In innovation-focused economies, informal institutions like trust, taking initiative, speaking up, and being responsible play a crucial role. These findings indicate that informal institutions become even more significant once formal institutions are established.

CONCLUSIONS

Institutions are rules that control how people interact with each other and encourage them to behave in similar ways. These rules can be official or unofficial and are followed by everyone, including the government and individuals. Many books and articles in institutional economics study formal institutions, which usually means property rights and the rule of law. However, this is only the most noticeable aspect. Culture, religion, laws, and even past events continue to have a big impact on economics. Institutions impact the amount of money and resources invested in buildings, equipment, and people, as well as how businesses are organized to produce goods and services. Research shows that the quality of institutions has the biggest impact on how much work people do and how much money they make globally. Institutions should help with creating things that are useful, and support saving money, learning new skills, coming up with new ideas, and sharing technology with others. Institutions are greatly affected by the way things have always been done in the past. efficiency in resources and infrastructure, which hinders their economic growth and overall progress. Consequently, these countries may struggle to achieve a desirable standard of living and may continue to lag behind more developed nations.

Situational environment means the circumstances or conditions that are present in a particular situation.

The research indicates that organizations were significant in helping technology advance and overcome economic growth limitations. The way that money and the way that businesses and governments work together made it possible for the industrial revolution to happen. This changed the way the world's economy works. The reduction in the cost of doing business made markets grow bigger, more cities were built, and more trading happened between countries. This made people want to make institutions better and share knowledge and new ideas, which led to the way our economy isnow.

Some new ideas were introduced slowly over time because society was changing. For instance, property rights became more strictly enforced and the Netherlands and Britain set up a group of people to represent them and a group of professionals to help run things. On the other hand, some new ideas and changes happened quickly because of big eventsin history. Examples include when Napoleon created the civil law system, when Europe became more organized with a constitution and when money was controlled centrally after the Napoleonic Wars. There was also progress in Russia and Austro-Hungary because they were scared of outside dangers.

The government, businesses, and organizations outside of the government should focus more on evaluating institutions.This involves measuring certain factors related to the institutions and considering how the institutions operate when making decisions in both the public and private sectors. The government should make policies that make things better for everyone.

We should include the examination of institutions as a regular part of social science research. Formal institutions, like government organizations, and informal ones, like family or community groups, both shape the values and norms in society. For example, schools and churches are formal institutions that influence how people think and behave. But even informal groups, like friends or neighbors, can also impact a person's beliefs and actions. Trust and motivation should be considered when evaluating the overall environment of an institution. The big amount of data from surveys all over the world lets us combine these factors in economic studies. It is important to carefully study and assess the formal and informal institutions in countries like Eastern and Central European countries that have recently become democracies. These countries are adopting laws from Western Europe as well as important principles and standards for the market economy to work well.

Institutions have been and still are very important in helping the economy grow. Institutional economics is a discipline that looks at how formal and informal institutions, history and modern values, and individuals and society all interact with each other. This makes it a very promising field of study.

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