

# The Mustard Seed Disposition in the Informal Sector: Analysing its Growth and Expansionary Prospects in Zimbabwe

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## Abstract

The study investigated and analysed the growth and expansionary prospects of the informal sector in Zimbabwe and the drive for people to join the sector. This was done through the desk research method and personal observation. The study reviewed the growth and graduation trends of the informal sector enterprises in Zimbabwe and the barriers to growth being faced by the sector. The study shows that the Zimbabwean informal sector enterprises are not growing or graduating due to their micro capacity and type. The implication is that both the growth and expansion prospects of this sector in Zimbabwe are very limited. This is due to many growth-inhibiting challenges and constraints faced by these enterprises reviewed in the study. The study concludes by proposing some measures that can be implemented to allow unfettered growth and expansion of the sector's enterprises.

**Keywords:** *informal sector; growth; dualism; structuralism; self-employment; economic development*

## INTRODUCTION

According to the World Bank, the informal sector around the world comprise the majority of businesses. It accounts for more than 90% of

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businesses and over 50% of employment globally (World Bank, 2021)<sup>3</sup>. Regionally the informal sector plays a significant role on the African continent contributing up to 33% of GDP, and 45% of employment (Mparutsa, 2021). The share of informal economic activity in Africa remains the largest in the world, and its employment contribution is considered as high by Chen (2001), indicating that close to 93% of newly created jobs in Africa are all coming out of the informal sector. In the Middle East, 20-40% of the workers are accommodated in the informal sector too (Gatti *et al*, 2011). Around the world, it has also been shown that economies are driven by informal sector-based enterprises; China, Brazil, Germany and India are typical examples. The formalisation and transitioning of the informal sector enterprise to big enterprises is pivotal in any economy in the world today as they act as the fertile seedbed of entrepreneurship and business growth, as well as innovation and employment creation.

The Zimbabwean informal sector has become the key engine of economic growth, job creation and economic development. According to the IMF (2017), Zimbabwe's informal sector is the sixth-largest in Africa contributing between 40% and 50% to economic growth. Currently, over 75% of the country's total workforce is absorbed by the informal sector (Mangudya, 2021), implying that approximately 7 out of 10 jobs are being created by the informal sector in the country. Indeed, there was a time when most jobs in the country came from both the public and private sector, however, this has changed and the informal sector is generating new jobs. The informal sector is contributing to the advancement of gender equality and youth empowerment in the country as it comprises more female participants and a high proportion of young business owners within the sector.<sup>4</sup>

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<sup>3</sup>These World Bank figures capture the contribution of small and medium enterprises only and therefore if the contribution of micro enterprises that constitute the bulk of the informal sector is included it means these figures could become much, much higher.

<sup>4</sup>Everyday there are young people, including many of our university graduates, in our country who keep on walk up and down the streets total defeated and having given up any hope of finding gainful employment. As a result the important role that can be played by the informal sector of continuing to absorb even more unemployed youths can prove to the much cherished panacea to the prevailing high unemployment level particularly amongst the youth in the country

The study was done through the use of desk research and personal observation. The desk research component involved the reviewing of relevant competing theories and drawing useful insights from existing complementary informal sector studies from Zimbabwe and the rest of the world. In addition, extensive and detailed document analysis was carried out to provide a good framework for analysing the study. The study included a literature search and review of existing academic and non-academic documents, that include written unpublished papers, journal articles, reports, and case studies.

## **THE INFORMAL SECTOR: CONCEPT AND THEORY**

The originality of the use of the term 'informal sector' is associated with the dualistic model of economic development put forward by Lewis (1955). It is within the confines of his theory that he identified the existence of two sectors in a dualistic economy setting: the subsistence or rural agriculture sector and the modern urban industrial sector. Lewis postulated that given the large reserve of labour supply in the subsistence sector if the rate of rural to urban migration exceeds the number of new jobs generated in the modern urban industrial sector; an additional new sector, the "informal sector", emerges. This new sector is the one that helps to absorb the excess unemployed hands in the modern urban industrial sector. The term "informal sector", however, later formally appeared in the International Labour Organization (ILO) country mission reports published in conjunction with Institute for Development Studies (IDS) economists in the early years of the World Employment Programme (Benanav, 2019).

The ILO defines the informal sector as an economic sector that is not subjected to formal contracts, licensing or taxation, with operations that are not part of the nation's Gross Domestic Product (Shinder, 1998). Saavedra and Tommasi (2007) using the same perspective define the sector as an income-generating activity that is not regulated by the state and where taxes are not collected. It is also defined as all economic activities that are hidden from official authorities for monetary, regulatory and institutional reasons (Medina and Schneider, 2018: 4). For this study, the informal sector was defined as a sector made of business people whose businesses are not registered their business activities are not regulated by the government or the government finds it difficult to

regulate. In addition, they are also involved in the buying and selling of goods and services that are not declared to the government for tax purposes, do not offer social security benefits to their employees and do not adhere to stipulated labour laws.

Based on the above definitions it can be concluded that the informal sector is a sector that incorporates people into illegal and unregulated working environments particularly in the developing world. Under these circumstances, people may choose to create their means of employment, when unable to work or find jobs in the formal sector or when the income is inadequate to sustain adequate living conditions. In this sector, workers are usually unprotected by a social safety net and the sector is subject to many illegalities in terms of working hours, minimum wage, health and safety restrictions. Minimum wage laws do not exist in the informal sector and there is no observation on the regulation of working hours (Nichter and Goldmark 2009).

The roots of the informal sector can be explained within the confines of the Dualist theory propagated by the ILO (1970). The dualistic theory explains an economy that is divided into two distinct sectors namely the formal and the informal sectors. According to the ILO (1972), the dualistic theory argues that the informal sector exists to provide a safety net and income to the poor. Explaining this from Rodan's (1943) Big Push theory perspective, Becker (2004) hinted that the existence of the informal sector will only cease to exist when a country has modernised and industrialized. Furthermore, the dualist theory focuses on the persistence of informal activities and highlights that it is a result of the inadequacy of formal job opportunities. The theory further stipulates that the expansion of the informal sector is a result of economic failure. Bureau and Fendt (2011) posit that the existence of this sector represents a systematic flaw showing failure of the economy. The reasons behind economic failure especially in developing countries include; the mismatch between population growth and employment growth. It is also caused by foreign currency shortages that lead to severe production bottlenecks that in turn exacerbate hyperinflation. Lack of sound economic policies also leads to a lack of foreign exchange needed by the country. Insufficient foreign exchange leads to low importation of critical raw materials. The

other reason is an overreliance on one sector of the economy leading to a lack of growth in the formal sector exacerbating the growth and expansion of the informal sector. Low capacity to borrow has also been cited as a cause of economic failure.

The structuralist approach was popularised by Moser (1978). It contradicts the dualistic perspective by arguing that the formal and informal sectors are independent but interconnected. The approach hints that the informal sector is a by-product of the arrival of a deregulated economy (Amin, 2002). The informal sector is linked to the formal sector through the demand and supply of inputs. Individuals join the informal sector to increase their ability to compete both locally and at the global level. Further, the expansion of the informal sector is associated with the need to reduce labour costs and avoid the powers of labour unions and formal regulations by the state. The need to compete, avoid regulations and reduce labour costs has led to the establishment of offshore industries, specialisation and subcontracting chains (Chen, 2012). People in Zimbabwe join the informal sector to avoid labour costs and regulations imposed by law. Portes *et al.* (1989) suggested that as the nature of jobs change the transfer of production contracts to the self-employed begins. In summary, structuralism reflects that informality arises out of economic necessity. Further, the need to survive in the absence of alternatives by individuals has also led to the expansion of the informal sector in developing countries.

The human capital school of thought has been championed and used by several economists, like Kim *et al.* (2003). The theory is used to explain the success of small business owners who are in the informal sector and their small businesses. The theory asserts that people with higher levels of human capital realise higher performance in executing relevant tasks (Becker, 1964). Human capital as argued by Becker (1975) entails education and experience. It examines the variables that entrepreneurs acquire such as education, experience and their effects on business outcomes. The theory explains that a person's level of education is positively related to his or her desire to become an entrepreneur. Schooling positively affects entrepreneurship. The informal self-employed who are mainly school dropouts, earn less than those who are educated.

This explains the desire for educated people to be self-employed more than their less-educated counterparts. The knowledge that is gained from experience and education represents a resource that is heterogeneously distributed across individuals. Kim *et al.* (2003) concluded that human capital factors are positively related to becoming a promising entrepreneur. In Zimbabwe, a significant number of educated people have joined the informal sector. Some people join the informal sector to complement their salaries while others join due to a lack of alternative jobs.

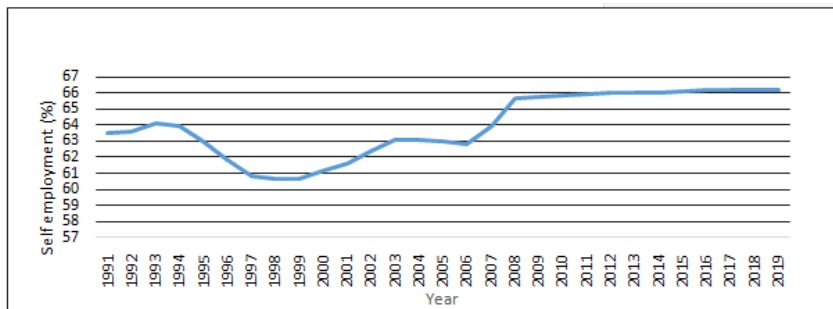
The main proponents of the legalist view are (Feige (1981), Desoto (1989, 2000), Kirshner (2009) and Chen (2012). They argue that as a result of exorbitant, inefficient, cumbersome and costly government rules and regulations, some business people tend to informalise operations because they find it hard to comply with them. These businesses decide to join the informal sector to avoid the burden of high taxes and strict regulations in the formal sector. This theory is also relevant to the understanding of the reasons behind business people in Zimbabwe deciding to take the informal sector route. Most business people in Zimbabwe choose to operate informally to avoid the costly and cumbersome burden of complying with complex government rules and regulations and the accompanying corruption.

## **OVERVIEW OF THE INFORMAL SECTOR IN ZIMBABWE**

The informal sector in Zimbabwe has been growing very fast on the back of declining formal job opportunities and has become the largest employer as the economy is failing to absorb many job seekers. Ndiweni and Verhoeven (2013) estimated that just after Zimbabwe's independence in 1980, a small percentage of 10% of the Zimbabwean workers were employed in the informal sector. The informal sector activities in the country increased during the Economic Structural Adjustment Programme (ESAP) period of 1991-1995 and the economic and political crisis that occurred between 2000 and 2008. Zhou and Pindiriri (2014) argue that more people joined the informal sector during the latter period. Statistically after the collapse of the industry due to the hyperinflation crisis of the 2000s, the informal sector has become the backbone of the economy with almost 5.2-million people operating in the informal sector, 65% of whom are

women. This crisis forced people to demonstrate a high degree of creativity especially in sectors like carpentry, brick-laying, brick moulding and sculpturing.

Due to low skills, many other unemployed people also joined street vending, cross-border trading, and illegal money changing. According to the 2011 Labour Force Survey, 84% of the currently employed population aged 15 years and above are found in the informal sector (ZEPARU, 2014). Mangudya (2017) points out that the sector now comprises over 2.8 million enterprises of different sizes and employs more than 5.7 million people, approximately 4.2 million of these are young people under the age of 35 and the number continues to rise<sup>5</sup>. Figure 1 shows the corresponding developments in informal sector self-employment activities in Zimbabwe from 1991 up to 2019.



**Figure 1: Self-employment 1991-2019 (% total employment)** (International Labour Organisation 2019)

The informal sector contributed on average 61% towards the country's GDP over the period 1991 to 2015, making Zimbabwe's economy one of the largest informal economies in the world (Medina & Schneider, 2018). This shows that informal sector activities in Zimbabwe have grown significantly over time. The hyperinflation that affected the economy between

<sup>5</sup>This is a big jump in both the size of the sector and numbers being employed when compared with the 1990s when they were more than 845000 micro and small scale enterprises employing approximately 1.6 million people. This means that after post ESAP deindustrialization and post 2000 political and economic crisis new entrants in the labour kept on finding solace in the informal sector.

2000 and 2008 led to the dollarization of the economy in 2009. Although the economy made significant improvements in its performance during this period the expansion of informal sector activities was unstoppable. As a result post-2009, the informal activities continued to grow through people engaging in various self-employment activities that increased the sector's contribution to GDP to an average of 66% between 2010 and 2019 (ILO, 2019). This was because the period after 2013 was characterised by many problems such as a rise in inflation, unstable exchange rates, foreign exchange shortages, balance of payments deficit, unsustainable international debt, and electricity shortages. All these adversely affected the various sectors of the economy, thus eliciting the continued growth of the informal sector. To date, Zimbabwe has the largest informal sector in Sub Saharan Africa and is second-largest to Bolivia in the world (Madin and Frierich, IMF, 2018; 23). What the latter tells us is that the informal sector economy is now the real economy of Zimbabwe that has also become the largest employer in the country.<sup>6</sup>

TheFinScope study (2012) shows that the majority of informal sector players are involved in small-scale production with the agriculture sector accounting for 43% driven by growing produce for the fruit and vegetable market. About 9% were into manufacturing, mainly tailoring, carpentry, welding and brick making, whilst 33 % were in the non-tradable service sector and petty trading activities. The latter activities involved the buying and selling of clothes, electronics and other accessories, food, fruits and vegetables, furniture as well as the selling of newspapers and airtime. This is evidenced by the sprouting of flea markets across the country and conversion of former big business premises into small retail business operating space in many cities, towns and growth points in the country. In addition to the aforementioned, other main informal business activities are undertaken, including cross-border trade, retailing, and artisanal mining (LEDRIZ, 2017).

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<sup>6</sup>What is problematic however is the observation that the large numbers being employed in the sector is not a direct result of employment growth within existing business, but it is due to the unceasing daily influx of new entrants or arrivals into the sector. The inference that can be made from this is that informal sector businesses in Zimbabwe are failing to graduate or transition into medium and largescale enterprises with formalized operational structures that the country desperately needs to drive its private sector driven development and innovation agenda.



When it comes to the main participants in the informal business sector, women and youth constitute the majority of the participants. ZEPARU (2014) also found that informal business activities are dominated by female entrepreneurs who account for 50.3% of those currently employed in the informal sector, dominating the wholesale and retail trade and primarily operating from homes and streets. Men tend to dominate the relatively complex and larger activities such as construction, transport, welding and carpentry.<sup>7</sup>

#### *GROWTH AND GRADUATION OF INFORMAL ENTERPRISES: A REVIEW SOME STATISTICAL EVIDENCE*

One of the major arguments espoused for promoting the growth of the informal sector enterprises is that these enterprises serve as the breeding ground or seedbed where medium and large enterprises emerge. The informal sector, therefore, constitutes the entry point and training ground for entrepreneurs and a testing ground for the development of low-cost products. Yet, this can only happen if a strong graduation pattern of micro-enterprises that constitute the majority in this sector, from one size category to another takes place. Research findings, however, show that only a small proportion of informal sector enterprises in Africa including Zimbabwe have ever grown from the micro category of 1-10 workers to the 11-50 workers category, clearly pointing to very weak growth and graduation process of the informal sector enterprises in Africa. The results also show that the proportion of the 1-5 worker category enterprises that reached eleven or more employees is less than the proportion of the 6-10 worker category, that reached sixteen or more employees.

Other micro studies carried out in Rwanda (1988), Botswana (1984), Sierra Leone (1982), the Philippines (1981), India (1987) and Colombia (1987) all emerge with one common result that supports the weak graduation capacity of informal sector enterprises. The microdata showed that modern small and medium enterprises in these countries did not emanate from the micro-enterprises 1-5 worker size category. Instead, in four of the countries studied the majority of the studied enterprises started

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<sup>7</sup> Until recently, the informal transport sector that includes commuter omnibuses operators, pirate taxes and intra and inter-city shuttles popularly known as “mushikashika” was the leading employer of many people including a large number of Zimbabwe’s jobless youths.

with 10 or more workers. The percentage of enterprises with micro or informal sector origins varied widely from 10.7% in Rwanda to 65.6% in India (Liedholm, 1992). The study by Mullei (2003) also confirmed more or less the same results. It found that small enterprises of the informal sector type suffer high mortality rates, remain informal and rarely graduate into high value-adding activities. Many also rarely grow beyond the micro-level of 1-10 workers and hardly transform but remain stunted. To make matters worse the mortality rate is alarming with only a few enterprises surviving a few months to one year.

According to Muriithi (2017: 439-40), the mortality rate of small and micro enterprises among African countries remains very high with 5 out of 7 new businesses dying in their first year. In Uganda, for example, one-third of new business start-ups do not survive beyond one year after their birth. In South Africa, 75% of small businesses die in their infancy hence the country has the highest mortality rate in the world. The expansion of the informal sector in Africa and other many parts of the world thus, mainly takes place through new enterprises' birth rather than by the expansion of employment within existing enterprises. In other words, employment generation by the sector takes the form of the establishment of new enterprises rather than the expansion of existing ones.

A study traced the movement of enterprises through different size categories over time (Moyo *et al.*, 2002). The analysis was restricted to enterprises where there was information on the number of workers at start-up that is five years before the survey and during the survey time-2002 with a specific focus on the movement across sizes between start-up and the time of the survey. The enterprise sizes were categorized as follows: micro1 (1-5 workers), micro2 (6-10 workers), small1 (11-30 workers), and small2 (31-50). The study's findings show that of the 211 enterprises in the study sample drawn from the informal sector, 129 or 61.1 % of all the sampled enterprises either remained stagnant or declined to lower level size categories, whilst 82 or 38.9 % managed to graduate into a higher size category. The breakdown by initial and current firm size categories reveals very informative information as indicated in Table 1.

Whilst 193 of the sampled firms started up as micro-enterprises of Type 1, by the time of the survey only 115 were still in this category. The other 54, 20 and 4 had graduated into micro-enterprises of Type 2 (6-10), small firms of Type 1 (11-30) and small firms of Type 2 (31-50) size categories respectively. Of the 12 firms, that were in the micro-enterprises of Type 2 (6-10) size category at start-up only four of them were still in this category at the time of the survey. An equal number de-graduated into the micro-enterprises of Type 1 (1-5) size category, whilst the other 3 and one graduated into the Type 1 (11-30) and Type 2 (31-50) small firm size categories respectively. Of the 4 firms found in Type 1 (11-30) small firm size category at start-up, 3 remained locked into this category and one of them managed to graduate into the Type 2 small firm size category. However, all the two firms that were at start-up were of Type 2 (31-50) small firms had de-graduated to the Type 1 small firm size category and micro-enterprises Type 1 size category respectively as witnessed in Table 1.

**Table 1:** Number of Graduating and Non-graduating Firms According to Initial Firm Size<sup>8</sup>

Current Firm Size	Initial Firm Size				All Firms
	1-5	6-10	11-30	31-50	
1-5	115	4	0	1	120
6-10	54	4	0	0	58
11-30	20	3	3	1	27
31-50	4	1	1	0	6
All Firms	193	12	4	2	211

*Source:* Moyo *et al.* (2002)

Table 1 shows that the informal sector enterprises in Zimbabwe are characterised by weak growth and graduation processes. Instead, the de-graduation phenomenon is also very prevalent in this sector. Available data also indicates that about 50% of newly-established enterprises in the Zimbabwean informal sector die within their first three to four years of existence (Liedholm and Mead, 1991).

<sup>8</sup>Although this study was carried out some way back, its finding will not change much even if new data is collected at present to replicate the analysis.

## *BARRIERS TO GROWTH AND GRADUATION OF INFORMAL ENTERPRISES IN ZIMBABWE*

Based on the statistical evidence in Table 1, it is clear that the majority of informal sector enterprises rarely grow or graduate into higher enterprise size categories. Several reasons in the case of Zimbabwe are cited in the literature. From a review of the literature survey carried out by International Finance Corporation (IFC) (2018), it is clear that the challenges faced by small enterprises are similar across the world. The survey evidence also shows that the severity of these challenges, however, differ depending on the enterprise's size and its life cycle, that is whether it is at the start-up stage or growing phase. According to the survey start-ups usually report a combination of lack of market demand, access to finance, lack of equipment and competition as their main challenges. Growing enterprises, on the other hand, highlight access to finance and competition and lack of access to skills, technology, labour and burdensome regulations as key barriers to their growth and graduation.

Informal sector enterprises operating in Zimbabwe face more or less similar constraints that limit their growth and expansion prospects. A study carried out by Gombarume and Mavhundutse (2014) in Chitungwiza found out that informal sector businesses in the area were not getting enough financial support from financial institutions. An unstable macroeconomic environment was also found to limit the growth of businesses operating in the sector. Tinarwo (2016) who studied the growth constraints of informal enterprises operating in Gazaland, Harare found that lack of government support, harassment by local authority officials, stiff competition, lack of markets, lack of finance, lack of training or skills and low levels of technology use were some of the major barriers to the sector's growth and expansion. Suppliers mistrust and poor infrastructure were also highlighted as the other factors inhibiting the growth and formalisation of businesses in the sector. The most recent study on the challenges faced by informal sector enterprises is the one by Matsongoni and Mutambara (2021). They studied the challenges of informal small and medium manufacturing enterprises in Zimbabwe's five major cities of Harare, Bulawayo, Gweru, Masvingo and Mutare. The study's findings show that the informal manufacturing businesses face limited access to finance; lack of infrastructure and collateral security;

limited research, development and marketing skills; poor business structures; lack of entrepreneurial and management skills as well as not only strict but a poorly defined legal and regulatory framework that adversely affects the growth and development of these enterprises.

## **CONCLUSION AND POLICY RECOMMENDATIONS**

The literature reviewed in this article shows that in many countries in the developing world, informal businesses do not grow. . The agreed fact is that they tend to remain micro and are of the survivalist type implying that both the growth and expansion prospects of the sector are very limited. In the Zimbabwean case, this is due to many growth-inhibiting challenges faced by these enterprises reviewed. As such, there is a need to continually come up with new measures to support informal sector businesses for them to realise meaningful growth and expansion. For this to happen we recommend the following:

### *IMPROVED ACCESS TO FINANCE*

Both adequate finance and accessing it at affordable interest rates are crucial for informal sector businesses growth and graduation in Zimbabwe. Sufficient finance is mostly needed to secure the requisite tools and machines, buying raw materials, and acquiring the business premises to operate from. This means that both existing public and private financial institutions should strive, via the implementation of innovative lending packages, to avail more financial resources to informal sector businesses at affordable cost.

### *REDUCING THE CUMBERSOME ADMINISTRATIVE AND REGULATORY BURDEN*

According to Fafchamps (1994), the cost curves of most micro and small enterprises of the informal sector type are hump-shaped. This means that most informal sector enterprises have very little incentive to grow or graduate because they face increasing unit costs and therefore, a severe disincentive to increase their investment outlays for growth purposes. Cumbersome compliance costs associated with prohibitive administrative and regulatory burdens contribute disproportionately to these costs. The government should continue implementing its cost of doing business reforms to incentivise informal sector businesses to grow and graduate.

### *TRAINING ON MANAGERIAL AND FINANCIAL SKILLS*

Lack of management skills has been cited several times in empirical reviews. As such lack of or limited management skills is indeed a possible explanation for the lack of growth of informal enterprises in the country and their observed lack of graduation as well. Training should be extended to include both financial and marketing skills. As a consequence, training of informal sector business owners should be done continuously in the areas of business and financial management and sales and marketing.

### *PROVISION OF ADEQUATE INFRASTRUCTURE AND SUPPORT SERVICES*

Central government and local authorities in the country should help to promote informal sector business growth and expansion by undertaking a variety of other actions that include the building of industrial estates or manufacturing shells and providing premises at low rental costs. Government should also enter into public-private partnerships that will result in the development and improvement of the physical infrastructure and business development services available to informal sector businesses. This will ultimately enable these businesses to enhance their competitiveness, growth, expansion and survival opportunities.

### *REALIGNING THE EDUCATION SYSTEM*

The current education model starting from primary level to university needs to be changed or aligned to meet the present needs of the informal sector from a human capital development perspective. The country's education system should be skewed towards producing entrepreneurs with the ability to produce goods and services and to be in a position to form and transform their small businesses into formal small, medium and large enterprises.

### *PROMOTING FORMALISATION*

It has been observed that in comparison with informal enterprises, enterprises that are registered at the start-up stage have better growth prospects. A multi-country study by Mullei (2003) for example found that the impact of registration at the start-up on growth odds was positive for the growth rate of small enterprises in Zimbabwe. Firms that are registered at start-ups are not only more likely to grow but also grow faster. So, registration will put informal enterprises on a firmer growth

and legal footing. This will in turn permit them wider market access; suffer less harassment from public officials; increased access to public services and supplier credit and other financial services that are vital to both their continued growth and survival. The government of Zimbabwe should incentivise informal enterprise owners to register their businesses by reducing the burdensome legal and regulatory framework and complex administrative procedures to positively influence them to decide to formalise their businesses<sup>9</sup>.

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<sup>9</sup> For more details on some of the measures that can be used to incentive informal businesses to formalise see USAID (2005)

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