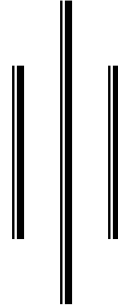


**A STUDY ON PROFIT PLANNING AND CONTROL OF PUBLIC
ENTERPRISES**

(With Reference to Nepal Electricity Authority)

A Thesis



Submitted To

**Office of the Dean
Faculty of Management
Tribhuvan University**



Submitted By

**Kushma Khar Dhakal
Shanker Dev Campus**

T.U. Registration No.: 7-2-39-197-2006

Roll No. : 1696/066

In the Partial Fulfillment of the Requirement for the Degree of

Master's of Business Studies (MBS)

Kathmandu, Nepal

2014

RECOMMENDATION

This is to certify that the Thesis

Submitted by

KUSHMA KHAR DHAKAL

Entitled:

***A STUDY ON PROFIT PLANNING AND CONTROL OF PUBLIC
ENTERPRISES***

(With Reference to Nepal Electricity Authority)

*Has been prepared as approved by this Department in the prescribed format of
the Faculty of Management. This thesis is forwarded for examination.*

.....
Asso. Prof. Prakash Singh Pradhan
(Thesis Supervisor)

.....
Prof. Dr. Kamal Deep Dhakal
(Head of Research Department)

.....
Associate Prof. Prakash Singh Pradhan
(Campus Chief)

.....
Romakant Bhattarai
(Thesis Supervisor)

VIVA-VOCE SHEET

We have conducted the viva-voce of the thesis presented

By

KUSHMA KHAR DHAKAL

Entitled:

A STUDY ON PROFIT PLANNING AND CONTROL OF PUBLIC ENTERPRISES

(With Reference to Nepal Electricity Authority)

And found the thesis to be the original work of the student and written according to the prescribed format. We recommend the thesis to be accepted as partial fulfillment of the requirement for the

Degree of Master's in Business studies (M.B.S.)

Viva-Voce Committee

Head, Research Department
Member (Thesis Supervisor)
Member (Thesis Supervisor)
Member (External Expert)

DECLARATION

I, hereby, declare that the work reported in this thesis entitled “*A Study On Profit Planning And Control Of Public Enterprises (With Reference To Nepal Electricity Authority)*” submitted to office of the Dean, Faculty of Management, Tribhuvan University, is my original work done for the partial fulfillment of the requirement for the Masters of Business Studies (MBS) under the supervision of Asso. Prof. Prakash Singh Pradhan & Romakant Bhattarai of Shanker Dev Campus, Putalisadak, Kathmandu.

.....

KUSHMA KHAR DHAKAL

Researcher

Roll No: 1696/066

Shanker Dev Campus

T.U. Regd. No. 7-2-39-197-2006

Date: - February, 2014

ACKNOWLEDGEMENT

This is an attempt to present thesis entitled “*A Study On Profit Planning And Control Of Public Enterprises (With Reference To Nepal Electricity Authority)*” prepared for partial fulfillment of the requirement for the Degree of Master of Business Studies (MBS) is an outcome of continuous and immeasurable cooperation and support of several hands. I would like to express my heartfelt gratitude to all for their support.

I express my sincere honor and special gratitude to my academic supervisor, Asso. Prof. Prakash Singh & Romakant Bhattarai for their generous guidance, thoughtful encouragement and brilliant insight throughout this research work.

I owe great intellectual debt for support and immense contribution to Administrative of NEA. I am thankful to library staffs of Shanker Dev Campus and T.U. library for their cooperation.

KUSHMA KHAR DHAKAL

Roll No: 1696/066

Shankar Dev Campus

Kathmandu, Nepal

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ABBREVIATIONS

A/C	Account
BEP	Break Even Point
C. V.	Coefficient of Variation
COGS	Cost of Goods Sold
CV	Coefficient of Variation
CVP	Cost Volume Profit
EBIT	Earning Before Interest and Tax
F	Favorable
F.C.	Fixed Cost
FY	Fiscal Year
GWH	Giga Watt per Hour
MBA	Masters' of Business Administration
MBS	Masters' of Business Studies
MOS	Margin of Safety
NEA	Nepal Electricity Authority
NP	Net Profit
P/V	Profit Volume
PPC	Profit Planning & Control
SD	Standard Deviation
SDC	Shankar Dev Campus
T. U.	Tribhuvan University
U	Unfavorable
V.C.	Variable Costs

CHAPTER I

INTRODUCTION

1.1 Background of the Study

Profit is the primary measures of business success. At least, normal profit is necessary for the operations of any kind of organizations. Without profit organization cannot operate its functions. Making profit is not easy because “Profits do not just happen, profits are managed. Profit is a motivating factor behind many managerial activities. Profit is financial reward. Economics theories on profit may be put in three broad categories. The first theory looks upon profit as the reward for bearing risks. The second view, profit as the consequence of friction and imperfection in the competitive adjustment of the economy to dynamic changes. Third sees profit as the reward for successful innovation. A business firm is an organization designed to make profit and profit is the primary measurement of its success. Profit can not be achieved easily. It should be managed well with better managerial skills. So profit is the planned and controlled output of management.

Planning means deciding in advance what to do in future. It is a method of thinking out acts and purpose before hand. Planning is an effective management tool for decision making. It gives direction to the decision makers as well as manager to take the proper decision. Planning is pre-determined course of action for achieving goals or objective effectively at a fluid environment within a certain period through the selection of best alternatives among the various alternatives. On the other hand, it holds accountability and responsibility about result to individual. Planning also states what, where and how things will be accomplished. An adequate planning is necessary for control of operations.

Three major function of management are planning, execution and control and these are the key elements of the management process. Business management must plan to its activities is in advance carryout the plan and institute appropriate technique of observation and reporting to insure that deviation from plans are properly analyzed and handled. In planning the manger fixes the objectives of the organization as a whole and in the light of this, the goals of the various departments of the organization. Then, he proceeds to prepare a kind of blue print mapping out the ways of attaining these objectives naturally then all other functions of the manager depend upon planning. Planning is effective management tool for decision maker as well as manager to take the proper decision.

Control is the process of ensuring that actual activities confirm to plan activities. Control helps in correction. Therefore, planning and controlling are major function of management. Controlling is the measurement and correction of performance in order to make sure that enterprise objective and the plans devised to attain them are accomplished. Control provides timely information that may prompt the revision of goals. The purpose of control is achieved with setting standards comparing predicted and actual results against these standards and taking correctives actions.

Profit, planning and control are an important approach, mainly in profit oriented enterprises. Profit planning is nearly a tool of management, which is used to plan and control business operation and interaction. Profit planning and control is a new term in the literature of business. Though, it is a new term, it is not a new concept in the management. It is also known as comprehensive budgeting. It can be defined as a management planning covering all phase of profit operation for a definite future period. A project planning is a formal expression of policy, plan, objectives and goals established by manager for the concern as a whole as for each sub-division.

Profit planning and control cannot be through as a separate technique. It cannot be operated in dependently of the total management process. It is integration in different managerial approach and technique such as sales forecasting. Production planning and control, inventory control also focus on performance reporting and evaluation of performance to determine the causes of both high and low performance.

The Profit planning and control includes;

- Development and application of board and long-range objectives of the enterprises.
- Specification of enterprise goals.
- Development of a Strategic long-range profit plan detailed by assigned responsibilities.
- Establishment of a system performance report detailed by assigned responsibilities.
- Development of follow up procedure.

1.2 Statement of the problems

Any enterprises need profit to survive and complete in the market. The success or failure of an enterprise is measured on the basis of per unit profit or surplus or productivity improvement. Many PEs have not prepared both long range and short range plans regularly and also the objectives of short range plans have no relation with the long range planning control.

In context of Nepal, NEA functioning in public utility sector it is the basic infrastructures for the development of the nation without it no industrialization of the economy can be imagined. In this context, NEA has great role than other public enterprise as all manufacturing, nonmanufacturing industries and government, depend upon information supplied by it. It is not facing marketing competition and is enjoying almost monopoly over the distribution of services. So this organization is a large scale public enterprise of the country.

Most of the public enterprises of Nepal are in a big crisis. Some of them are liquidated. some are privatized and some PEs are in the process of privatization the first privatization policy was introduced in united kingdom during 1980s and in Nepal it gained momentum after the restoration of multiparty democracy in1990.

NEA is a fully government-owned and government controlled organization. Government is looking toward to privatization of this organization and primary studies are being undertaken. However this organization has been victimized in different political movements. The major problems facing by NEA are as follows.

- Lack of proper execution of plan
- Operating expenses is in increasing trend as compared to increase in its activities.
- Lack of adequate infrastructures.
- Political interference.

The present study intends to analyze and examine the Profit planning and control of NEA. Furthermore the study tries to answer following questions.

- What are the major problems and issues relating to development and implementation of profit plan?
- To what extent is the process of budgeting being followed by NEA in developing and implementing profit plans?
- What is the situation of budgeted and actual activities?
- Whether the financial performance is sound or not?
- What step should be taken to improve budgeting system and profitability in this Organization?

1.3 Objectives of the study

This study is an attempt to draw a vital conclusion about NEA regarding its economic capability, operating efficiency and the financial positions. This organization is a large-scale public enterprise, which is one of the basic infrastructures for the development of the nation. Without the help of this corporation, industrialization seems to be impossible. The primary objective of this study is to assess the application of comprehensive profit planning and control or budgeting system in NEA with the following specific objectives.

- To analysis the various budget activities adopted by NEA.
- To assess the financial performance of NEA by using BEP analysis and ratio analysis.
- To forecast future sales and profit trend of NEA.
- To examine the practice and effectiveness of profit planning in NEA.

1.4 Need & Significance of the study

In every organization, the availability of the resources is scarce and out of these scarce resources, the objectives of the organization are to be accomplished. The financial performance of the organization depends upon the uses of its resources. PEs are getting loss day by day due to under utilization of available resources. As a result, most of the PEs has bad financial performance. Profit planning process is not applied in the real sense in Nepalese PEs.

- The main reason to study this research work is to analyze and examine the profit planning system of the organization whether it is applying profit planning system of the properly or not.
- It also tries to analyze and examine the practice of preparing various functional budget of NEA. Finding some problems faced by corporation, while developing and implementing the functional budget and to

recommend some measure to improve profit-planning system as well as cost recovery system of corporation.

- Budgeting is the key to the productive financial planning, so, all organizations running under commercial principle have to give emphasis in regard to this most important single tool while managing their physical and financial targets.
- Various function budgets are the tools for proper profit planning and control. This study is intended to analyses and examines the budgetary practices used in NEA.
- This study is concise, practical, usable and valuable to the major parties interested in the budgetary practice and profit planning and control. It will also be useful and beneficial to organizations, Nepal Government and other interested parties and stakeholders.

1.5 Limitations of the study

Following factors have limited the scope of this study.

- The study covers a period of 5 years since 2065/66 to 2069/70 on the basis of historical records as provided.
- The comprehensive and accuracy of the study is based on the data available from the management of both organizations and other sources.
- As the data used are mainly secondary in nature, there may be the chances of error in such data.
- This study is concentrated in accounting and financial aspects only.

1.6 Organization of the Study

This study is divided into five separate chapters.

Chapter I- Introduction

This chapter contains the brief introduction of the subject matter i.e. background of the study, statement of the problem, objectives of the study need & Significance of the study, limitation of the study & Organization of the study.

Chapter – II: Conceptual Framework & Review of Literature

The second chapter includes pilot studies and textual concepts with regard to conceptual framework on Budgeting, Profit Planning along with the review of major books, journal, research work and previous theses.

Chapter – III: Research Methodology

The third chapter includes research design, population & sample, sources and types of data, data processing technique and method & tools of data analysis.

Chapter – IV: Presentation & Analysis of Data

The fourth chapter deals with the presentation and analysis of data. It analyzed the data and interprets the results using different accounting and statistical tools, table, chart and graphs. It also includes major findings of the study.

Chapter – V: Summary, Conclusion & Recommendation

This chapter contains Summery, Conclusions and Recommendation. This chapter briefly represents the summery of the whole study and the conclusions and the recommendations for the effective and smooth running of the NEA under the study.

Besides these, bibliography and annexure are presented at the end of the thesis. Similarly acknowledgements, table of contents, list of tables, list of figures, abbreviations are included in the front part of the thesis report.

CHAPTER II

CONCEPTUAL FRAMEWORK AND REVIEW OF LITERATURE

This chapter is concerned with review of literature relevant to the topic Profit planning and control of NEA. The purpose of reviewing of literature is to develop some expertise in one's area, to see what new contribution has made and to receive some ideas for developing a research design. Thus, previous studies cannot be ignoring as they provide the foundation of the present study. This chapter highlights the literature that is available in concerned subject as to my knowledge, research work, and relevant study on this topic, review of journals and articles and review of thesis work performed previously.

2.1 Conceptual Framework

2.2 Review of Previous Study

2.2.1 Review of Journal/Articles

2.2.1 Review of Thesis

2.3 Research Gap

Research gap refers to the gap between previous research and this research. Many research studies have been conducted by the different students, experts and researcher about profit planning and control. There is gap between the present research and the previous researchers. The findings of the previous researches were mostly based on actual and budgeted figure. Most of the previous researches did not disclose the financial position. Thus to fill up those gap the current research is conducted. This research study is based on using current data which are not included in previous studies. This study aims to access the profit system of NEA. This study tried to indicate the role of profit planning to increase its profit. This study attempts to analyze the financial position of the NEA by using various statistical and financial tools. It also concludes the various findings of the research and recommendation for

immediate and long term improvement and corrections. So, this study will be fruitful to those interested person, parties, scholar, civil society, general public, businessmen and government for academically as well as policy prospective.

CHAPTER III

RESEARCH METHODOLOGY

Research methodology is the way to solve systematically about the research problem. Research methodology is a general plan of how the researcher is going about answering the research questions that has set. The research worked undertaken following a systematic way, which is called the research methodology. This chapter describes the research methodology or research strategy employed in this study. The major contents of research methodology are as follows.

3.1 Research Design

Research design is the plan, structure, and strategy of investigation conceived to obtain answers to research questions. Generally, research refers to definite procedures and techniques, which guide to study and propounds ways for research viability. Both analytical as well as descriptive design has been applied design for this study, this study is closely related with the various areas of sales, production and other related statement.

3.2 Populations and Sample

This research aims to studying Profit planning & control of NEA. In now days, there are thirty-six public enterprises operating in Nepal so the all thirty-six public enterprises are population of the study out of them NEA is selected for the study purpose therefore the NEA is the sample of the study. Sample of the study is selected on the basis of judgmental sampling method.

3.3 Nature and Sources of Data

This study is based on secondary data. However, primary data and information have been obtained through informal discussions with the executives and other related staffs of the NEA. The secondary data are collected from annual reports of NEA, balance sheet, profit and loss A/C, cost detail sheet, previous thesis and other relevant published and unpublished documents of NEA.

3.4 Research Variables

The research variables of this study is mainly sales, production, profit and loss, capacity utilization, manpower, capital expenditure, breakeven point, profit volume ratio, margin of safety, flexible budget and cash flows related to short term and long term periods of NEA.

3.5 Period Covered

The present study covers two times dimensions long range and short range. The time period of five years for the purpose of trend analysis for long planning and the time period of one year (current year) for the purpose of short range planning are taken. Data are collected from fiscal year 2065/066 to 2069/070 for analysis.

3.6 Data Analysis Tools

The collected data from various sources are managed to analyze and presented in proper tables, formats and graphs such as table and formats are interpreted and explained wherever necessary. To analyze the collected data financial and statistical tools are used. In statistical tools, mean, standard deviation, coefficient of variation, correlation coefficient, coefficient of determination, probable error of correlation, regression equation, time series analysis, graphs and diagrams are taken, whereas in financial tools ratio analysis, BEP analysis are used.

3.6.1 Statistical Tools

3.6.1.1 Arithmetic Mean or Average

3.6.1.2 Standard Deviation

3.6.1.3 Regression Analysis

3.6.1.4 Correlation Coefficient

3.6.1.5 Coefficient of Variation

3.6.1.6 Least Square Linear Trend Analysis

3.6.1.7 Assessment of the Sample Correlation Coefficient (t-test)

3.6.2 Accounting Tools

3.6.2.1 Percentage Change

3.6.2.2 Contribution Margin

3.6.2.3 Profit Volume Ratio

3.6.2.4 Break Even Point

3.6.2.5 Margin of Safety (MOS)

CHAPTER IV

PRESENTATION AND ANALYSIS OF DATA

Profit planning is used for development and acceptance of proper objectives and goals for an organization. A profit plan is a comprehensive and coordinated plan of an enterprise for some specific period in future. Planning is carried out to fulfill the responsibility of forward thinking and future operation of the organization. To meet the objectives, the researcher has tried to present and interpret the collected data in systematic manner and presented and tabulated in meaningful ways. For that purpose sales plan, cost, profit, contribution margin, Break-even analysis, income statement, sensitivity test etc. are done, which are the major variables of PPC analysis.

- 4.1 Sales Plan & Control of NEA
- 4.2 Production Plan of NEA
- 4.3 Comparative Analysis of Actual Production & Sales
- 4.4 Cost of Sales Plan of NEA
- 4.5 Operating Expenses Plan of NEA
- 4.6 Operating Profit Plan of NEA
- 4.7 Net Profit/loss Plan of NEA
- 4.8 Plan for Number of Consumers of NEA
- 4.9 Regression Analysis
- 4.10 Cost – Volume - Profit Analysis
- 4.11 Major Findings of the Study

- All the fiscal year sales targets are achieved up to only 92% level still the achievement level have been increased to 100.05% in the year 2012/013.
- The average budgeted and actual sales of NEA are Rs. 17426.45 & Rs. 16929.48 and the achievement of sales during the five year study period is 96.92%. There is positive correlation of 0.9922 between budgeted and actual sales of NEA.
- All the fiscal year sales unit targets are achieved up to 95% level still the achievement level have been increased to 100.09% in the year 2012/2013.
- The average budgeted and actual sales units of NEA are 2610.38 GWH & 2577.75 GWH and the achievement of sales unit during the five year study period is 98.68%. There is positive correlation of 0.9978 between budgeted and actual sales unit of NEA.
- The average budgeted and actual production units of NEA are 3608.51GWH & 3612.33 GWH and the achievement of production unit during the five year study period is 100.11%. There is positive relationship between budgeted and actual production.

- The actual sale is more than 70% of total production in each fiscal year. The average production and sales units of NEA are 3612.33 GWH & 2577.75 GWH similarly and the proportion of sales on total production unit during the five year study period is 71.33%.
- The average budgeted and actual costs of sales of NEA are Rs. 12007.98 & Rs. 11804.91 million and the coefficients of variation are 18.62% & 17.38% these figures shows high fluctuation in budgeted cost rather than actual cost.
- The average budgeted and actual operating costs of NEA are Rs. 6266.09 & Rs. 6487.72 million and the coefficients of variation are 17.68% & 18.92% these figures shows high fluctuation in actual operating cost rather than budgeted operating cost.
- The average budgeted and actual operating profits/losses of NEA are Rs. -2.56 million & Rs. 252.65 million. The result of correlation coefficient is positive correlation of 0.8252 between actual and budgeted operating profit/loss of NEA.
- The budgeted & actual average net losses of NEA are Rs. 6110.34 & Rs. 5588.04 million and the coefficient of variation are 44.43% & 37.99% these figures shows high fluctuation in budgeted net loss rather than actual net losses.
- The budgeted and actual numbers of consumers of organization are not fluctuated. In the all fiscal year targets are achieved more than 100%.
- From the regression analysis, it is seen that the actual sales of NEA in the fiscal year 2013/014 will be Rs. 25749.99 million, cost of sales Rs. 15612.99 million, operating cost Rs. 9200.54 million, operating profit Rs. 1745.76 million, net loss Rs. 4343.86 million, total production 4260.45 GWH & total sales will be 3159.25 GWH.
- It is found that NEA is operating below BEP since BFP sales is less than actual sales during the study period and NEA has the negative margin of safety in each fiscal year during the study period.

CHAPTER – V

SUMMARY, CONCLUSION & RECOMMENDATIONS

This is the final chapter of this research study, which has been divided into summary, conclusion and recommendations. In this chapter, the researcher examine the processed data to come into new concluding upon the PPC analysis of NEA. It also aims to give forth some suggestion that must be helpful for further enhancement of the operation of NEA.

5.1 Summary

Every business organization set up with certain objective of providing services to people and earns profit as income whether that is productive or non-productive. But it is not a joke to fulfill that objective easily in this competitive world of business. As globalization take place it became tougher to sustain in market. So, they not only just try and see the result also do hard work and provide many facilities to secure from loss. Hence they need to think about future course of action in such a way so hat they can accomplish their business objectives. In order to make profit it is necessary to check business capacity, activities, utilization of resources and if there is any part to reduce cast because little reduction in expenses can make profit in income. Hence, profit planning tools helps to assist in analyzing the situation. Therefore, proper planning & controlling is important to survive & lead the company successfully. Organization cannot achieve its goal without proper planning and implementation.

Nepal still belongs to the groups of the least development country. Due to recession, the economic growth is not increasing. Political instability, strikes, bandas, shortage of fuel, food, raw material, insecurity of public, higher rate of transportation, power cut of electricity, labor hike, higher rate of wages etc largely impact negatively in the development of industries.

Profit planning is the planning of activities in such way that it helps in increasing the income at a minimum possible cost or at optimum cost. PPC can be used an effective remedy for the organization running in loss and maintain same or high level profit. It is combination of various financial and physical techniques, which not only helps on increasing profit but also to reduce unnecessary cost and utilize the expenses in the best manner. This study aims at examining the application of profit planning in NEA.

This study has tried to cover the various aspects of profit planning in NEA from the time of fiscal year 2008/09 to the end of fiscal year 2012/013. In the first introductory chapter, this study has tried to give brief introduction, brief profile of NEA, statement of the problem, objective of the study , limitation of the study, significance of the study and organization of the study. During the research works an extensive review of various literatures, books, past thesis, journals have been made and internet materials from relevant websites were also consulted. The work was compiled into “review of literature” chapter. Research methodology followed for this research work is mentioned in the chapter three entitled as “Research Methodology”. Likewise, Data relating to various activities of the NEA has been collected, presented in tabular and various diagram form and are tired to be interpreted in the study report in logical ways. Data are then analyzed applying various financial, mathematical and statistical tools have been listed in a systematic manner. All these works are compiled in the fourth chapter titled as “Data Presentation and Analysis” of the study. Finally, the summary, conclusions and the recommendation are made for this study is hereby being presented in this chapter five titled as “Summary, Conclusion and Recommendation”.

5.2 Conclusion

Different types of profit planning tools, which are used in the academic field and in multinational companies of developed nation are not applied by NEA. NEA has not segregating cost into fixed and variable. Segregation of cost into

fixed and variable is the fundamentals of PPC analysis. The company did not adopt the cost control programme. The accumulation and apportionment of cost on the basis of cost center is not done by the company. Therefore, NEA has not been able to use PPC properly.

Sales revenue of NEA is increasing in a fluctuating trend. NEA is not producing sufficient electricity. Profit pattern of the company shows that the company is ineffective in profit planning. The cost structure of NEA discloses variable cost and fixed cost which indicates the risk due to high variable cost. CVP analysis shows that the contribution margin did not cover the fixed cost. BEP of the company is greater than actual sales due to a low PV ratio. The business of the company is in high operating risk due to higher break-even sales.

The plans are prepared from the top level and later it is communicated to the lower level. There is a lack of authorities to formulate various plans in lower level management. Company has not analyzed its strengths and weaknesses. NEA has not been able to utilize its capacity in optimum level, very high cost on large projects are another problem of NEA. Most of the public enterprises created financial burden to the government. To run NEA properly controlling of cost and participative management are essential. NEA has practice to make planning for each activity like sales, production, cost of sales, operating profit, net profit but the overall profit planning activities are not more effective.

5.3 Recommendations

On the basis of above study, the following recommendation seems to be fruitful to the management of NEA.

- NEA has not practiced CVP analysis. So it is suggested that NEA should practice CVP analysis and cost volume profit relationship should be considered while formulating profit plan.

- Classification of cost into variable and fixed as well as controllable and non-controllable must be made within specific framework of responsibility center and time.
- Cost plan of NEA are not systematically maintained. Separate cost control department need to be established to control cost.
- Sales revenue of NEA is in increasing trend but it is not sufficient to cover the cost and earn profit.
- Price rising is not only one alternative to increase sales revenue controlling is necessary to decrease the wasteful expenses. NEA should adopt the controlling tools.
- PPC manuals should be communicated from top to lower levels. All personnel should be participated on decision making and planning process.
- Systematic and periodicals performance reports should be strictly followed to trace poor performance and take corrective action immediately and timely.
- NEA should reduce variable cost and fixed cost as well as increase sales revenue to generate profit. This also helps in reducing break-even sales.

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